



## NEWS

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### Reforming FIRPTA (Foreign Investment in Real Property Tax Act of 1980) Would Ease Pressure on Commercial Real Estate Markets and Stimulate Economic Growth

(WASHINGTON D.C.) — The Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) is an outdated U.S. tax law that discourages non-U.S. investors from investing in U.S. commercial real estate, harms the U.S. economy and needs to be reformed, according to a new report by two leading economists who served on the White House Council of Economic Advisers under different administrations.

In their study, *“How FIRPTA Reform Would Benefit the U.S. Economy,”* noted economists Martin Neil Baily and Matthew J. Slaughter detail how FIRPTA continues to inhibit foreign investment at a time when plunging values and loan defaults in U.S. commercial real estate pose a major threat to America’s economic recovery. Information on Baily and Slaughter appears below.

“FIRPTA needs to be modified to bring more liquidity into the current market, which is starved for equity investment,” said Real Estate Roundtable President and CEO Jeffrey D. DeBoer. “In these very challenging economic times, a nearly thirty-year old tax policy that was originally designed to protect farmland does not fit today’s marketplace realities. FIRPTA has impeded investment for decades by placing an onerous tax burden on foreign investment in all forms of U.S. commercial real estate, including office buildings, hotels and retail establishments. It is time for Congress to propose practical changes to FIRPTA.”

The Baily-Slaughter report addresses how FIRPTA reform would support U.S. commercial real estate by encouraging additional investment capital from abroad to bolster economic recovery. With a pressing need for large amounts of refinancing in the U.S. commercial real estate sector, the report notes that approximately 65% of commercial mortgages scheduled to mature in the next few years will not qualify for refinancing due to stricter bank lending standards. “With a typical debt maturity of 10 years, approximately \$350 billion in commercial real estate debt must be retired or rolled over each year. What is acutely needed is more capital,” the report states.

Due to FIRPTA, the end result of a non-U.S. investment in U.S. real estate can be an effective tax rate as high as 54.5% — an initial 35% tax on the gains from the real estate investment, plus additional tax on the after-tax proceeds. Compared to much more favorable tax rates on other asset classes in the U.S., real estate is a less-favored asset class – absent some relief from this high-cost tax structure.

The Baily-Slaughter report illustrates how FIRPTA imposes tax penalties on foreign investment in commercial real estate – penalties that do not exist when foreigners buy other U.S. assets such as Treasury securities, corporate equities or corporate bonds. The report also details how FIRPTA reform would help to stabilize commercial real estate values and refinancing pressures.

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The report's authors recommend FIRPTA reforms include "... outright repeal or, less dramatically, an initial holiday could be implemented: e.g., declare that new foreign investments in U.S. commercial real estate over the next five years would be exempt from FIRPTA. We think that the sizable economic benefits of reforming FIRPTA would exceed the small fiscal costs it would entail."

At a July 2009 hearing before the Joint Economic Committee (JEC) hearing, Roundtable President and CEO Jeffrey D. DeBoer initially sounded the alarm about economic stress on commercial real estate markets. His testimony before the JEC included a Five Point Plan – including FIRPTA reform – to address the liquidity crisis. DeBoer testified that "... the obstacles imposed under FIRPTA have led many non-U.S. investors to invest in real estate elsewhere – to such countries as Brazil, China and India – shifting wealth and economic dynamism away from the U.S. market. The laws relating to foreign investment in U.S. real estate should be reviewed by Congress and corrected in a responsible way to allow increased investment into US real estate."

#### **About the FIRPTA Report's Authors**

*Martin Neil Baily* is a senior fellow of Economic Studies and the Bernard L. Schwartz Chair in Economic Policy Development at Brookings. He focuses on issues of globalization, competitiveness and U.S. economic policy. Baily served as chairman of the Council of Economic Advisers during the Clinton administration (1999–2001) and one of three members of the council from 1994 to 1996.

<http://www.brookings.edu/experts/bailym.aspx>

*Matthew J. Slaughter* is Associate Dean for the MBA Program and Signal Companies Professor of Management at Tuck School of Business at Dartmouth, focusing on the economics and politics of globalization. Professor Slaughter served as a member on the Council of Economic Advisers in the Bush Administration (2005-2007), focusing on international trade, investment and the competitiveness of the U.S. economy.

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#### **About The Real Estate Roundtable**

The Real Estate Roundtable brings together leaders of the nation's publicly-held and privately owned real estate ownership, development, lending and management firms with the leaders of national real estate trade associations to jointly address key national policy issues relating to real estate and the overall economy. Collectively, Roundtable members' portfolios contain over 5 billion square feet of office, retail and industrial properties; over 1.5 million apartment units; and in excess of 1.3 million hotel rooms. Participating trade associations represent more than 1.5 million people involved in virtually every aspect of the real estate business.

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