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THE HOME PURCHASE TAX CREDIT: A PRESCRIPTION FOR ECONOMIC RECOVERY

TESTIMONY OF DALE LEPPA CHAIRMAN, LEPPA RENTS-BOBCAT OF AKRON ON BEHALF OF THE ASSOCIATED EQUIPMENT DISTRIBUTORS BEFORE THE U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON SMALL BUSINESS

JUNE 5, 2008

Good morning Chairwoman Velazquez, Ranking Member Chabot, and other distinguished members of the House Small Business Committee.

My name is Dale Leppo and it is my pleasure to come before you today both in my capacity as a small business owner and as a spokesman for my industry. I am the chairman of Leppo Rents-

Executive Summary:

- Economic data released last week suggests that the residential real estate crisis is getting worse.
- The downturn in the residential real estate market is hurting consumer confidence, worker mobility, and small construction industry companies.
- Both the House and Senate have passed home purchase tax credit legislation. However, given new evidence of the scale of the residential real estate crisis, the home purchase tax credit should be dramatically expanded in conference and quickly enacted into law.
- To revitalize the real estate market and stimulate demand, AED urges adoption a \$7,000 home purchase tax credit for individuals and couples (regardless of income level) who purchase any primary residence (regardless of value, loan status, etc.) by Dec. 31, 2008.

Bobcat of Akron, a family-owned company that sells, rents, and services Bobcat, Gradall, and JLG construction products from six locations throughout northern Ohio. I am also the 2008 chairman of the Associated Equipment Distributors' (AED) Government Affairs Committee and served as the national chairman of AED in 2006. For those of you not familiar with it, AED is the national trade association the represents authorized, independent distributors of construction, mining, forestry, and agricultural equipment. AED has more than 1,000 members and approximately 48 percent of our distributor members report annual revenues of \$10 million or less.

Since mid-January, AED has been urging Congress to enact a home purchase tax credit to stimulate the residential real estate market. Last month the House of Representatives approved a housing stimulus bill that includes a refundable \$7,500 tax credit for first-time homebuyers. The tax credit would have to be repaid over 15 years and would be phased-out for individuals and couples earning more than

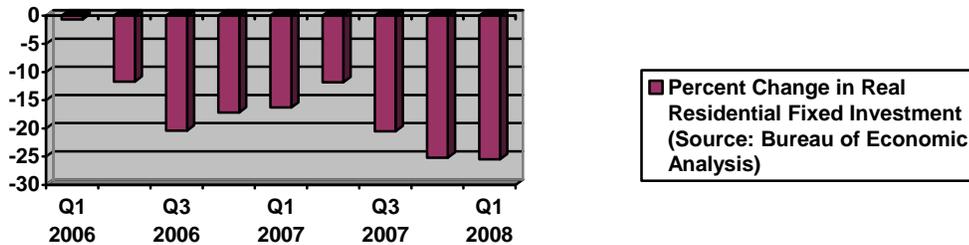
\$70,000 and \$140,000 respectively. A housing stimulus bill that passed the Senate on April 10 would provide a \$7,000 tax credit over two years for buying a home that is in foreclosure.

We are pleased that the both the House and Senate have passed legislation in this area. We now urge that Congress act quickly to finalize home purchase tax credit legislation and, given signs that the residential real estate crisis is getting worse, we further urge that the tax credit be expanded in conference beyond what has passed the House and Senate to ensure maximum impact and benefit. Specifically, we recommend that Congress adopt a \$7,000 home purchase tax credit for individuals and couples (regardless of income level) who purchase a primary residence (regardless of value, loan status, etc.) between June 30 and Dec. 31, 2008.

The Effect of the Housing Market Downturn on the Economy and Consumer Confidence

The downturn in the residential real estate market has had a dramatic impact on the U.S. economy over the last two and half years. The Bureau of Economic Analysis (BEA), which has consistently cited the housing market as a major drag on the economy, reported on May 29 that real residential fixed investment (i.e., home purchasing) decreased 25.5 percent in the first quarter of 2008.¹ BEA data show that real residential fixed investment has fallen in every quarter since the beginning of 2006 and that the decline in the first quarter of this year was the biggest yet. In other words, although we have been weathering this storm for quite some time, the residential real estate market is getting worse, not better.

Home Purchasing 2006-2007



Other data support this assertion. The Office of Federal Housing Enterprise Oversight (OFHEO) reported on May 22 that U.S. home prices fell 3.1 percent over the last year - the largest decline in the past 17 years.² The figures were part of OFHEO's seasonally adjusted purchase-only house price index. The index, which is based on data from home sales, was 1.7 percent lower on a seasonally-adjusted basis in the first quarter of this year than in the fourth quarter of 2007. According to OFHEO, the first quarter of 2008 saw the largest quarterly price decline on record. OFHEO also reported that home prices fell in 43 states, with the largest decline - eight percent - in California and Nevada.

¹ "Gross Domestic Product: First Quarter 2008 (Preliminary) – Corporate Profits: First Quarter 2008 (Preliminary)", Bureau of Economic Analysis, May 29, 2008 <<http://www.bea.gov/newsreleases/national/gdp/2008/pdf/gdp108p.pdf>>.

² "Decline in House Prices Accelerates in First Quarter", Office of Federal Housing Enterprise Oversight, May 22, 2008 <<http://www.ofheo.gov/newsroom.aspx?ID=435&q1=1&q2=None>>.

The Conference Board reported on May 27 that the consumer confidence index had fallen to a 16-year low³ and analysts have cited the housing market (along with higher fuel and food prices) as a primary cause of consumer pessimism.⁴ *The Economist* recently suggested another pernicious consequence of the residential real estate crisis that has henceforth received little attention: "A downturn centered on housing ... constrains one of the biggest safety valves in America's economy: people's ability to move." In other words, whereas in past economic downturns, Americans have been able to migrate from depressed areas to parts of the country where the economy is stronger, "This time, that mobility is hampered by people's inability to sell their homes."⁵

The Effect of the Housing Market Downturn on Equipment Industry Small Businesses

In addition to the overall impact on the national economy, the downturn in the housing market is also having a direct impact on construction equipment distributors around the country.

The construction equipment industry is dominated by small- and medium-size family-owned businesses. The home construction process involves such diverse activities as land clearing and grading, road construction and paving, sewer and drinking water line installation, home site excavation, and landscaping. Thus, the housing market is one that impacts equipment distributors in almost every market category. Traditionally, industry analysts have monitored housing starts data as important indicator of the health of the equipment industry.

In an attempt to document the impact of the housing downturn on our members, AED conducted a member survey in late March and early April. An overwhelming 93 percent of the equipment distributors who responded to AED's 2008 Government Affairs Survey said that the housing slump has had an impact on their companies, with close to half (46 percent) saying that it has had a major impact.⁶

That is the national picture from 30,000 feet. Now let me explain more specifically how the downturn has affected us in northern Ohio. The Association of Equipment Manufacturers (AEM) compiles data for retail equipment sales and new units put into rental fleets in every county in the United States. The data are broken up by category of machine. Two of the biggest unit volume categories are skid steer loaders and mini excavators (often lumped together as "compact equipment"). One of the primary applications in which compact equipment is used is residential construction. Compact equipment is a big part of my company's business.

³ "The Conference Board Consumer Confidence Index Declines", The Conference Board, May 27, 2008 <<http://www.conference-board.org/economics/ConsumerConfidence.cfm>>.

⁴ Catherine Clifford, "Consumer Confidence: Worst Since '92 - Conference Board's Measure Falls More Than Expected in May Amid Concerns About a Weak Labor Market and Poor Business Conditions", CNNMoney.com, May 27, 2008 <http://money.cnn.com/2008/05/27/news/economy/consumer_confidence/?postversion=2008052713>.

⁵ "The Geography of Recession", *The Economist*, Feb. 9, 2008 <http://www.economist.com/world/na/displaystory.cfm?story_id=10650727>.

⁶ "Housing Downturn Has Had Big Impact on Equipment Industry, But Depreciation Bonus Already Helping, AED Survey Shows", *Washington Insights*, Associated Equipment Distributors, April 2008, <<http://www.aednet.org/government/aed-washington-insights.cfm?id=04/01/2008&show=yes#ref3>>.

Table 1 below quantifies what has happened in the market for skid steer loaders and mini excavators in 18 counties in northeast Ohio (including Akron, Canton, Cleveland, Wooster, Youngstown) and

Table 1 –Northern Ohio and Western Pennsylvania Compact Equipment Sales (Jan. through April) Source: Association of Equipment Manufacturers						
Type of Equipment	2005	2006	2007	2008	Percentage Change 2005 to 2008	Percentage Change 2007 to 2008
Skid Steer Loaders	286	255	215	149	-48 percent	-31 percent
Mini Excavators	104	108	107	63	-39 percent	-41 percent
Total Compact Equipment	390	363	322	212	-46 percent	-34 percent

three counties in western Pennsylvania (including Mercer) during the last four years for the months of January through April. Simply put, compact equipment sales have dropped 46 percent since

2005. Over the last year alone, the skid steer market is off 31 percent and the mini excavator market is off 41 percent.

From the ground, it is easy to see that the cause of the sharp decline in these equipment markets is the slowdown in residential construction. The fact that too many houses are sitting empty without buyers has led to a significant drop in new housing starts. As a result, my customers (homebuilders and others) are going out of business, equipment distributors are closing branches, we are having to repossess equipment from non-paying customers, and overall business activity in the construction industry is down. My company has survived because commercial and industrial markets offset the residential slowdown for us in 2007, but to be quite candid, keeping up in 2008 is proving to be a challenge.

Based on discussions with my colleagues around the country, I can say with a high degree of confidence that every one of you on this committee has small construction industry companies in your districts facing the same challenges I am.

The Case for a Home Purchase Tax Credit

It is for all the foregoing reasons that AED has played a leading role in advocating for a home purchase tax credit since the beginning of the year. In the past, temporary tax incentives have helped to influence consumer behavior and speed economic recovery. The best recent example is the depreciation bonus. During the economic slowdown of 2000 and 2001, business purchasing dropped off dramatically. However, after Congress created the depreciation bonus in early 2002, business capital investment immediately began to turn around. An AED study supports the notion that the depreciation bonus was at least part of the reason.⁷ We therefore believe that a temporary, broad-based home purchase tax credit that incentivizes residential real estate purchasing would dramatically improve conditions in the housing market. As I noted earlier, the tax credit proposals recently passed by the House and Senate are narrowly tailored. We believe that given the scale of

⁷ Christian A. Klein, "Capital Investment Incentives Work: A Study of the Past and Future Impact of the Depreciation Bonus and Small Business Expensing Level Increases On Utility Contractor Equipment Purchasing", May 12, 2003 <http://www.depreciationbonus.org/pdf/NUCA_AED_Tax_Study.pdf>.

the crisis and the fact that conditions have continued to worsen since the House and Senate passed their bills, the tax credit should be expanded in conference. To ensure maximum impact, the tax credit should:

- Be available to taxpayers of any income level and regardless of whether the taxpayer has previously owned a home;
- Apply to any primary residence purchase;
- Not discriminate based on the status of the house (i.e., whether it is new, in foreclosure, etc.); and
- Not require taxpayers to repay the benefit.

AED specifically proposes that Congress enact a \$7,000 tax credit for individuals and couples (regardless of income level) who purchase a primary residence (regardless of the home's loan status, value, etc.) between June 30 and Dec. 31, 2008.

This approach has a number of advantages:

- It would stimulate demand and slow the decline in home values, thus addressing a major economic worry and contributor to consumer pessimism.
- It directly targets the housing market which, as indicated by BEA, has been a major drag on the economy.
- It would help bring stability and confidence to the housing market, thereby speeding economic recovery.
- It would provide benefits to taxpayers of all income levels; however, the proposal is progressive because homebuyers would receive the same tax credit regardless of income or the value of the home being purchased. Thus, it would disproportionately benefit those at the lower end of the income spectrum.
- It would help make homes more affordable by effectively putting cash in the pockets of home purchasers, thereby helping homebuyers ease into their new mortgages.
- The benefit would go directly to individuals and families who buy homes, not to developers, realtors, mortgage companies, or banks.

Based upon projections that 5.66 million homes will be sold in the United States in 2008⁸, the cost of providing a \$7,000 tax credit for each home purchased for six months would be less than \$20 billion given that not every transaction involves a primary residence.

⁸ "Stable Existing-Home Sales Expected in Early 2008, then Gradual Rise", National Association of Realtors, Jan. 8, 2008, <http://www.realtor.org/press_room/news_releases/2008/pshi_jan08_stable_existing_home_sales.html>.

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Conclusions

America is facing an economic crisis unlike any in a generation. While other recent economic slowdowns have been the result of one or two factors (e.g., the decline in business purchasing that led to the 2000-2001 downturn), the U.S. economy is now facing a number of challenges at once: a residential real estate slump, escalating oil and food prices, a consumer credit crisis, and a weak dollar. Of all of these, Congress is best positioned to address the residential real estate crisis and the most effective way to do so is through a home purchase tax credit.

I therefore again, on behalf of AED members and small construction industry companies throughout the country, urge Congress to act quickly to enact a broad-based, temporary home purchase tax credit to stimulate residential real estate purchasing for the remainder of 2008. If enacted before the end of June, a home purchase tax credit could significantly improve the housing market as we enter the height of the buying season. However, the window of opportunity is extremely narrow and any delay in enacting the proposal will only postpone our recovery.

Thank you for holding this hearing on such an important issue. We look forward to working with you and your colleagues in the House and Senate in the coming weeks to make a home purchase tax credit a reality.

For questions regarding this testimony or for more information, please contact:

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