

# National Association of REALTORS® Issue Brief

## Commercial Real Estate

Fall 2018

**1031 LIKE KIND EXCHANGES:** In December 2017, Congress passed and the President signed into law H.R. 1, the Tax Cuts and Jobs Act. The law made dramatic changes to the U.S. tax code, many of which impact real estate. A chief concern was that tax reform would repeal or limit like-kind exchanges under Section 1031; while the law repealed 1031s for personal property, it specifically retained them for real property.

**NAR ACTION:** NAR participates in multiple coalitions to protect Section 1031 from repeal or limitation. As part of the “1031 Like-Kind Exchange Coalition,” which includes non-real estate industry groups, NAR commissioned a study from Ernst & Young on the macroeconomic effects of repealing Section 1031. As part of the “Real Estate 1031 Like-Kind Exchange Coalition,” made up solely of real estate groups, NAR commissioned a study focusing on the 1031s and their economic impact on real estate. NAR participated in meetings with key members of Congress (including leadership and the tax writing committees) as well as press events in support of Section 1031. Retaining Section 1031 was a talking point at the Spring 2017 Hill visits, and NAR continually stressed its importance in letters on tax reform to the Hill.

**ADA SUIT NOTICE REQUIREMENT:** The Americans with Disabilities Act (ADA) lacks a notice requirement, leaving commercial property owners who in good faith believe their properties comply with the law vulnerable to lawsuits. Under the ADA attorneys may collect fees relating to pursuing claims of noncompliance, while plaintiffs cannot collect damages. Once a suit is filed, there is not opportunity to cure the infraction, so property owners spend time and money on attorneys and fees which could be used to fix the issue. In recent years, “drive-by” ADA suits, by attorneys targeting commercial properties with small, easily-correctible infractions, have been on the rise.

**NAR ACTION:** NAR participates in a coalition advocating for reforms to the ADA to curb “drive-by” suits, including adding a notice provision to give property owners the opportunity to correct infractions before a suit is filed, encouraging swift compliance with the ADA instead of lawsuits. NAR supported H.R. 620, the ADA Education and Reform Act, a bipartisan bill sponsored by Rep. Poe (R-TX), which would accomplish those goals; it passed the House in February 2018, but has not found support in the Senate. NAR is now working with the Senate to find a solution to this issue.

**BASEL III:** The Basel Committee created a new risk-weight regime (“Basel III”) for High Volatility Commercial Real Estate (HVCRE), which includes commercial acquisition, development, and construction loans, and raised their risk-weight from 100 – 150%. This negatively impacted credit availability for commercial real estate and increased the lending standards above what federal regulators already required. In response, Congress introduced legislation to clarify the rule and the federal banking agencies proposed a rule to decrease the risk-weight for these loans while broadening the number of loans included.

**NAR ACTION:** NAR sent two comment letters to the banking agencies in 2017 on the proposed HVADC rule, and submitted letters for Congressional hearings in the House Financial Services and Small Business Committees stressing the burden that overly-broad regulations for lending institutions have on commercial real estate. Ultimately, Congress passed legislation clarifying and simplifying the requirements under the HVCRE rule. H.R. 2148, the “Clarifying Commercial Real Estate Loans,” was sponsored by Rep. Pittenger (R-NC) and passed the House in the fall 2017. A companion bill – S. 2405 – was introduced in the Senate by Sens. Cotton (R-AR) and Jones (D-AL); it was included in S. 2155, a regulatory relief package, which passed both chambers of Congress and was signed into law in the Spring 2018. The law clarifies definitions and exemptions in the HVCRE rule. NAR strongly supported the legislation and advocated in Congress for its passage. Now the federal banking agencies are considering a rule to conform the federal regulations to the new law (which is already in effect).

**CARRIED INTEREST:** It is a common practice among real estate partnerships to permit a general partner (who contributes expertise, and occasionally some capital) to receive some of the profits through a “carried interest,” even when the general partner has contributed little or no capital to the enterprise. The general partner’s profits interest is “carried” with the property until it is sold; in most cases, the general partner then receives the value of any carried interest as capital gains income (which is lower than ordinary income). Capital gains treatment for income from a carried interest is seen as a reward for entrepreneurs who take the risks inherent in new projects and in making capital investments. Capital gains treatment of carried interests also mitigates the impact of inflation on a long-term investment.

**NAR ACTION:** NAR opposes any proposal that would eliminate capital gains treatment for any carried interest of a real estate partnership. In the Tax Cuts and Jobs Act, passed into law in December 2017, retained carried interest but requires a three-year <sup>COMMERCIAL</sup> holding period to qualify for capital gains treatment.

**CREDIT UNION LENDING:** The National Credit Union Administration (NCUA) enacted a rule that would eliminate restrictions on credit unions making member business loans (MBL). The rule gives credit unions more autonomy in creating commercial lending policies unique to each credit union. The rule created a new treatment for construction and development loans. The rule went into effect on January 1, 2017. The NCUA also adopted new rules expanding the field of membership for credit unions.

**NAR ACTION:** *NAR wrote a letter in support of MBL rule change, highlighting the important role of credit unions in commercial real estate lending and the success of small businesses. These rule changes will help expand credit unions as a source of lending.*

**DODD-FRANK LAW:** Implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act continues. Members of the Republican-controlled House of Representatives and within the Trump Administration have stated that want to repeal Dodd-Frank entirely, and in April 2017 House Financial Services Committee Chairman Rep. Hensarling (R-TX) reintroduced H.R. 10, the Financial CHOICE Act, which repeals many sections of Dodd-Frank as well as other regulations of financial institutions.

**NAR ACTION:** *NAR is closely following all rule-making surrounding Dodd-Frank, and submits comments to the relevant federal agencies on topics affecting commercial real estate whenever possible. NAR has also weighed in on various Congressional Hearings on the topic of financial regulatory reform, stressing the importance of common-sense regulations that are well-tailored to the problems they are meant to address. NAR will continue to monitor bills in the 115<sup>th</sup> Congress that roll back or otherwise amend the law.*

**EB-5 PROGRAM:** EB-5 Regional Centers help identify American business needs in the community and help direct foreign investor funds to those projects. In return for investing and creating American jobs, these foreign investors are eligible for visas that allow them to live in the United States. The Regional Centers began as a pilot program in 1992, but have been extended several times.

**NAR ACTION:** *NAR has sent several letters to Congress as well as to the Director of the U.S. Citizenship and Immigration Services in support of the permanent authorization of the EB-5 Regional Center program. NAR is part of a real estate industry coalition supporting the program, and has sent multiple coalition letters to lawmakers urging its reauthorization. Congress has extended the EB-5 Visa Program multiple times via the budget extensions, and it is currently set to expire December 7, 2018. NAR will continue to monitor this issue in the 115<sup>th</sup> Congress and advocate for permanent reauthorization of the EB-5 Regional Center pilot program.*

**ENERGY DEDUCTION 179D:** The Section 179D deduction in the Internal Revenue Code encourages greater energy efficiency in commercial and larger multifamily buildings, by allowing for cost recovery of energy efficient windows, roofs, lighting, and heating and cooling systems meeting certain energy savings performance targets. Congress retroactively extended 179D through the end of 2017 in February 2018 as part of a larger extenders package in the budget compromise.

**NAR ACTION:** *NAR supports the extension and enhancement of the 179D deduction by providing a sliding scale of incentives that correlate to actual and verifiable improvements in a retrofitted building's energy performance. NAR is part of the "179D Coalition," made up of supportive industry groups, and will continue to monitor and advocate for the long-term reauthorization of this deduction in the 115<sup>th</sup> Congress. NAR continues to stress to the Congressional tax-writing committees the importance of this provision and its benefits to commercial real estate.*

**FEDERALLY SUPPORTED COMMERCIAL APPRAISALS:** The Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Board of Governors of the Federal Reserve System (collectively the Federal Banking Agencies) issued a proposal to increase the appraisal threshold for commercial real estate Federally Related Transactions from \$250,000 to \$400,000. In April 2018, the agencies announced the final rule, which raises the appraisal threshold for CRE transactions up to \$500,000.

**NAR ACTION:** *NAR submitted a comment letter to the agencies in support of this change.*

**THE JUMPSTART OUR BUSINESS STARTUPS (JOBS) ACT OF 2012:** The final elements of the JOBS Act, addressing small company capital formation and crowdfunding, are in effect. The rules update and expand Regulation A, an existing exemption from registration for smaller issuers of securities, enabling smaller companies to offer and sell up to \$50 million of securities in a 12-month period, subject to eligibility, disclosure and reporting requirements. Title III regulates crowdfunding platforms and defines unaccredited investors and how they can participate in crowdfunded projects.

**NAR ACTION:** *NAR supports regulation easing restrictions on businesses' ability to raise capital, and increasing liquidity in the commercial*

real estate market. NAR has expressed support to Congress for the potential that crowdfunding has to increase capital in commercial real estate markets. NAR will continue this work in the 115<sup>th</sup> Congress, as well as participate in meetings with the SEC and its committees.

**MARKETPLACE FAIRNESS:** Online retailers are not required under federal law to collect and remit sales tax the same way “brick-and-mortar” stores – clients of commercial real estate practitioners – are. As a result, consumers may be able to purchase goods online for a seemingly lower price due to not paying state sales tax (they are supposed to remit it on their state tax filings each year, but the vast majority do not), which creates a disparity between physical and online retailers. In 1992, a Supreme Court case ruled that Congress had to grant authority to the states to require remote sellers to charge and remit sales tax unless they had a physical presence within the state. Since then, bills were introduced in Congress to do that, but none passed into law. In 2017, the Supreme Court heard the case of *South Dakota v. Wayfair, Inc.*, about a South Dakota law requiring some remote sellers to collect and remit sales tax; overturning its previous ruling, the Court held that the law could stand, recognizing the changed landscape since their 1992 ruling. This opens the door for states to pass similar laws, and will aid in leveling the playing field between online and brick-and-mortar retailers.

**NAR ACTION:** NAR joined two amicus briefs to the Supreme Court supporting the position the Court ultimately ruled in favor of in *South Dakota v. Wayfair, Inc.* In addition, NAR is a member of the Marketplace Fairness Coalition, which advocates for internet sales tax fairness legislation. In the 115<sup>th</sup> Congress, NAR supported two such bills. S. 976, the Marketplace Fairness Act (sponsored by Sens. Enzi (R-WY) and Alexander (R-TN)) and H.R. 2193, “The Remote Transactions Parity Act,” (sponsored by Rep. Moen (R-SD) and Womack (R-AR)). NAR will continue to monitor the changing landscape of this issue post-Wayfair, to support legislation advancing sales tax parity, and to oppose legislation that harms brick-and-mortar commerce in favor of online retailers.

**MARKETPLACE LENDING:** The Department of Treasury issued a report in May 2016 on marketplace lending, i.e. online lending such as social finance, crowdfunding, or peer-to-peer lending. The report highlighted the role that these lenders play in the economy, but also expressed concern for the overlapping regulations governing these entities, and the loopholes they create. The Office of the Comptroller of the Currency (OCC) issued a report in December 2016 exploring the merits of creating a special purpose bank charter for “FinTech” (financial technology) companies. The report focused on the role of bank charters in regulating financial markets. The new charter was finalized in Spring 2017 and applications began that year.

**NAR ACTION:** NAR supports easing restrictions on businesses’ ability to raise capital, and increasing liquidity in the commercial real estate market. NAR submitted a letter to the OCC highlighting the growing role that these lenders play in real estate, and the need for balancing innovation and regulation. The letter also referenced NAR’s commitment to innovation.

**NATIONAL FLOOD INSURANCE PROGRAM (NFIP):** The National Flood Insurance Program (NFIP) was extended for five years in 2012 by the Biggert-Waters Act, but Congress must reauthorize it again to continue providing flood insurance after 2017. Biggert-Waters was later amended by the “Homeowner Flood Insurance Affordability Act,” which restored grandfathering properties under lower risk rates upon remapping, reducing increased rates of non-grandfathered properties, and repealing rate premium increases at the sale of properties (including refunding increases to those who have already paid them). Later in 2014 FEMA launched the Office of the Flood Insurance Advocate, to assist property owners with questions and concerns over flood insurance rates and maps.

**NAR ACTION:** NAR continues to work closely with Congress and FEMA to implement the rest of the law, consistent with the statutory deadlines and congressional intent. NAR led a commercial real estate coalition to advocate for commercial priorities in the program’s reauthorization, which has been shared with the House Financial Services Committee and the Senate Banking Committee. In the 115<sup>th</sup> Congress, several bills have been introduced to reauthorize and reform the NFIP, and the House passed a 5-year reauthorization bill (H.R. 2874, the 21<sup>st</sup> Century Flood Reform Act, sponsored by Rep. Duffy (R-WI)); however the Senate has yet to take action on a long-term reauthorization measure. The NFIP is currently set to expire on November 30, 2018, after several short-term extension measures to keep the program from expiring.

**UNMANNED AERIAL SYSTEMS (DRONES):** FAA rules for small unmanned aerial systems (UAS) allow the operation of small UAS (less than 55 lbs.) for commercial purposes with a FAA UAS operator certificate. Though use of UAS is still restricted, the FAA is working on rules allowing flights beyond-visual-line-of-sight, at night, and over crowds, as well as a separate rule dictating the use of “micro-UAS,” which are those weighting less than 4.4 lbs.

**NAR ACTION:** NAR worked with the FAA and Congress to develop and advocate for UAS rules permitting commercial use of drones in a way that is affordable for users and safe for communities. This work included testifying at a Congressional hearing on the issue, sending comment letters to the FAA and the National Telecommunications and Information Administration, as well as participating in working groups and an Aviation Rulemaking Committee (ARC) with the FAA on micro-UAS. NAR will continue to work with the 115<sup>th</sup> Congress and the FAA as they move on to address further rulemaking needs for UAS.