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Corporate Reorganizations

Top Tax Lawmakers Counter IRS 10-Year REIT-Conversion Proposal

IRS rules that require a 10-year built-in gain recognition period for real estate investment trusts and regulated investment companies don't match congressional intent, the top members on the Senate Finance and House Ways and Means committees said.

Temporary rules (T.D. 9770) released in June say that assets moved from a corporation to a REIT or a RIC within 10 years of a spinoff will be taxed as though the corporations sold the assets at fair market value. The conversion period should be five years, to be consistent with the built-in gain recognition period for S corporations, the lawmakers said in an Oct. 18 letter.

"We ask the regulations be modified to provide that REITs, RICs and S corporations are all subject to the same five-year built-in recognition period in order to be consistent with congressional intent and longstanding practice," the letter said.

The letter, to Treasury Department Secretary Jacob J. Lew, was signed by Finance Chairman Orrin G. Hatch (R-Utah), ranking member Ron Wyden (D-Ore.), Ways and Means Chairman Kevin Brady (R-Texas) and ranking member Sander M. Levin (D-Mich).

The letter is likely to add credibility to the REIT industry's desire to subject REITs and RICs to the same

conversion periods as S corporations. The National Association of Real Estate Investment Trusts opposes the regulations and has asked the Internal Revenue Service to withdraw and repropose the rules.

Congressional Clarity. Congressional intent is really important to the IRS, Richard C. LaFalce, a partner at Morgan, Lewis & Bockius LLP, said. But there wasn't much disagreement about what Congress meant when it passed the Protecting Americans from Tax Hikes Act, he said.

"It almost seems as though the IRS was aware of this and then came out with the 10-year rule anyway," LaFalce told Bloomberg BNA.

The rules address what the IRS saw as a hole in the PATH Act language that restricted corporations from spinning off real estate assets into a REIT tax-free.

The IRS has scheduled a hearing on the rules for Nov. 9. Outlines are due by Oct. 26 from those who wish to speak at the hearing.

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Text of the lawmakers' letter is at <http://src.bna.com/jrF>.