

GREETINGS...

Greetings to our clients, associates and friends in the US, China and Asia. Frances and I look forward to our upcoming trip to Shanghai, Beijing and Taipei. We hope you enjoy the latest edition of our company newsletter.

Sincerely,
Aaron Schechter and Frances Chou

HOT TOPICS...

CIC looking to invest in US distressed real estate...

China Investment Corp. (CIC), China's \$300 billion sovereign-wealth fund, is considering large investments in US distressed real estate, according to knowledgeable sources. Recently, officials from CIC have held talks with large US private equity fund managers regarding potential investments in distressed assets, including mortgage securities backed by commercial property.



CIC is also considering investing through US government's bailout programs, the Treasury's Public-Private Investment Program, known as PPIP. Under the program, the Treasury will co-invest with designated funds that buy toxic mortgages that have been clogging banks' balance sheets. The US government, through the Treasury and the Federal Reserve, will also make financing available to the ventures. In other words, CIC and the US Treasury would be partners in borrowing money from the US government to buy troubled mortgages. The PPIP will utilize several fund managers and each fund limits any single investor to a 9.9% stake. Initially, the PPIP program is being allocated US\$30 billion.

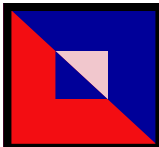
One analyst estimated that in order to achieve any meaningful diversification in its portfolio, CIC would need to set aside between US\$4 - \$10 billion in global property investments in the next 18 months, and estimates that by 2104 CIC's property investments in the US alone could reach more than US\$20 billion. In order to diffuse any political risk, CIC's US investments are likely to be minority stakes, invested through US fund managers, as opposed to direct stakes in actual properties. It has been estimated that US commercial real estate values have already declined by 35%. Currently, US real estate executives are lobbying to amend the tax law to encourage overseas capital to flow into US real estate, thus helping to prevent a further decline in commercial-property values.

China's consumers...

With US consumers pulling back in response to the recession, many US companies are increasingly looking towards fast-developing countries such as China, India and Brazil to boost sales. The shift reflects a rebalancing as the world relies less on the US consumer and more on consumer spending in places like China.

China has the world's fastest-growing consumer market, increasing by 8% per year in real terms over the past decade. Retail sales have increased by more than 17% in real terms during a recent 12 month period, though this figure may be inflated due to government purchases. Yet domestic consumption as a share of GDP has fallen in China and is very low by international standards, only 35% in China, compared to 50-60% in most other Asian economies and 70% in the US. Consumers in the US and Europe each pump more than US\$9.5 trillion a year into the global economy, even at their current recession-diminished pace. China's much poorer households spent just over \$1.5 trillion last year. Yet Chinese incomes continue to rise.

China has been credited with the speed of its economic stimulus plan in response to the global downturn, and economists hope that it will make the structural reforms necessary to continue to keep domestic demand growing and reducing its trade deficit, but also to derive more growth from domestic consumption and less from investment. While there is opportunity for foreign



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HOT TOPICS (Continues)...

companies, challenges remain due to cultural and governmental barriers as well as stiff competition, piracy and weak rule of law. (For a previous discussion of China's stimulus plan and investment see our recent newsletter article at <http://www.splusc.com/Newsletter080709.pdf>).

LEARN THE ROPES....

Real Estate Event Hosted by UC Berkeley Haas Alumni Network, Los Angeles Chapter

Aaron Schechter was co-organizer of the recent event, REAL ESTATE: Where From Here? Fast recovery or lingering doldrums...hosted by the UC Berkeley-Haas Alumni Network-Los Angeles Chapter in association with the USC Lusk Center for Real Estate and the USC Marshall School of Business Alumni Association. The event was held this past Sept. 17, 2009, at the Luxe Hotel in Brentwood, CA and drew over 250 attendees.

LEGALLY SPEAKING...

Be Aware of US Tax Liabilities When Investing in US Real Estate

A lot of foreign investors are interested in investing in US real estate market, however, oftentimes, foreign investors are unfamiliar with US federal and state tax law regulating foreign real estate investors, which will become costly for the foreign investors. Back in 1980, the US federal government implemented the Foreign Investment in Real Estate Tax Act ("FIRPTA") to impose tax on the gains received by foreign investors from the sale of their US property. This article will discuss a few basic issues.

The definition of a "foreign investor" is a nonresident alien individual (a person, who does not have a green card, a substantial presence in the US or tax treaty benefit as to residency) or a foreign corporation. Pursuant to the treaty between the US and China, any real estate income derived by a Chinese resident from real property situated in the US may be taxed by the US, and vis versa.

For any income derived by a foreign investor from US real estate, the foreign investor will generally pay income tax like a US investor, which is quite different from the exemptions that foreign investors can enjoy on other types of income earned in the US. With regard to capital gain tax, a foreign investor will also pay similar capital gain tax as a US investor, which is approximately 15% for a nonresident alien individual investor, who probably will be taxed at the lower long-term capital gain rate, and approximately 40% for a foreign corporation. In addition, a foreign corporation might be subject to additional US tax known as the Branch Tax, which is a 30% tax applied to foreign companies that is the equivalent of the tax imposed on dividends paid by domestic corporation to foreign shareholders in the absence of an applicable US tax treaty. Further, any dividends that a US corporation pays to the nonresident shareholder of that corporation might be subject to US withholding tax on such dividends.

To ensure collection of such taxes from the foreign investors, FIRPTA requires any buyer, who transfers any US property to a foreign investor, to withhold 10% of the purchase price at closing and send it directly to the Internal Revenue Service (the "IRS"), instead of paying the full amount to the foreign seller. California has a similar statute, which requires the buyer to withhold 3 1/3% of the purchase price at closing and send it directly to the Franchise Tax Board (the "FTB"). Such payments are just an "advance payment" toward the foreign seller's US income tax obligation arising from the sale, and the foreign seller must file a US income tax return for the year of the sale by the applicable deadline.

Therefore, it is clear that a careful structure and tax planning of the real estate investment by a foreign investor is extremely crucial in order to avoid being subject to unnecessary tax issues in the future. In our next newsletter, we will discuss how to properly structure the real estate investment transaction.