

October 16, 2009

Member of Congress  
United States House of Representatives  
Washington, DC 20515

RE: Reject Carried Interest Tax Hike

Dear Representative:

More than ever, commercial real estate is navigating through uncertain and unprecedented times. It is clear that the U.S. commercial real estate industry is struggling and threatens to undermine the overall U.S. economic recovery. With the pressing need for large amounts of refinancing and declining property fundamentals, the near-term prognosis for this sector is not good. Under this extraordinary backdrop, we are particularly dismayed to learn that the Ways and Means Committee may consider increasing the tax on “carried interest”<sup>1</sup> as an offset to pay for upcoming legislation or new federal programs.

The legislation would tax the “carried interest” returns real estate professionals receive from the investment partnerships they organize and manage as ordinary income (35% top tax rate) – even if the nature of the income to the partnership is capital gain (15% top tax rate). The legislation also would add a 3 percent self employment tax, resulting in a near-tripling of the carried interest tax rate.

Since 2007, our industry has stressed to lawmakers time and time again the potential negative consequences of the carried interest legislation to the commercial real estate industry. We have explained the following:

- The proposal goes way beyond the “high income” people it is intended to impact—and in fact would alter the taxation of all partnerships large and small;
- Partnerships are the predominate business model used in all types of real estate development, ownership and investing including office buildings, apartments, hotels, shopping centers and senior housing;
- The legislation does not contain transition rules and, as a result, represents a retroactive tax increase that will significantly change the economics of transactions entered into decades ago;
- The legislation punishes general partners for aligning their risk and interests with equity investors. This is nonsensical because investors demand this alignment so the general partner remains incentivized to bring the investment to its maximum return;

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<sup>1</sup> Carried interest is a much misunderstood term. It simply means the percentage of income received from an investment that is greater than the percentage of the capital investment. In many ways, it is a return on “sweat equity”.

- Real estate professionals will be pushed to substitute investor equity with debt to avoid having to use a carried interest arrangement. The encouragement of more and riskier debt is bad policy in general and especially bad given how over-leveraged the economy is today; and,
- Raising capital for real estate investment will become even more difficult in an already challenging environment. Capital formation is what leads to job and tax base creation -- this proposal would discourage it.

Lastly, with the current turmoil threatening our economy, the mention of taxing carried interest at the higher ordinary income rate now has the potential of worsening the current credit crisis and, if enacted into law, having a negative impact on all businesses, particularly real estate partnerships.

Instead of raising taxes in a crisis, we believe it would be prudent to seek to calm investors and consumers' fears and encourage investment and entrepreneurial risk taking, which is so important to the nation's financial recovery. The small amount of revenue that would be actually raised by this proposed change does not justify the harmful impact to the real estate industry and to the economy as a whole.

It is bad policy in good economic times, and disastrous policy given the current economic conditions. We urge you to oppose any effort to increase taxes on carried interest.

**American Hotel & Lodging Association**  
**American Resort Development Association**  
**American Seniors Housing Association**  
**Building Owners and Managers Association International**  
**International Council of Shopping Centers**  
**NAIOP, The Commercial Real Estate Development Association**  
**National Apartment Association**  
**National Association of Real Estate Investment Managers**  
**National Multi Housing Council**  
**The Real Estate Roundtable**