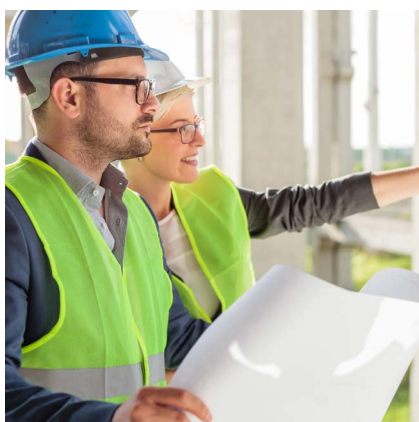


Creative Trust Planning for Real Estate Developers

Learn about tax-advantaged trust strategies under today's tax laws



Key takeaways

- Tax Legislation passed in 2025 includes many significant tax provisions for business owners, including real estate businesses, that should be considered
- Planning for the ultimate continuation or sale of your business is as important as growing your business
- From a strategic planning perspective, real estate developers may want to consider targeted trust strategies

As a real estate developer, you may be in a favorable income tax position because of the nature of your business and the assets you employ in that business. Assets such as depreciable buildings, depreciable construction machinery and equipment, as well as other business assets, may provide income tax deductions that effectively shelter much of your income. These income tax benefits may be realized by you as a sole proprietor of your development business or as an owner of various pass-through entities, such as partnerships or limited liability companies that hold your real estate development assets.

Let's take a look at today's current tax laws and then we'll explore some specific strategic planning opportunities using trusts that may be of value to real estate developers.

Section 199A

Under current law, there is a deduction for non-corporate taxpayers under Internal Revenue Code (IRC) section 199A. The section applies to income earned through partnerships, S corporations, limited liability companies (LLCs) taxed as partnerships, and sole proprietorships, and provides a deduction of up to 20% of qualified business income (QBI). The definition of QBI can be rather complex, but for the real estate industry, it includes income from real estate development, leasing, and operations. QBI does not, however, include capital gains income, which is important for real estate developers, since this means the QBI calculation may not include gains from the sale of real estate. Importantly, this provision was made permanent in 2025.

A deduction limitation feature within section 199A for business owners such as those in real estate involves income thresholds that may phase-out or eliminate a current year's deduction. The limitation calculation is complex and beyond the scope of this article, so this is an area where working with your qualified tax and accounting professional is crucial.



Interest deduction limits

Businesses may choose to use loans or lines of credit to fund business operation expenses or for expansion purposes. The interest paid or accrued on these, although not the principal, may be deductible similar to other operating expenses subject to certain limitations, under IRC section 163(j).

For S corporations, partnerships, and LLCs treated as partnerships, the interest limitation applies at the partnership level. Any deduction not allowed for a taxable year may be carried forward indefinitely.

It's important to note that the One Big Beautiful Bill Act (OBBBA), passed in July 2025, redefined Adjusted Taxable Income, or ATI. From 2021, under prior legislation, ATI would be computed based on the accounting concept of Earnings Before Interest and Taxes (EBIT). Now, ATI is computed based on Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA). There is no expiration to this definition of ATI. Effectively, this allows for the opportunity of greater business interest expense deductions as the 30% threshold is applied to a higher number.

It is important to note that this limitation does not apply to interest incurred by the taxpayer in any real property development, redevelopment, construction, acquisition, rental, operation, management, or leasing if the taxpayer makes an election, or certain financial thresholds.

Enhanced cost recovery provisions

Cost recovery is the process by which businesses deduct the cost of capital assets, such as equipment, buildings or intangible assets, over time. Enhanced cost recovery is a tax or accounting method to allow a business to recover the cost of investment more quickly than the normal standard.

The OBBBA permanently extended and modified additional first year depreciation deduction and increased the bonus depreciation allowance to 100% of property acquired and placed in service on or after January 19, 2025.

New incentive for qualified production property (QPP)

The OBBBA introduced a temporary 100% first-year depreciation allowance for qualified production property (QPP), which generally includes tangible personal property with a useful life of 20 years or less, as well as qualified improvement property (QIP). This is the portion of nonresidential real property used in qualified production activities. This applies if construction began after January 19, 2025, and before January 1, 2029, and the property is placed in service before January 1, 2031.

As these measures are complicated and require coordination with a business's other tax considerations it is optimal to consult with a tax professional for best tax determinations when many tax provisions may interact.



In addition, IRC section 179 allows businesses to expense the entire cost in the year it is put into service, instead of depreciating over its useful life. The OBBBA increased the maximum section 179 deduction amount for small businesses to \$2.5 million, with the phase-out threshold amount raised to \$4 million. These changes are effective for property placed in service in taxable years beginning after December 31, 2024.

This is of particular interest to real estate developers because the definition of section 179 property includes certain depreciable tangible personal property used primarily to furnish lodgings as well as to include improvements made to nonresidential real property, such as roofs, heating, ventilation, air conditioning, fire protection, and alarm and security systems. It's important to understand that you must have net income to take section 179 expensing, and cannot create a loss by using it.

Exchanges of real property still allowed

IRC section 1031 is referred to as the like-kind exchanges rule and was put in place to encourage ongoing investment in real estate by delaying the payment of taxes until a piece of property is eventually sold. By exchanging one piece of property for another, the taxpayer may carry over the basis, effectively carrying over the gain from the old parcel into the newly acquired one. This rollover of tax basis continues indefinitely until the taxpayer disposes of a piece of real estate without replacing it. At that time the taxpayer will recognize a gain on the disposition. These types of exchanges continue to be allowed.

An important caveat is that real estate held primarily for sale to customers is not eligible, which may affect condo developers. Additionally, any portion of the real estate that includes personal property may no longer get like-kind treatment.

Wealth Transfer Taxes

Wealth transfer taxes are a group of taxes levied on the transfer of assets from one individual to another either during life or at death. Beginning January 1, 2016, the OBBBA increased the estate, gift, and generation-skipping transfer (GST) tax exemption to \$15 million per person and \$30 million for married couples. This is a permanent increase and will be adjusted annually for inflation.

Trust strategies to consider in light of current tax laws

- Implementing Delaware dynasty trusts to capture large potential growth outside of your estate
- Funding irrevocable life insurance trusts to provide liquidity
- Utilizing multiple irrevocable non-grantor trusts to maximize use of the section 199A deduction
- Utilizing new like-kind exchange rules within trusts
- Decanting current trusts to provide more flexibility for tax basis management
- Taking advantage of today's high federal exemption to fund or add to trusts

With the many changes and opportunities available under today's tax laws, it's important to consult with your advisory team to be certain your real estate investments and your personal wealth plan are working in an integrated and advantageous way.



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Note that estate planning strategies require individual consideration, and there is no assurance that any investment, financial, or investment strategy will be successful.

Note that a few states, including Delaware, have special trust advantages that may not be available under the laws of your state of residence, including asset protection trusts and directed trusts.

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