Speak

Betty

Yes

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September 25, 1986

Nov. 6
Willard Hotel

The Honorable Robert J. Dole
Senate Majority Leader
S-230 Capitol Building
Washington, D. C. 20510

Dear Senator Dole:

The National Association of Industrial and Office Parks will hold a conference on the 1986 Tax Reform Act on Thursday and Friday, November 6 and 7, 1986. The Conference, entitled "Surviving and Thriving Under the 1986 Tax Reform Act," is designed to give NAIOP members and other real estate professionals a comprehensive understanding of the new law and its impact on commercial real estate transactions.

On behalf of the Association, I would like to invite you to address the opening dinner of the Conference at 8:00 p.m. on Thursday, November 6, 1986. The Conference will be held in the newly renovated Willard Hotel and I believe will attract widespread interest throughout the industry. I appreciate your consideration of our invitation and I will contact your office shortly after you receive this letter to determine if your schedule will permit you to join us.

Very truly yours,

James H. Davidson

James H. Davidson - Leah Richardson

JHD:lck

9/26 interim ltr
10/21 Advised Leah Sen would do -- will want to speak as early as possible

Don? yes

BOB DOLE
KANSAS

United States Senate
OFFICE OF THE MAJORITY LEADER
WASHINGTON, DC 20510

November 5, 1986

TO: Senator Dole

FROM: George Pieler

SUBJECT: Talk to National Association of Industrial and Office Parks

You are scheduled to speak to NAIOP at 8:00 p.m. on Thursday evening, November 6, at the Willard Hotel.

The purpose of their conference is to review the impact of tax reform on commercial real estate. Attendees will be about half owners of commercial real estate ventures, and the other half real estate tax people.

Your address will open the conference, so the group will not have gotten into technical briefings on tax reform yet.

They recommend you take credit (and will give you full credit) for working with Senator Bentsen to try to ease the impact of the new passive loss rules on real estate: specifically, your attempt to win an 'active developer' exception from the passive loss rules.

Anything you can say about possible modifications of the tax bill in 1987 obviously would be of interest. For example, will there be a new effort to get an 'active developer' exception; how will the IRS treat interest on mortgage-backed securities, and how will REIT income and losses be treated.

With regard to the IRS issues, the Service has already announced a list of "priority items" in tax reform, for which they plan to give "guidance" to taxpayers as early as possible (hopefully, with some statements issued before the end of the year). The list, which includes the entire passive loss area, was proposed for comment several weeks ago, and comments are due by November 28.

In addition, IRS Commissioner Lawrence Gibbs has said that the Service will try to expedite the entire process of issuing regulations on the tax reform bill by eliminating several layers from the internal review process, and speeding up coordination with Treasury.

Attached are materials on the real estate provisions of tax reform; on the economy; and on the possible Senate agenda in the 100th Congress.

Attachments

Senate Agenda: the 100th Congress

• There's no doubt about it, the agenda for the 100th Congress is going to be different under Democrat control. Already some issues are shaping up, as Senator Bentsen promises a big trade bill. And while Senator Byrd wants to work with President Reagan, you can bet a lot of the Reagan agenda will be put to the test: including aid to the contras, SDI, and the defense buildup.

• On the tax front, we can still expect corrections to the tax reform bill, and probably some substantive modifications as well--depending on what kinds of problems pop up as the new tax reform law is scrutinized in detail. But so far Democrats are saying there won't be any tax increase unless President Reagan asks for one--and you can bet the President will "just say no" to any tax hike.

• All of this means the Congress has a tough, tough row to hoe in meeting the Gramm-Rudman-Hollings deficit targets. In case anyone forgot, Gramm-Rudman is still the law: and it requires us to come up with a deficit of only $108 billion in 1988. That means a lot more deficit-reduction measures are needed, even if the economy grows at a fairly healthy clip in 1987.

• When you consider that the defense budget is already close to the bone--especially when we can't do anything to undermine President Reagan's negotiating hand with the Soviets--the deficit options are down to a pretty narrow range. So we all want to see what the new leadership in Congress comes up with.

• In addition, there are some important issues that we took up in the 99th Congress but didn't finish: matters like tort liability reform, the item veto, the balanced budget amendment, and banking legislation. All of these deserve the attention of the 100th Congress: as do President Reagan's nominations, particularly to the Federal bench.

November 6, 1986

The Economy in Late-1986

• The economy is still doing pretty good, and basically we're on the right track. But economic forecasts for the rest of the year are getting increasingly schizophrenic: because there are some mixed signals out there.

• The economy grew at a 2.4% pace in the third quarter of 1986, but only 0.6% in the 2nd quarter. The index of leading indicators has gone up steadily although at a declining rate. In fact, back in April the index rose by 1.5% the highest monthly rise in three years. Unemployment is down to 7.0%, and the stock market has recovered well from its September decline. On the other hand housing starts declined three months in a row before picking up in August: housing has been one of our bright spots this year, and starts declined again in September.

• What's becoming increasingly clear is that the we're seeing the downside of lower energy prices and lower interest rates before we can reap the benefits the oil price plunge costs us jobs in the energy industry, and lower interest rates cut government revenues, thereby adding to the deficit. At the same time, the trade deficit is slow to respond to the drop in the dollar: exports are unlikely to boost the economy until late this year or early next. But exports have begun to turn around: the trade deficit declined in both August and September.

• Still, there are undeniably powerful forces at work that should improve the prospects for strong growth. The drop in oil prices and lower inflation should increase the purchasing power of energy users and helps moderate inflationary pressures that might otherwise build as the dollar declines. And the Federal Reserve for the most part has been willing to provide sufficient monetary stimulus to encourage steady growth, given the reduced risk of inflation.

• The key now, to revive an old phrase, is to "stay the course". The financial markets expect us to the Gramm-Rudman deficit targets--that reduction in the government's financing needs will do a lot to keep recovery on a steady path. We must reject the illusion of protectionism, and keep markets free and open by strengthening the President's hand in trade negotiations. If we can do all that, plus fully implement the low rates in the new tax reform bill designed to boost long-term growth and productivity, the economy can be in good shape for a long time to come.

- Further moves toward lower interest rates -- and here the Fed has begun to provide real leadership -- would help us and help stabilize the world economy. The Japanese cut in their discount rate in late October may make it easier for the Fed to go further in that direction.

September 24, 1986

TAX REFORM

IMPACT ON REAL ESTATE

- There is much to recommend the tax reform bill in the sense of lowering rates and making sure that everyone with substantial income will have to pay some income tax. But that does not mean this bill is perfect tax reform.

- The treatment of real estate and other investments in limited partnership form is troublesome. A good case can be made for the passive loss rules as a way to curb tax shelters, but lenghthening the cost recovery periods and eliminating the investment tax credit, combined with reduced tax rates, would have gone a long way toward making tax shelters unattractive, even without the passive loss limitations.

- Even assuming the passive loss rules were necessary to combat tax shelters, a good argument could be made that it was overkill to apply the limitations to existing investments.

- As many of you know, I worked hard to provide transition relief to minimize hardship in the short run. We had some modest success in the Finance Committee in getting a four-year phase-in of the passive loss and interest limitations.

- And, in conference, I was successful in moderating the double impact of the investment interest limitation and the passive loss limitation. While this may seem to be a technical point, I can assure you that it was not easy to find the $3.6 billion that it took to make that technical change. This should make the transition period at least somewhat less harsh.

TAX REFORM

PASSIVE LOSS LIMITATIONS

- One of the largest revenue raisers on the individual side is the passive loss limitation. Despite the four-year phase-in, it will raise $36 billion over five years In 1991, alone, it is estimated to raise $12 billion.

- It also raises more money from wealthy individuals than from middle or lower income individuals. Thus, the maximum tax rates can be lowered without the Joint Tax estimators telling us that rich people will get more of a tax cut than other individuals.

- On the other hand, it is a strange thing to treat income and losses from limited partnership interests differently from interest and dividends and salary or so-called "earned" income. There really is no good reason not to be able to net your income and losses from different sources.

- In other areas of the tax code we go to great lengths to say that all types of income are the same. There are a number of allocation issues in the foreign area which are based on this concept such as the rules dealing with interest, for example.

- It would seem that, if we did not want tax shelters, we probably would be more honest with ourselves to address the artificial incentives that create large deductions, not make new artificial distinctions between different types of income and losses.

- In fact, with the repeal of the investment tax credit, the lengthening of the depreciation period, especially for real estate, and the broadening of the at-risk rules, we probably have done most of what should have been done without the passive loss rules.

- I'm concerned that the motivation behind the passive loss rules was less tax policy than it was merely revenue raising to fund the lower rates. That is how we got ourselves in the bind of applying the passive loss limitations to existing investments, rather than making the rule prospective.