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Business

Capital gains aren't always an easy call

Economic View

N. GREGORY MANKIW

What is carried interest? And why does it get the tax treatment it does?

These arcane questions are usually reserved for the green-eyeshade crowd. And for good reason: They can be so bewildering that they seem to be taken from an I.Q. test written just for accountants.

But because they concern a few very high-income individuals, including the presidential candidate Mitt Romney, for whom I am an adviser, they have been getting broader attention lately in the United States. So let's examine the issue.

Throughout almost the entire history of the U.S. income tax, the tax rate on capital gains has been lower than that on ordinary income. Today, the top rate is 15 percent for capital gains and 35 percent for ordinary income. There are good reasons for this — including, for example, the fact that capital gains are not indexed for inflation. But put that aside. If we are going to tax capital gains at a lower rate, one question necessarily arises: What is a capital gain, and how can we distinguish it from ordinary income?

U.S. tax law does not necessarily recognize time or sweat equity added to financial investments.

The answer seems simple. If you have a job, the money you are paid for your work is ordinary income. If you buy an asset at one time and sell it later for a higher price, the profit you made from holding it is a capital gain.

But is it really that easy? Consider five examples, and see if you can identify what is ordinary income and what is a capital gain:

- Abe buys a vacation home for his family for $800,000. Some years later, when his children have grown and left home, he sells it for $1 million. He makes $200,000.
- Bob is a real estate investor. After scouring the market for the best investment opportunities, he buys a house for $800,000 that he believes is undervalued. A few years later, he sells it at $1 million, for a profit of $200,000.
- Carl is a real estate investor and a carpenter. He buys a dilapidated house for $800,000. After spending his weekends fixing it up, he sells it a couple of years later for $1 million. Once again, the profit is $200,000.
- Dan is a real estate investor and a carpenter, but he is short of capital. He approaches his friend, Ms. Moneybags, and they become partners. Together, they buy a dilapidated house for $800,000 and sell it later for $1 million. She puts up the money, and he spends his weekends fixing up the house. They divide the $200,000 profit equally.
- Earl is a carpenter. Ms. Moneybags buys a dilapidated house for $800,000 and hires Earl to fix it up. After paying Earl $100,000 for his services, Ms. Moneybags sells the home for $1 million, for a profit of $100,000.

How much capital gains and ordinary income do we attribute to Abe, Bob, Carl, Dan and Earl? (To keep things simple, assume that Ms. Moneybags is untaxed. Think of her as running a pension fund or a university endowment.)

Let's take the easy cases first. It seems clear that Abe has a capital gain. His profit of $200,000 comes from simply holding an asset over time. And it seems equally clear that Earl's $100,000 is ordinary income. He is being paid for providing his services.

But between these cases, the situation gets murky. Bob and Carl are being rewarded in part for the time they spend, but the tax law treats both as having earned entirely through capital gains. The tax code does not count the time that Bob spent looking for investments as employment and his gain as taxable labor compensation, even though some of it arguably is. Nor does it try to tax Carl's sweat equity as labor compensation.

This brings us to Dan and his partnership with Ms. Moneybags. The tax law treats this partnership as exactly equivalent to Carl's situation. In this case, however, the $200,000 capital gain is divided into halves: Some of it goes to Ms. Moneybags, who provided the cash, and some goes to Dan, who provided the sweat equity. Once again, nothing is treated as ordinary income.

In some ways, this treatment makes sense. After all, Dan is doing half of what Carl did, so why should he have to pay a higher tax rate than Carl did on that half of his income? On the other hand, it seems that Dan is getting off easy. Dan does not seem very different from Earl, because both are getting $100,000 for fixing up the house.

If these examples leave your head spinning, you are not alone. Economists and tax lawyers who study these issues are unsure about the best way to

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ARIS MESSINIS/AGENCE FRANCE-PRESSE

A protester in a cloud of tear gas during clashes with the police last month near the Parliament in Athens, where lawmakers were debating further austerity measures.

A slow start and then near failure

BRUSSELS

2nd bailout for Greece called for bargaining, coaxing and good luck

BY LUKE BAKER AND SOPHIE SASSARD
REUTERS

Wolfgang Schäuble was playing sudoku on his iPad as he waited to hear whether Greece's negotiating team had persuaded private creditors to accept a bigger loss on their Greek bonds.

Mr. Schäuble, the German finance minister, needed this last piece of the debt restructuring puzzle to fall into place.

Without the private creditors — banks, insurers and investment funds — a €130 billion, or $172 billion, deal to save Greece from default could fall apart.

The consequences for the euro area could be catastrophic.

Mr. Schäuble finally got what he wanted only hours before dawn on Feb. 21, after negotiations that had run all night. What emerged was the world's biggest debt restructuring deal, an agreement affecting about €206 billion worth of Greek government bonds, according to the law firm Linklaters, which acted as an adviser.

During interviews with dozens of people involved in the seven months of talks involving banks, national governments, the European Union, the European Central Bank and the International Monetary Fund, a picture has emerged of how the agreement on Greece's second bailout came together — and how close it came to failing.

The discussions on Feb. 20 had gotten off to a slow start. Seated at a large table in a seventh-floor room of the Justus

MARIA MAROGIANNI/EUROPEAN PRESSPHOTO AGENCY

Charles H. Dallara, left, of the Institute of International Finance, and Jean Lemierre, a special adviser to the French bank BNP Paribas, played top roles in reaching a debt deal.

With each passing week came growth in the extent of the losses needed to ensure that Greece cut its debt.

Lipsius building in Brussels, ministers and advisers from the 17 euro zone countries haggled.

North European countries, in particular Germany and the Netherlands, took a hard line in demanding increased participation in the rescue by the private sector.

A deadline loomed for Greece to make a €14.5 billion debt repayment on March 20. Negotiators had been at that point before, several times.

The mood in the room on this occasion was one of determination that there must be a satisfactory conclusion.

"There was never a sense that it was going to implode or get derailed, but things did stall at times," said a senior official directly involved in the talks. Like others interviewed for this report, he was willing to speak only on condition of anonymity, as the content of the discussions remained confidential and both politically and financially sensitive.

The deal came seven months to the day after the first so-called private-sector initiative agreement with Greece's creditor banks.

That was the first of three attempts to resolve the private creditor part of the debt crisis that had exploded in late 2009, when Greece's incoming government had disclosed that public finance figures had hidden a huge black hole.

The contribution of the private sector was demanded by Chancellor Angela Merkel of Germany and her finance minister as the price for securing a second bailout for Greece by European governments.

In a first agreement, reached July 21, 2011, private creditors had accepted a 21 percent write-down on the value of their bonds.

But the agreement unraveled as Greece's economic plight worsened and the funding gap grew.

In another agreement, on Oct. 26, the figure rose to 50 percent, but that also failed to last.

By late February, representatives of Greece's private creditors, led by Charles H. Dallara, the managing director of the Institute of International Finance, were staring at even bigger losses.

Cast by some as villains, they sat along the corridor in a separate room, waiting to find out how much more in losses Greece and its main public-sector lenders would try to inflict on them.

With Mr. Dallara, a 62-year-old American, was Jean Lemierre, a special adviser to Greece's largest private-sector creditor, the French bank BNP Paribas, and one of the most experienced debt restructuring negotiators in the business.

For Mr. Lemierre, whose experience included leading the so-called Paris Club of creditors that successfully negotiated the restructuring of Latin American and African debt, these were by far the most drawn-out and complicated talks of his career. He had been brought in to help the creditors negotiate after the deal reached in October had fallen through.

Every time a new agreement came close, there would be more bad news about the state of the Greek economy, and the carefully negotiated figures would have to be recalculated to fit with the increasingly gloomy forecasts coming from the I.M.F., one of the main parties at the table.

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Spain warns it won't be able to reach deficit goal

BRUSSELS

Announcement at end of E.U. meeting adds to fears over crisis recovery

BY STEPHEN CASTLE

A European summit meeting that had looked to be surprisingly routine after two years of crisis nevertheless ended with another test for the credibility of the euro zone Friday, when Spain announced that a deepening recession meant it would have to abandon its deficit-reduction targets for this year.

Coming on the day that 25 European leaders signed a new fiscal pact designed to further enshrine budgetary discipline, the unexpected announcement from the Spanish prime minister, Mariano Rajoy, illustrated how many European economies remained trapped between the need to repair their finances and an opposing pressure to restore economic growth.

Though markets have calmed in recent weeks, largely thanks to the action of the European Central Bank, leaders gave differing verdicts on whether the crisis was behind them or whether the euro zone had just bought valuable time to shore up the currency.

Spain's predicament is a reminder of how, in several countries, the austerity measures that evolved from the debt crisis have eroded confidence and reduced growth, thereby making it harder to escape a downward spiral.

Without discussing his budget plans in detail with fellow European leaders, Mr. Rajoy set himself a target for 2012 of a deficit equivalent to 5.8 percent of gross domestic product, arguing that this was more realistic than the original goal of 4.4 percent. Mr. Rajoy said he was acting within guidelines because Spain still intended to hit the European Union's public deficit goal of 3 percent of G.D.P. in 2013. On Monday, the Spanish government said that its budget deficit in 2011 was 8.5 percent, well above its 6 percent goal.

"I'm backing austerity and aim to reduce the deficit from 8.5 percent to 5.8 percent; that's significant austerity," Mr. Rajoy said after a two-day summit meeting in Brussels ended Friday, adding that he did not consult other European leaders about a step he described as a "sovereign decision by Spain."

Though there was some support for Mr. Rajoy, on the grounds that he still intended to hit the 2013 target, his decision to make an announcement, rather than negotiating first with the bloc's executive branch, the European Commission, was seen by some as a political misstep.

In 2009, Spain was given an extra year to meet its targets, and the unilateral move now could make it more difficult for the commission, which polices budget policy, to show further leniency when countries like Germany are preaching strict adherence to the rules to preserve the euro.

"Rajoy is still a bit inexperienced," said one official not authorized to discuss the issue. "He thinks that most of the people around the table are political allies who will support him. But here you put your political considerations away because the dynamic that counts is that of national interests."

In recent months, E.U. governments have negotiated what at least on paper amounts to an even tougher fiscal compact, promising to write into their national law a commitment to balanced budgets. They have also rewritten the

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Twitter lightens the load for tracking quirks of U.S. dialects

NEW YORK

BY JENNIFER SCHUESSLER

To scholars and linguists, the Dictionary of American Regional English is an invaluable guide to the way Americans not only speak but also live — a homegrown answer to the Oxford English Dictionary, served up with heaping sides of "slump" (cobbler), "turkey cheese" (cottage cheese) and "wapatuli" (a potent Wisconsin punch).

It was based largely on research by a team of fieldworkers who fanned out across the United States some 50 years ago in vans called Word Wagons, querying Americans about their ways of talking about kitchen implements, farm animals, bodily ailments, misbehaving children, stupid neighbors and more.

The linguists of the future, however, may not have to go to such literal lengths to find geographical variations in speech. According to a paper delivered at an annual meeting of the American Dialect Society in January by Brice Russ, a graduate student at Ohio State University, the 200 million or so messages posted each day in the supposedly placeless world of Twitter may end up being a rich source of information about regional difference.

So far, the sheer number of words on the site has proved daunting.

"You see computational linguists using Twitter to predict box-office revenues and opinion polls or to do sentiment analysis," Mr. Russ said by telephone. "But when it comes to answering the more traditional kinds of questions linguists look at, people are still trying to figure out what to do with so much data."

To demonstrate the validity of Twitter-based research, Mr. Russ searched

The 200 million or so messages posted daily can be a rich source of insight on how Americans talk.

through an estimated 400,000 Twitter posts coming from identifiable locations and zeroed in on three different linguistic variables, starting with the regional distribution of "soda" versus "pop" or "Coke," something that has been well studied by scholars and amateurs alike.

Next, he tracked the use of "hella," an intensifier (as in "hella boring") that is associated with Northern California but whose regional distribution has been examined only anecdotally. Finally, he looked at the well-documented syntactic construction "needs X-ed" (as in "the car needs washed"), which is especially common around Pittsburgh.

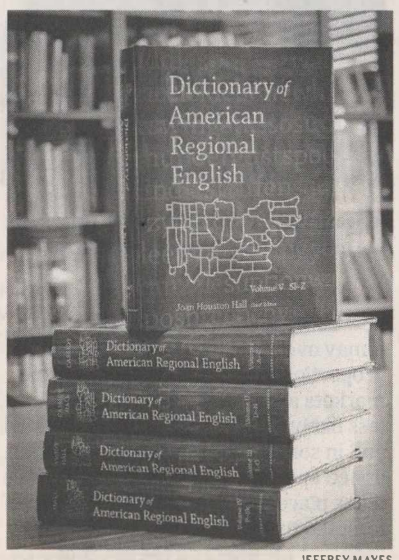
Mr. Russ's results for carbonated beverages, plotted onto a Google map, track closely with previous research, with "pop" predominant from the Midwest to the Pacific Northwest, "Coke" predominant in the South and "soda" ruling the Northeast and Southwest while also cropping us elsewhere. But his map for "hella" shows the word leapfrogging up the West Coast to Seattle (and, more puzzlingly, popping up in St. Louis and Kansas City, Missouri).

"People may be moving up the coast, bringing it with them," he said, adding that he was utterly confounded by the "hella" hotspots.

As for the "needs X-ed" construction, Mr. Russ detected hints of a southward drift since it was studied in the mid-1990s, though he was cautious about drawing firm conclusions.

"There could have been diffusion southward," he said. "Or I may have just caught something that the previous research missed."

Mr. Russ is not the first to use digital media to study regional language variation. At a meeting last year of the Linguistic Society of America, a team from



JEFFREY MAYES

Twitter could supplement the fieldwork required for standard linguistic studies.

Carnegie Mellon University presented a paper showing that a Twitter user's location could be predicted to within 300 miles, or 480 kilometers, by tweets alone. The Lexicalist, a project begun in 2010, has analyzed millions of words on the Internet to map usage patterns according to various demographic factors. And a dialect survey led by Bert Vaux, formerly of Harvard, used online surveys to map different names for sneakers (or "gym shoes" in Illinois), varying pronunciations of "aunt" or "crayon," and answers to questions like, "What do you call a drive-through liquor store?" (Most popular answer: "I have never heard of such a thing.")

Twitter, whose users are often younger, more urban and less white than Internet users in general, does provide some methodological challenges to researchers, Mr. Russ acknowledged.

Among other things, he noted, it shows only where users are now, not where they are from originally. But it may allow them to track linguistic patterns on a vast scale and in something close to real-time, identifying phenomena that can then be investigated more deeply by traditional fieldwork.

Mr. Russ emphasized that Twitter-mining was unlikely to replace the kind of old-fashioned, on-the-ground word hunting that produced the Dictionary of American Regional English.

"The 'bobbasheelys' and 'crawdads' of English don't always show up on Twitter often enough to be mapped on a large scale," he said, referring to two of the dictionary's classic entries.

Spain says deficit goals won't be met

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euro zone rule book to make it more difficult for countries that break the rules to avoid financial sanctions.

Since the old rules were repeatedly flouted, the credibility of this new system is now very much under scrutiny.

So far, the commission has said it cannot rule on the Spanish case until it has more information about why the country will miss its deficit targets, and until it has seen its next budget proposals. On Thursday, however, the commission took a tough line with the Netherlands, which also announced that its budget shortfall next year would miss its goal, at 4.5 percent of G.D.P. That would match the expected outcome for this year, but is below its original target of 3 percent.

The controversy over Spain's public finances cast a shadow over a meeting that some leaders had tried to present as a return to normality after a series of frenzied meetings over the past two years, some of which ended around dawn.

This time, leaders wrapped up their discussions, which began with dinner, by 11 p.m. on Thursday and concluded the Friday session by midday.

When asked whether she was relieved to be at a summit meeting where she could be in bed by midnight, Chancellor Angela Merkel of Germany joked that she was "with you all until midnight," referring to her late-night, off-the-record discussions with German journalists. "It could have been worse," she added.

Leaders struck a somewhat different tone over the extent to which they believed the crisis had abated after the injection of some €1 trillion, or $1.3 trillion, into euro zone banks in recent months by the E.C.B., and a provisional agreement on a second package of loans for Greece worth €130 billion, or $172 billion.

"It is not a 100 percent guarantee," said President Nicolas Sarkozy of France, "but we are in the process of coming out of the crisis." By contrast, Mrs. Merkel struck a more cautious note. "We are not living in ordinary times. We are in a fragile situation," she said. Much progress has been made, she added, "but to say the situation is not all that dire would be wrong."

Final agreement on the Greek bailout is still required and Germany itself is under pressure to agree to expand the euro zone bailout fund. One proposal, to run the temporary fund alongside its permanent €500 billion replacement, had been scheduled for discussion at the meeting but was postponed. This idea, which could generate a total fund of around €700 billion, is now likely to be decided before the spring meeting of the Group of 20 finance ministers, according for one senior official who requested anonymity because of the sensitivity of the issue.

Paul Geitner contributed reporting.

The twists behind the Greek debt deal

GREECE, FROM PAGE 9

Days before their session of Feb. 20, euro zone finance ministers had canceled a meeting at the last minute. The intention had been to turn up the heat on the Greek government to force it to agree to more austerity measures. The plan had worked. Now was the moment to reach a deal with the private creditors.

But negotiation fatigue was setting in, and another bleak report from Greece's international lenders had highlighted another likely gap in its funding, further muddying the waters.

With leadership needed, it was the Dutch finance minister, Jan Kees de Jager, who got the talks moving, the senior official said.

"He was very focused on how to close the gap between the 136 billion funding requirement and the 130 we needed to get it down to," said the senior official directly involved in the talks, speaking in euro terms and referring to the €130 billion that negotiators were aiming for.

One of Greece's sternest critics in public, in private Mr. de Jager was intent on pushing the deal through. The role he played demonstrates the degree of brinkmanship that was involved in the months of hard negotiations. Just days before agreement was finally reached, Mr. de Jager had publicly threatened to vote against it.

To get the dialogue going and to put pressure on the private creditors to forgive more of Greece's debt, a small contact group, including the E.C.B. board member Jörg Asmussen, shuttled between the main room and the room where Mr. Dallara, Mr. Lemierre and their advisers were waiting.

The creditors had tried to draw a line when they had said they would not accept a write-down of more than 50 percent.

But they knew a disorderly Greek default would inflict tremendous damage on their investments and their business.

"The talks with the banks were very tough," Mr. de Jager said. "It went up and down several times, and time and again we had to send the negotiating team back to get a better deal."

The months from July 2011 to February 2012 had seen numerous meetings in Brussels, Paris and Athens. Mr. Dallara had spent much of his time working at the Grande Bretagne Hotel in Athens. From there, he and his team had a view of the worst anti-austerity rioting to have scarred the Greek capital so far.

Members of the steering committee of the private-sector lenders said they had never felt threatened during their stays in Athens. Their biggest complaint was the long periods of waiting for meetings with the Greek negotiators. For despite its prime spot on Syntagma Square and its view of the Parthenon and the Parliament building, the hotel was a gilded prison. Members of the team soon tired of eating every meal there, as they waited for the Greek prime minister, Lucas D. Papademos, to summon them.

One day they took time to visit the Acropolis, and Mr. Dallara occasionally went out shopping, returning with books to help fill the time between meetings. Greek negotiators called off one such meeting at the last minute, adding to the tension.

The figure of Josef Ackermann, the chairman of the Institute of International Finance, was always in the background, at the end of the telephone line when Mr. Dallara needed him.

"The talks with the banks were very tough. It went up and down several times, and time and again we had to send the negotiating team back."

Mr. Ackermann, who is also the chief executive of Deutsche Bank, stuck to his agenda during a crucial phase of the talks in late January and attended the World Economic Forum in Davos, Switzerland. Mr. Dallara skipped the event, his badge unclaimed at the parties to which he had been invited.

Mr. Ackermann's line to Mrs. Merkel was also important at main points during the discussions.

For the banks and insurers, a low point in the negotiations came early last December, at a meeting in Brussels.

The private creditors were joined by officials from the European Union, the I.M.F., the E.C.B., the German and French Finance Ministries and the Greek government.

Representing Athens were Petros Christodoulou, the head of the Public Debt Management Agency, and two debt restructuring specialists. They were Lee C. Buchheit, of the law firm Cleary Gottlieb Steen & Hamilton, and his former colleague, Mark Walker, who had left the firm for Lazard, the investment bank, in June.

Greece, supported by the I.M.F. and its mission chief to the country, Poul Thomsen, was now proposing a deal that would leave private creditors swallowing losses deeper than the 50 percent they had agreed to, according to one of the participants, who spoke on condition of anonymity because of the sensitivity of the talks.

"People were shocked at how far apart we were in the proposals," the participant in the meeting said later.

Vega Asset Management, the sole fund representative on the committee, resigned not long afterward.

As the talks continued in the ensuing weeks, Greece's three-year recession deepened, toughening the I.M.F.'s stance on the size of the loss that was coming for creditors.

With each passing week came growth in the extent of the losses needed to ensure that Greece cut its debt as a proportion of gross domestic product. The I.M.F. had set Greece a debt-to-G.D.P. goal of 120 percent.

Some government negotiators were starting to despair.

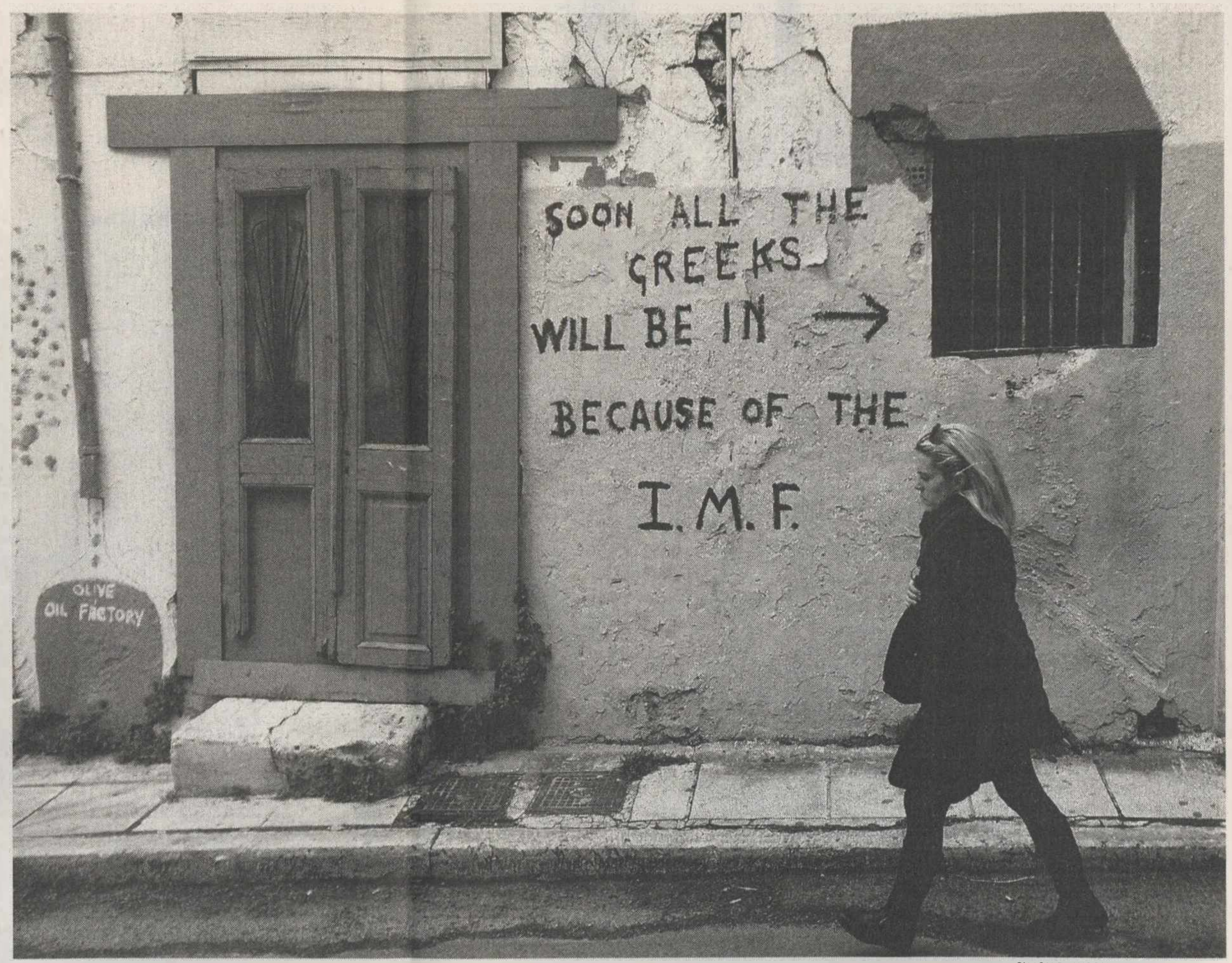
A change came with the arrival Nov. 1 of a new president at the E.C.B., which throughout the euro zone debt crisis had resisted calls from the United States and others to act as lender of last resort.

At a stroke, the new president, Mario Draghi, dispelled much of the pessimism in December, initiating a three-year money line to banks that pumped nearly half a trillion euros into the financial system.

At the last moment, the E.C.B. also moved to secure a second Greek bailout, agreeing to forgo the profit it had made on its Greek government bond holdings and return them to its stakeholders — the euro zone member states — to pass back to Athens. That proved crucial in persuading the I.M.F. that the package added up and would put the debt-to-G.D.P. target of 120 percent within reach by 2020.

The E.C.B. money meant that by February, the banks were in a much more optimistic mood and a deal was once again possible.

Sophie Sassard reported from London.



SIMON DAWSON/BLOOMBERG NEWS

A neighborhood in Athens. Public resentment is high in Greece because of the severe belt-tightening demands of international lenders.

Pakistan goes public with plan to censor Web

PAKISTAN, FROM PAGE 1

the technology "should be able to handle a block list of up to 50 million URL's (concurrent unidirectional filtering capacity) with processing delay of not more than 1 milliseconds."

Following the Arab Spring, which demonstrated the power of the Internet to help spread political and social change, Pakistan's move to clamp down has set off a storm of protest among free-speech groups in the country and beyond.

Opponents of censorship say they are doubly appalled because they associated this kind of heavy-handed approach more with the previous regime of Gen. Pervez Musharraf than with the current government of President Asif Ali Zardari.

"The authorities here are big fans of China and how it filters the Internet," said Sana Saleem, chief executive of Bolo Bhi, a group that campaigns against restrictions on the Internet. "They overlook the fact that China is an autocratic regime and we are a democracy."

"What makes this kind of censorship so insidious is that they always use national security, pornography or blasphemy as an explanation for blocking other kinds of speech," Ms. Saleem said, adding that her site had been blocked for several months in 2010 when it made reference to a ban on Facebook. Access to the social networking service had been restricted because of a page featuring a competition to draw the prophet Mohammed — something that is considered blasphemous by Muslims.

The Technology Ministry's Research and Development Fund says in its tender that the Internet filtering and blocking system will be "indigenously developed," but campaigners like Ms. Saleem say they think it is likely the agency will try to adapt Western technology for the purpose.

To try to prevent this from happening, Ms. Saleem wrote to the chief executives of eight international companies that make Net filtering technology, asking them to make a public commitment not to apply for the Pakistani grant.

On Friday, one of them, Websense, which is based in San Diego, responded, declaring in a statement on its Web site that it would not seek the contract.

"Broad government censorship of citizen access to the Internet is morally wrong," Websense said. "We further believe that any company whose products are currently being used for government-imposed censorship should remove their technology so that it is not used in this way by oppressive governments."

Websense had previously withdrawn the use of its technology from Yemen after facing accusations from the OpenNet Initiative, a U.S.-Canadian academic group, and other organizations that it had been used by the government of that country to stifle political expression on the Internet.

Governments around the world buy filtering and blocking technology to root out illegal content like child pornography. Some private companies employ it to restrict access to social networks and other distractions on company computers.

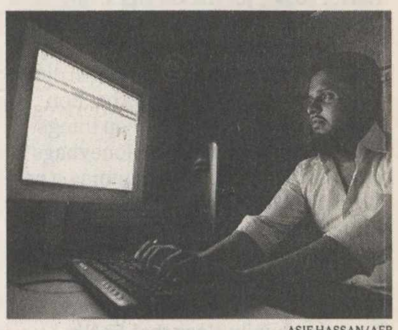
But the use of Western technology to rein in political speech in countries with repressive regimes has come under increasing scrutiny since the Arab Spring. The OpenNet Initiative said in a report last year that at least nine governments in the Middle East or North Africa had used such products, with the Western companies maintaining lists of sites to be blocked, including sites featuring skeptical views of Islam and even dating services.

Even before implementing its new system, Pakistan has been an active censor. The country was 151st, out of 179, on a ranking of media freedom by the Paris-based group Reporters Without Borders in 2011.

"Reporters Without Borders urges you to abandon this project, which would reinforce the arsenal of measures for communications surveillance and Internet censorship that have already been put in place by your government," the group wrote in a letter Friday to Prime Minister Yousaf Raza Gilani.

To free-speech advocates in Pakistan, the government's seeming insouciance about censorship is a particular cause for alarm.

"This is a case study," said Ms. Saleem of Bolo Bhi, which is based in Karachi and whose name means "speak up." "No government has ever done this so publicly."



ASIF HASSAN/AFP

An Internet cafe in Karachi, Pakistan. The government is seeking an automatic blocking and filtering system like China's.

A step back in '11 for U.S. home prices

Floyd Norris

OFF THE CHARTS

Home prices in the United States, which seemed to begin to recover in 2009, fell to new lows in 2011, according to the Standard & Poor's/Case-Shiller index of prices.

Seattle and Atlanta were among the metropolitan areas where prices have fallen the most since the national market seemed to hit bottom.

"Prices peaked in Seattle after the rest of the United States, so Seattle is a little bit behind in the correction that will bring prices back in line with income levels," said David Stiff, the chief economist of Fiserv, which collects the data and calculates the Case-Shiller indexes. Foreclosures are rising there, as they are receding in some areas where problems appeared earlier.

As can be seen in the accompanying charts, 5 of the 20 markets tracked by the Case-Shiller indexes peaked in 2007. Four of them — Seattle; Atlanta; Charlotte, North Carolina; and Portland, Oregon — are down at least 7 percent from the spring of 2009. Only Dallas has held up relatively well.

Dallas was also a special case during the housing boom, with prices rising more slowly than in any other market except Detroit. One reason for both its slow ascent and subsequent slower fall may be that refinancing mortgages was harder in Texas, because of state laws. That meant there was less money available to bid up prices in good times, and there were fewer homes worth less than was owed when the bad times arrived.

Detroit home prices have also done relatively well in recent months. In 2011, prices there rose a small amount, making it the only market to show a gain for the year.

Some of the markets where speculation was heaviest seem to be recovering. Prices in all three California markets are still higher than they were in the spring of 2009, and prices in Phoenix, Arizona, fell less in 2011 than they did in most markets. But Las Vegas, perhaps the most speculative market during the boom, is still suffering. Prices there have fallen nearly 20 percent since the spring of 2009, more than in any other market.

It is possible that the U.S. home price situation is not as bleak as portrayed by the Case-Shiller indexes. A major challenge for any home price index is assuring comparability. Case-Shiller does that by comparing prices of homes with the prices of the same homes when they were previously sold.

The risk is that such comparisons may overlook changes to the home between transactions. During the boom, that meant the index might overstate gains because a home had risen in value in part due to the addition of a new bedroom or swimming pool. Now, it may overstate losses because a disproportionate portion of sales in some markets are foreclosures, which are less likely to have been well maintained and in some cases may have been abandoned and vandalized before a new sale takes place. Mr. Stiff said Fiserv had attempted to minimize that problem by reducing the effect on the index of home sales that appear to show unusually large increases or decreases.

Another national index, maintained by the Federal Housing Finance Agency, showed a smaller decline in prices in 2011, with prices hitting bottom in February before rising a little late in the year. That index is based on data from Fannie Mae and Freddie Mac, which are regulated by the finance agency.

ELAINE THOMPSON/AP

A Seattle house that sold. Home prices fell the most in the Seattle and Atlanta regions.

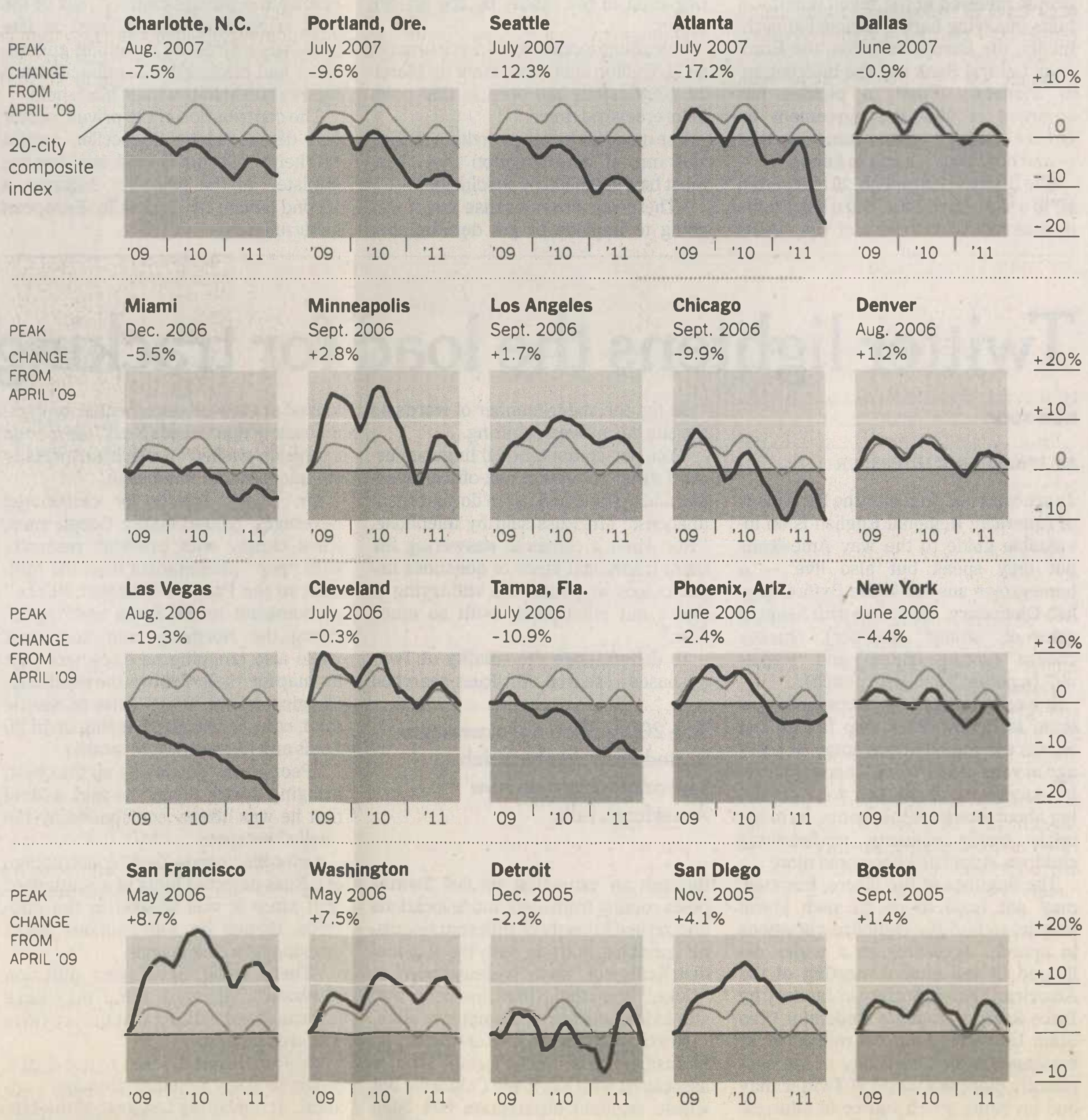
U.S. home prices resume fall

Home prices in most parts of the United States appeared to bottom out in the summer of 2009 and to begin a slow recovery. But now they have fallen below 2009 levels in most markets, according to the Standard and Poor's/Case-Shiller indexes released in the past week. Markets where prices peaked in 2007, rather than earlier, generally seem to be suffering the most now.

S. & P./CASE-SHILLER 20-CITY COMPOSITE INDEX

Change from January 2000

S. & P./CASE-SHILLER INDEXES *Change from April 2009 to December 2011*



Source: Standard & Poor's/Case-Shiller

Note: Data are not seasonally adjusted