



## The Imminent Commercial Real Estate Crisis and The CRE Solution

### Problem Summary

Commercial real estate (CRE) transactions have dropped a staggering 90 percent since 2007. Between now and 2014, \$1.4 trillion in CRE loans will be coming due; half of these currently are underwater. Commercial property values have plummeted by more than 40 percent, and commercial vacancies continue to increase. In addition, the construction industry has lost over two million jobs leading to job losses in related sectors and further shrinking revenue to state and local governments. Construction unemployment now hovers at about 20 percent. The largest CRE loan losses are projected to begin in 2011 falling disproportionately on small businesses and smaller regional and community banks, many of which are FDIC insured and have high concentrations of CRE loans. Because these banks play a critical role in providing capital to small businesses and new business start-ups, their failure could undermine the economic recovery, leading to further unemployment and greater economic instability.

### The CRE Solution

The 'CRE Solution' is a 3-year, tax deduction program that encourages commercial property owners to complete substantive efficiency renovation projects. The deduction would be granted on the full value of qualifying efficiency improvements up to a maximum amount. It would be tradeable and fully transferable to a new owner for the life of the deduction. The CRE Solution would amend the Energy Efficient Commercial Building Tax Deduction (26 U.S.C. 179(d)) from \$1.80 per sq.ft. to a range of \$3.00 to \$9.00 per sq.ft. for meeting energy reduction targets as follows:

| Existing Building Renovations                              |   | New Building Construction                                  |   |
|--|---|--|---|
| 3-Year   | Minimum Energy Reduction Target         | 3-Year   | Minimum Energy Reduction Target         |
| Maximum annual tax deduction per square foot of floor area | Percentage better than ASHRAE 90.1-2004 | Maximum annual tax deduction per square foot of floor area | Percentage better than ASHRAE 90.1-2004 |
| \$ 4.50  | 30%                                     | \$ 3.00  | 30%                                     |
| \$ 6.00  | 50%                                     | \$ 4.50  | 50%                                     |
| \$ 7.50  | 75%                                     | \$ 6.00  | 75%                                     |
| \$ 9.00  | Zero-Net-Energy                         | \$ 7.50  | Zero-Net-Energy                         |

For each \$6 billion of deferred CRE tax revenue, the CRE Solution would generate \$70.8 billion in new private spending, and \$15.4 billion in new federal tax revenue, more than paying for itself.

### The CRE Solution Impact

- Creates 1.3 million jobs, quickly and cost-effectively,
- Increases after-tax cash flow and property values, and reduces loan defaults,
- Increases CRE desirability and investment value,
- Increases new CRE sales (narrows the gap between the bid and ask price of CRE property),
- Brings ESCo's and A/E/C firms into the CRE efficiency renovation market,
- Decreases building energy consumption, greenhouse gas emissions, and operating costs, and
- Generates billions of dollars in federal, state, and local tax revenue.

## **The CRE Solution and Jobs**

The 'CRE Solution' commercial building tax deduction is designed to leverage deferred federal tax dollars to stimulate private spending for efficiency renovation and high-performance new construction. For each federal tax dollar deferred, building owners will spend, on average, \$11.80 on commercial building renovation and new construction. It is this \$70.8 billion in new private spending that creates 1.3 million jobs<sup>1</sup> for each \$6 billion in deferred taxes. Additionally, the CRE Solution will generate \$5 billion in state and local government revenue and \$15.4 billion in new federal tax revenue, more than paying for itself. And, as CRE property is sold, the government receives the deferred taxes. Since the CRE market is now frozen with few transactions and little construction taking place, a tax deduction tied to efficiency construction will increase government revenue as CRE property is sold and renovated, and new buildings built.

Both the amount of tax deduction and deferred allocation is weighted toward building efficiency renovation rather than new construction. The maximum tax deduction for renovation ranges from \$4.50 to \$9.00 per sq.ft. for renovation and \$3.00 to \$7.50 per sq.ft. for new construction. For each \$6 billion in deferred taxes, \$4.8 billion is allocated for renovation and \$1.2 billion for new building construction.

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<sup>1</sup> 588,621 direct, 339,020 indirect, and 372,937 induced jobs.