

FEA Press Release

March 17, 2015

Study Finds Repealing Like-Kind Exchange Rules Would Hurt U.S. Small Businesses and Reduce GDP

The Federation of Exchange Accommodators (“FEA”) announced that the Section 1031 Like-Kind Exchange Coalition (“Coalition”), of which it is a member, released a study, “Economic Impact of Repealing Like-Kind Exchange Rules,” which concludes that repealing the I.R.C. Section 1031 like-kind exchange rules would slow economic growth, reduce GDP and hurt many U.S. small businesses.

Ernst & Young was commissioned to conduct the study in response to legislative proposals to repeal Section 1031, and concludes that the GDP reduction would be driven primarily by decreased business investment due to increased cost of capital.

The study confirmed that repeal of Section 1031 would negatively impact businesses and taxpayers in a myriad of industries. The industries most severely impacted by repeal include real estate, vehicle and equipment leasing and rental, truck transportation, and construction.

On March 17, 2015, the Coalition hosted a press briefing featuring small business owners and industry professionals who described how like-kind exchanges helped their businesses and explained how repeal of Section 1031 would hurt their industries.

“Like-kind exchanges allow domestic businesses to efficiently expand and prosper, stimulating economic growth. This important provision is used by a wide array of businesses including farmers and ranchers, commercial and multi-family housing real estate investors, construction companies, trucking and transportation companies as well as small businesses that invest in real estate and own equipment rental and leasing operations,” commented Mary Cunningham, President of the Federation of Exchange Accommodators. “Like-kind exchanges also help promote environmental conservation by allowing ranchers and farmers to sell conservation easements on environmentally sensitive lands to conservation organizations. With capital gains tax deferred, the full sale proceeds can then be reinvested in more productive acreage or other income producing real estate,” she explained.

The findings of the Ernst & Young study quantify that a repeal of the like-kind exchange provisions to pay for a corporate rate cut, corporate tax reductions, or to fund increased spending, would unequivocally result in lower economic growth in the U.S. economy.

These findings demonstrate that repeal of Section 1031 would be contrary to the stated goals of tax reform, namely: economic growth, revenue neutrality and fairness. The economic impact study analyzed the impact of this proposal on the U.S. economy and concluded that the lower corporate rate financed by repealing Section 1031 would reduce GDP by an average of \$8.1 billion per year, with an aggregate loss of \$61 - \$131

billion over 10 years. It would further cause contraction in economic growth in the U.S., imposition of an unfair tax burden on certain economic sectors and would not be revenue neutral.

After analyzing the macroeconomic impact of repealing like-kind exchanges, the study "...finds that repeal of the like-kind exchange rules increases the cost of capital in the economy, even when combined with lower tax rates. The higher cost of capital is found to discourage business investment which adversely affects the overall economy. Repeal is found to negatively affect the economy ... under a range of modeling assumptions."

There is widespread agreement in virtually all schools of economic thought that the level of investment and the process of economic growth are closely interconnected. At its core, capital formation represents an investment in the future. Tax changes that raise the cost of capital reduce the incentive for capital formation and new investment. Such changes stifle an economy's ability to expand its production capacity, slow economic growth, and ultimately reduce GDP.

"Like-kind exchanges are good for real estate owners, good for job creation and good for the economy. Taxes on real estate sales always slow transactions and sometimes freeze markets. Allowing the exchange of like-kind properties helps small and large owners of business real estate stay invested so they can grow and expand their businesses and create jobs. Keeping capital invested, as the current like-kind property exchange rules allow, is the best way to promote long-term, job-creating economic growth," commented Jeffrey D. DeBoer, President and CEO of The Real Estate Roundtable.

The study was authored by the Ernst & Young Quantitative Economics and Statistics team led by Robert J. Carroll, PhD, its National Director. Dr. Carroll previously served as Deputy Assistant Secretary for Tax Analysis of the US Treasury Department where he was the Department's top economist working on tax policy issues. He is also a former Senior Economist with the President's Council on Economic Advisers.

The Section 1031 Like-Kind Exchange Coalition is comprised of 12 diverse industry associations whose members represent more than one million U.S. businesses and taxpayers that will be severely impacted should Section 1031 be repealed. In addition to the FEA, coalition members include The Real Estate Roundtable, the National Association of REALTORS®, the National Association of Real Estate Investment Trusts, the National Multifamily Housing Council, the International Council of Shopping Centers, the American Rental Association, the American Car Rental Association, the Iowa Soybean Association, the Equipment Leasing and Finance Association, the Alternative and Direct Investment Securities Association and the Associated Equipment Distributors.

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