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REAL ESTATE
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November 27, 2002

Internal Revenue Service
Room 5226
P.O. Box 7604, Ben Franklin Station
Washington, DC 20044

ATTENTION:CC:ITA:RU (REG- 103735-00; REG-154117-02; REG-154116-02; REG-154115-02; REG-154429-02; REG- 154423-02; REG-154426-02; REG-110311-98)

RE: Disclosure and List Maintenance Regulations

Ladies and Gentlemen:

The National Association of Real Estate Investment Trusts® ("NAREIT") wishes to thank you for this opportunity to comment on the temporary and proposed regulations issued on October 22, 2002, under Section 6011(a) regarding the filing of disclosure statements by taxpayers regarding potentially abusive transactions (the "Regulations").[1] The Regulations include an exception to the disclosure of two types of transactions by regulated investment companies ("RICs," or mutual funds). As further described below, we respectfully request that these exceptions be extended to real estate investment trusts ("REITs") when the Regulations are finalized. These exceptions involve the reporting of transactions with significant book-tax differences and loss transactions.[2] The application of each of these exceptions is addressed in further detail below.

NAREIT is the national trade association for real estate investment trusts ("REITs") and publicly traded real estate companies. Members are REITs and publicly traded businesses that own, operate and finance income-producing real estate, as well as those firms and individuals who advise, study and service those businesses. REITs are companies whose income and assets are mainly connected to income-producing real estate. NAREIT represents over 170 REITs and publicly traded real estate companies that own over $350 billion of real estate assets, as well as over 1,500 industry professionals who provide a range of legal, investment, financial and accounting-related services to these companies.

[1] T.D. 9017. Because the text of the temporary and proposed regulations is identical, for simplicity, this letter will cite only the temporary regulations.
[2] Treas. Reg. Sec. 1.6011-4T(b)(8)(ii).

First, we would like to commend the Treasury Department on the issuance of the Regulations. We believe that disclosure is frequently the best and least burdensome remedy to tax shelters, and we support the Regulations' emphasis on disclosure. Second, we would like to recommend that the Regulations extend the exceptions provided to disclosure for RICs to REITs, or at the very least to REITs that are subject to public reporting.

REITs: Background

Based on the mutual fund provisions of the tax law, Congress amended the tax law in 1960 to permit the formation of REITs. Because REITs were patterned after RICs, there are many provisions that are applied similarly for these two types of entities. Subchapter M provides for the tax treatment of both, and includes the allowance of the dividends paid deduction under section 561 of the Internal Revenue Code of 1960 (the "Code").[3] The legislative history underlying the tax treatment of REITs specifically indicates that Congress intended to equate the tax treatment of REITs with the treatment accorded to RICs.[4] In fact, because of the similarities between RICs and REITs, the Internal Revenue Service has, in several rulings, relied on published rulings involving RIC taxpayers to determine whether similar income was qualifying income for REIT purposes and vice versa.[5]

The Regulations: In General

Treas. Reg. § 1.6011-4T(a) provides that any taxpayer with a "reportable transaction" within the meaning of Treas. Reg. § 1.6011-4T(b) must disclose that transaction. As relevant here, Treas. Reg. § 1.6011-4T(b) provides that two particular types of transactions are considered to be "reportable transactions:" "loss transactions" under Treas. Reg. § 1.6011-4T(b)(5), and "transactions with a significant book-tax difference" under Treas. Reg. § 1.6011-4T(b)(6). Although the Regulations provide an exception for RICs with respect to both types of transactions,[6] the Regulations do not provide similar exceptions for REITs. Set forth below is our analysis as to why we believe that a similar exception should be provided for REITs.

1. Loss Transactions

The Regulations provide that a "loss transaction" includes any transaction resulting in, or that is reasonably expected to result in, a loss under section 165 of at least $10 million in any single taxable year or $20 million in any combination of taxable years for

[3] Unless otherwise provided, all section references herein shall be to the Code.
[4] H.R. Rep. No. 2020, 86th Cong., 2d Sess. 4 (1960).
[5] *See, e.g.*, PLR 97260134 (April 2, 1997), PLR 9636014 (June 6, 1996), PLR 9509011 (Nov. 30, 1994), PLR 9452032 (Nov. 30, 1994), PLR 9308013 (Nov. 24, 1992), PLR 8552063 (Sept. 30, 1985), PLR 8416018 (Jan. 13, 1984), GCM 39570 (Nov. 12, 1986). Cf. Rev. Rul. 77-199, 1977-1 C.B. 195.
[6] Treas. Reg. § 1.6011-4T(b)(8)(ii).

corporations.[7] A section 165 loss "includes an amount deductible by virtue of a provision that treats a transaction as a sale or other disposition, or otherwise results in a deduction under section 165. A section 165 loss includes, for example, a loss resulting from a sale or exchange of a partnership interest under section 741."[8] Thus, capital losses and section 1231 losses are subject to disclosure as well as ordinary losses.

Although the Regulations exempt RICs from the disclosure of loss transactions, the Regulations do not provide a similar exemption for REITs.[9] RICs are generally required to register with the Securities and Exchange Commission under the Investment Company Act of 1940. Many REITs either are publicly traded or are required to register with the SEC under the Securities Exchange Act of 1934 (the "34 Act"). Such REITs must disclose all material transactions in their public filings. We believe that the same policy applicable to exempting RICs from disclosing loss transactions also should apply to exempt REITs from these requirements. At the very least, because of the similarities in RICs and REITs described above, and because SEC-registered REITs must disclose all material transactions in their public filings, the exemption for RICs should be extended to REITs that are reporting companies under the 34 Act. This limited exception will avoid unnecessary filings by such taxpayers without exempting transactions that are not otherwise disclosed by non-SEC-registered REITs.

2. Transactions With a Significant Book-Tax Difference

The Regulations define a transaction with a significant book-tax difference as a transaction when the treatment for Federal income tax purposes of any item or items from the transaction differs, or is reasonably expected to differ, by more than $10 million on a gross basis from the treatment of the item or items for book purposes in any taxable year.[10] Book income is determined by applying U.S. generally accepted accounting principles ("GAAP") for worldwide income.

This category of transaction generally applies to taxpayers that are reporting companies under the 34 Act (and related business entities)[11] and to business entities that have $100 million or more in gross assets.[12] When a taxpayer is considered to participate in a transaction indirectly through a partnership, items from the transaction that otherwise may be considered items of the partnership (for tax or book purposes) are treated as items of the taxpayer (to the extent of the taxpayer's allocable share).[13]

Unless the regulations provide a specific exception for disclosure of a taxpayer's dividends paid deduction, disclosure would be required. The dividends paid deduction is

[7] Treas. Reg. § 1.6011-4T(b)(5).
[8] Treas. Reg. § 6011-4T(b)(5)(ii)(B).
[9] Treas. Reg. § 1.6011-4T(b)(8)(ii).
[10] Treas. Reg. § 1.6011-4T(b)(6).
[11] Treas. Reg. § 1.6011-4T(b)(6)(ii)(A)(1).
[12] Treas. Reg. § 1.6011-4T(b)(6)(ii)(A)(2).
[13] Treas. Reg. § 1.6011-4T(b)(6)(ii)(E).

a tax deduction that is not expensed under GAAP, and none of the exceptions under Treas. Reg. § 1.6011-4T(b)(6)(iii) applies to exempt the reporting of the dividends paid deduction. While RICs are exempted from the disclosure of significant book-tax differences,[14] the Regulations do not provide a similar exception for REITs. As a result, unless the Regulations are amended, substantially all REITs, including publicly held REITs, will be required to file a disclosure statement.

Since REITs file a special return (Form 1120-REIT) on which the dividends paid deduction is clearly identified on line 21b on page 1 of the return, as well as on Schedules A and M-1 of the return, it would seem that REITs already provide sufficient disclosure to the IRS a of the existence of the REIT and clear disclosure of the amount of its dividends paid deduction. For these reasons, we request that the dividends paid deduction should be excluded from disclosure for all REITs under Treas. Reg. § 1.6011-4T(b)(6)(iii). In addition, because of the similarities in RICs and REITs, the exemption for RICs from reporting book-tax differences generally should be extended to REITs, especially those companies that are reporting companies under the 34 Act.

Thank you for the opportunity to comment on these Regulations. If you would like to discuss the issues presented in this letter in more detail, please do not hesitate to contact me or Dara Bernstein at (202) 739-9400, or Gary A. Cutson, of PricewaterhouseCoopers LLP, at (678) 419-8850.

Respectfully submitted,

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[14] Treas. Reg. § 1.6011-4T(b)(8)(ii).