

# National Association of REALTORS® Issue Brief

## Commercial Real Estate

February 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 bill 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 bill does repeal 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 sector groups, NAR commissioned another economic study on Section 1031, this time focusing on its impact on real estate. NAR participated in Hill visits, meetings with key members of Congress (including leadership and the tax writing committees), and press events individually and as part of the coalition in support of Section 1031. Retaining Section 1031 was one of the talking points for 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) does not have a notice requirement, leaving commercial property owners who may in good faith believe that their properties comply with the law vulnerable to lawsuits. Under the ADA attorneys may collect fees relating to pursuing claims of noncompliance, but the plaintiffs themselves 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 have instead gone toward fixing the issue. In recent years, these "drive-by" ADA suits, by attorneys targeting commercial properties with small, easily-correctible infractions, are on the rise.

**NAR ACTION:** *NAR participates in a coalition of commercial real estate groups advocating to reforms to the ADA requiring that notice be given to property owners before a suit is filed, giving them an opportunity to use their time and resources to correct the infraction instead of on attorneys. NAR supports H.R. 620, the ADA Education and Reform Act, a bipartisan bill sponsored by Rep. Poe (R-TX), which would accomplish those goals. H.R. 620 was marked up and approved by the House Judiciary Committee in September 2017; NAR is advocating for a full House vote and is working with the Senate on companion legislation.*

**BASEL III:** The Basel Committee proposed a new risk-weight regime ("Basel III") for High Volatility Commercial Real Estate (HVCRE), which includes commercial acquisition, construction, and development loans, and raises their risk-weight from 100 – 150%. This negatively impacts credit availability for commercial real estate and increased the lending standards above what federal regulators already required. The Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Board of Governors of the Federal Reserve System have proposed a new standard for the same type of loans, called the High Volatility Acquisition, Development and Construction ("HVADC") loans. The proposal decreases the risk weight attached to these loans, but broadens the definition of what type of loan is included in this treatment.

**NAR ACTION:** *NAR actively works with its members and industry partners to understand the impact of the Basel III standards. NAR has joined comment letters calling for changes to the provisions that would be most limiting, as well as submitted letters to Congressional hearings in the House Financial Services and the Small Business Committees stressing the burden that overly-broad regulations for lending institutions have on commercial real estate. NAR signed on to a coalition letter urging for the delay in finalizing Basel III reforms, which was ultimately successful. In 2017, NAR has worked as part of a coalition to assist in drafting legislation clarifying which borrowers fall under the HVCRE rules. H.R. 2148, "Clarifying Commercial Real Estate Loans," sponsored by Rep. Pittenger (R-NC), was approved by a vote of 59-1 in the Financial Services Committee in October. NAR sent two comment letters – one as the sole author, one with a coalition – to the banking agencies in December 2017 in response to a request for comment on the proposed HVADC rule.*

**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 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, which are currently set to expire Jan. 19. 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 allowed this provision to expire at the end of 2016, following a two-year (one of which was retroactive) reauthorization of it in December, 2015.

**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, as it considers a tax extenders package in early 2018. NAR has met with the tax-writing committees in the House and Senate to stress 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.

**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, which address Small Company Capital Formation and permit crowdfunding as a financing source, are now effective. The new rules update and expand Regulation A, an existing exemption from registration for smaller issuers of securities. This enables 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, effective since January 2016, 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:** The Marketplace Fairness Act would allow states to require out-of-state online retailers to collect and remit sales tax on purchases made by residents, thus leveling the playing field between online sellers and traditional brick-and-mortar stores, the clients of Commercial REALTORS®. In 1992 the Supreme Court ruled that Congress must grant this authority to the states, but Congress has since failed to act. As a result, states have passed laws in an attempt to collect the lost sales tax, resulting in court challenges; in 2018 the Supreme Court granted *cert* to a case challenging a South Dakota law. Two bills have been introduced in the 115<sup>th</sup> Congress: 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)). Both bills are the same as versions introduced in the previous Congress that NAR supported.

**NAR ACTION:** *NAR participates in the Marketplace Fairness Coalition, which advocates for internet sales tax legislation. In the 114<sup>th</sup> Congress, NAR supported bills establishing internet sales tax fairness, while working with sponsors of the bills and the House Judiciary Committee and leadership to develop compromise legislation. NAR will continue to work with Congress on this issue, and joined a real estate industry amicus brief to the Supreme Court supporting granting cert to the SD case – South Dakota v. Wayfair, Inc. et al.*

**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. The NFIP was reauthorized multiple times in 2017 via budget extensions, and is currently set to expire on Jan. 19.*

**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.*