Capital and Credit

# Addressing the *Perfect Storm* of Pro-cyclical Regulatory Proposals and the Wave of Maturing CRE Debt

## Issue

There is growing concern about the potential for a *perfect storm* of regulations that could stall credit markets and impair capital formation – particularly for the $5.5 trillion commercial and multifamily debt market. While well-intentioned, we are concerned that the proposals – particularly the *Basel III Endgame* – could increase the cost of credit, diminish lending capacity, and undermine the essential role banks play in lending and financial intermediation for real estate. These proposed regulations come at a significant economic cost without clear benefits to the resiliency of the financial system. In addition to the proposed capital increases for banks, the Securities and Exchange Commission (SEC) has a number of proposed rulemaking measures that could have a chilling effect on real estate capital markets that could further impair liquidity and be a "death by a thousand cuts" for commercial real estate capital markets. It is important for policymakers to be mindful of how all these regulations interact.

There are $1.5 trillion of commercial real estate loans maturing in the next three years. The bulk of these loans were financed when base rates were near zero. They now need to be refinanced in an environment where rates are much higher, values are much lower, and in illiquid markets. For over a decade, with interest rates close to or at zero, loans were conservatively underwritten, with strong debt service coverage and low loan values. As the Fed has increased rates to fight inflation, we are now in an entirely different environment. Liquidity has contracted, and values have declined. Many of these loans will require additional equity, and borrowers will need time to restructure this debt. Capital formation is vital when credit markets tighten to help restructure maturing debt and fill the equity gap.

## The Roundtable's Position

- The $20.7 trillion commercial (CRE) and multifamily (MF) commercial real estate market is financed with $5.5 trillion of debt[1], 50.3% of which is provided by commercial banks. Of that outstanding debt, some $1.5 trillion of CRE and MF debt is maturing over the next

[1] Federal Reserve, Trepp.

three years (2023, 2024, 2025). Smaller banks hold approximately $2.3 trillion in commercial real estate debt.[2]

- As requested in The Real Estate Roundtable's March 17, 2023[3] letter, the June 30, 2023 *Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts* has reestablished a program similar to prior programs in 2009[4], 2010[5], 2020[6] that **calls for** "financial institutions to work prudently and constructively with creditworthy borrowers during times of financial stress."
- While this policy statement is helpful, additional steps are called for to help restructure and transition the ownership and financing of commercial real estate from a period of low rates and robust markets to a time of higher rates, declining credit capacity and uncertain economic growth. It also attempts to update the approach for the post-pandemic era, as increased remote working is shifting demand for commercial properties in ways that can adversely affect the financial condition and repayment capacity of borrowers.
- The 2023 *Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts* helps to renew the flexibility the regulators provided which allowed lenders to work with their borrowers more effectively during times of economic stress. It also attempts to update the approach for the post-pandemic era, as increased remote working is shifting demand for commercial properties in ways that can adversely affect the financial condition and repayment capacity of borrowers.
- The potential significant increase in capital requirements for large banks' capital market activities due to the *Basel III Endgame* could materially reduce the depth of banks' products and services

[2] Trepp data cited in the *Wall Street Journal*

[3] Roundtable Urges Federal Bank Regulators to Reestablish CRE Troubled Debt Restructuring Program, March 17, 2023, https://www.rer.org/policy-issues/policy-comment-letters/detail/roundtable-urges-federal-bank-regulators-to-reestablish-cre-troubled-debt-restructuring-program

[4] Policy Statement on Prudent Commercial Real Estate Loan Workouts, FIL-61-2009, October 30, 2009, https://www.fdic.gov/news/financial-institution-letters/2009/fil09061.html

[5] Meeting the Credit Needs of Creditworthy Small Business Borrowers, FIL-5-2010, February 12, 2010, https://www.fdic.gov/news/financial-institution-letters/2010/fil10005.html

[6] Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus, March 22, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20200322a1.pdf

# Addressing the *Perfect Storm* of Pro-cyclical Regulatory Proposals and the Wave of Maturing CRE Debt

offerings to the real estate sector, which will in turn lead to increased cost of raising capital and hedging risk for the industry. As a result, we anticipate that the industry could encounter difficulties in their access to liquidity and affordable funding to fuel growth and create jobs.

- While intended to "support financial stability" in the event of more bank failures, the August 29 Notice of Proposed Rulemaking from U.S. regulatory agencies would require large regional banks to increase their long-term debt (LTD) issuance by roughly 25 percent through the issuance of roughly $70 billion in fresh debt. They would also be required to reinforce their so-called living wills.
- The largest U.S. banks' capital and liquidity levels have grown dramatically since the original Basel III standards were implemented in 2013 in response to the 2008 Global Financial Crisis. Since 2009, Tier 1 capital has increased by 56 percent and Common Equity Tier 1 capital has tripled. Today, as the Federal Reserve recently observed, the U.S. "banking system is sound and resilient, with strong capital and liquidity."[7]
- While well-intentioned, we are concerned that the proposals could increase the cost of credit, diminish lending capacity and undermine the essential role banks play in lending and financial intermediation for real estate. The proposed increases in capital requirements come at a significant economic cost without clear benefits to the resiliency of the financial system.
- In addition to the proposed capital increases for banks, the Securities and Exchange Commission (SEC) has a number of proposed rulemaking measures that could have a chilling effect on real estate capital markets – e.g., the broadly drafted Conflicts of Interest in Securitization Rule; Rule 15c2-11; Private Fund; Custody Rule and others – that could further impair liquidity and be a "death by a thousand cuts" for commercial real estate. Capital formation is vital when credit markets tighten to restructure maturing debt.

[7] [1] https://www.federalreserve.gov/publications/files/svb-review-20230428.pdf

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# Commercial Insurance Coverage in an Evolving Threat Environment

## Issue

The proliferation of natural catastrophe and pandemic threats has raised concerns about commercial insurance coverage for commercial real estate. As economic losses caused by disasters increase, changing exposures around the world must be addressed in order to effectively manage natural catastrophe risk. These concerns have highlighted the lack of—and need for—insurance capacity and various lines of commercial insurance. Expanding coverage gaps and increased costs present challenges for businesses across many industries, including real estate. A lack of adequate coverage will lead to economic uncertainty, harm stakeholders and undermine the growth of communities.

Pandemic-related coverage in various lines of commercial insurance has been withdrawn or restricted going forward. Additionally risks from natural disasters like floods, hurricanes, wildfires, hail, tornadoes, and drought cost the U.S. billions of dollars each year. If policyholders are able to find coverage for these various lines, the pricing has increased dramatically, raising economic concerns.

Without adequate coverage, the vast majority of these natural catastrophe and pandemic-related losses are likely to be absorbed by policyholders. These widening coverage gaps and price hikes, raise serious economic concerns about protection gaps, coverage capacity, and increased costs for natural catastrophe and some pandemic-related business interruption losses. The COVID-19 pandemic exposed and exacerbated a protection gap in what the business and non-profit sectors assumed to be a resilient financial protection system of commercial insurance. The budget debate in Congress has raised concerns about the future of the National Flood Insurance Program, which is subject to temporary funding extensions and now must be reauthorized by November 17, 2023.

It is important to find solutions to fill these commercial insurance gaps across changing threat pattern. Whether they be related to natural catastrophe or pandemic risk, it is important to find a solution—either market based or with the partnership of the federal government—that will provide the economy with the coverage it needs to address catastrophic events.

The Roundtable, along with its industry partners, continues to work constructively with policymakers and stakeholders to develop and **enact an effective pandemic risk program**. We also continue to work with our industry partner organizations to advocate for an **improved National Flood Insurance Program (NFIP)** that can be re-authorized for a lengthy time period.

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# Commercial Insurance Coverage in an Evolving Threat Environment

The Roundtable works with the Business Continuity Coalition (BCC), which represents a broad range of business insurance policyholders from across the American economy to develop an **effective pandemic insurance program** that protects jobs by ensuring business continuity from economic losses. The Roundtable works with the BCC and policymakers, the administration, and other U.S. stakeholders.

A long-term reauthorization of the **National Flood Insurance Program (NFIP**) is essential for residential markets, overall natural catastrophe insurance market capacity, and the broader economy. The NFIP's commercial property flood insurance limits are low—$500,000 per building and $500,000 for its contents – so it is important to exempt larger commercial loans from the mandatory NFIP purchase requirements.

The National Flood Insurance Program (NFIP) is currently operating under a continuing resolution. Since the end of FY 2017, over a dozen short-term NFIP reauthorizations have been enacted. As policymakers continue to debate potential changes and improvements to the program, their challenge is to find a balance between improving the financial solvency of the program, reducing taxpayer exposure, and addressing affordability concerns. Without congressional reauthorization, the program will sunset on September 30, 2023.

## The Roundtable's Position

- Floods are the most common, costliest natural peril in the U.S. The NFIP was enacted in 1968 due to a lack of private insurance and increases in federal disaster aid. The Program is administered by the Federal Emergency Management Agency (FEMA) and is essential for homeowners, renters, and small businesses in affected areas.
- The level of flood damage from recent storms makes it clear that FEMA needs a holistic plan to prepare the nation for managing the cost of catastrophic flooding under the NFIP.
- The NFIP is important for residential markets, overall natural catastrophe insurance market capacity, and the broader economy. However, under the NFIP, commercial property flood insurance limits are low—$500,000 per building and $500,000 for its contents. NFIP has approximately five million total properties, only 6.7% are commercial. Nearly 70% of NFIP is devoted to single-family homes and 20% to condominiums. In the total program, 80% pay actuarial sound rates, however, in the commercial space, only 60% pay actuarial sound rates.

# Commercial Insurance Coverage in an Evolving Threat Environment

- Congressional hearings have illuminated numerous acute problems surrounding the NFIP, such as insolvency, increased risk of flooding across the country, and insufficient and inaccurate flood mapping. The unintended negative outcomes generated by the NFIP continue to grow and are now spreading to GSEs (government-sponsored enterprises) Fannie Mae and Freddie Mac.
- Lenders typically require base NFIP coverage, and commercial owners must purchase Supplemental Excess Flood Insurance for coverage above the NFIP limits. The NFIP's low commercial limits make it problematic for most commercial owners. As a result, The Roundtable has been seeking a voluntary exemption for mandatory NFIP coverage if property owners have flood coverage from commercial insurers.
- By permitting certain private issue insurance policies to satisfy the NFIP's "mandatory purchase requirement" for properties in flood plains financed by loans from federally guaranteed institutions, commercial property owners would have the ability to "opt-out" of mandatory NFIP commercial coverage if they have adequate private coverage outside the NFIP program to cover financed assets.
- The Roundtable and its partner associations support a long-term reauthorization and improvements of the NFIP that help property owners and renters prepare for and recover from future flood losses. Given the low coverage amounts provided to commercial properties, it is important to permit larger commercial loans to be exempt from the mandatory NFIP purchase requirements.
- Going forward, it is important to protect American jobs and to ensure a sustainable and speedy economic recovery from future natural catastrophe events and government-ordered shutdowns. If not remedied, these insurance gaps could hinder economic growth.
- The Roundtable is working with industry partners, stakeholders, and policymakers through the Business Continuity Coalition (BCC) to develop and enact an effective, prospective federal public-private backstop program for pandemic risk insurance coverage across a variety of commercial insurance lines. Similar to the Terrorism Risk Insurance Act (TRIA) enacted the year following the 9/11 attacks, this program would provide the economy with the coverage it needs to provide businesses with pandemic-related coverages in the face of a future pandemic.
- Senate Subcommittee on Securities, Insurance, and Investment members, Kyrsten Sinema (D-AZ), and Thom Tillis (R-NC) are working along with other Banking Committee

members to develop bipartisan legislation pandemic risk insurance program in the Senate. The BCC is working with this bipartisan working group with the goal of introducing legislation in the Senate.

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# Beneficial Ownership & Corporate Transparency Act

## Issue

Under the Corporate Transparency Act (CTA), many U.S. businesses will soon be required to disclose information on their "beneficial owners" under regulations issued (and to be issued) by the Treasury Department's Financial Crimes Enforcement Network (FinCEN). This disclosure obligation begins on January 1, 2024. The stated goal of the CTA is to prevent and combat money laundering, terrorist financing, corruption, tax fraud, and other illicit activity by requiring companies to disclose beneficial ownership information, or BOI, to FinCEN, a bureau of the U.S. Department of the Treasury.

The Rule imposes heavier compliance burdens on real estate businesses with numerous legal entities that own and operate real property across all asset classes. While the CTA and its implementing regulations are not specifically targeted to real estate businesses, it will have a direct impact on the industry. As discussed below, certain types of entities will be exempt from the reporting requirements; however, these exemptions will not apply to many typical real estate limited liability companies and partnerships formed to own and operate commercial properties.

The CTA requires reporting companies to supply three categories of information: information about the entity, BOI, and information about the company applicant. Each reporting company will have to provide information on its "beneficial owners" as well as the "company applicants" involved in forming the entity. A beneficial owner refers to an individual who owns at least 25% of an entity or indirectly exercises "substantial control" over it.

## The Roundtable's Position

- The Roundtable and a broad coalition representing millions of businesses throughout the country wrote to House Financial Services Committee Chairman Patrick McHenry (R-NC), in strong support of his legislation—the *Protecting Small Business Information Act of 2023* (H.R. 4035). McHenry's bill would delay the date when the *Corporate Transparency Act's* (CTA) beneficial ownership reporting requirements go into effect, currently scheduled for Jan. 1, 2024.

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# Beneficial Ownership & Corporate Transparency Act

- There is significant concern about the CTA's far-reaching scope and its **impact on many commercial residential real estate businesses** that use the LLC structure for conducting business. The coalition's letter states that Chairman McHenry's bill "legislation offers a commonsense solution to this pending regulatory trainwreck."

- The CTA amended the *Bank Secrecy Act* to require corporations, limited liability companies, and similar entities to report **certain information about "beneficial owners"** who own at least 25% of an entity or indirectly exercise "substantial control" over it.
- The CTA authorizes the Treasury's Financial Crimes Enforcement Network (FinCEN) to collect and disclose beneficial ownership information to authorized government authorities and financial institutions, subject to effective safeguards and controls. The statute requires the submission of regular reports to the federal government that include **a litany of sensitive personal identifiers of the owners, senior employees, and/or advisors of covered entities**.
- Although the measure is intended to provide support for law enforcement investigations into shell companies engaged in money laundering, tax evasion, and terrorism financing, it places many costs and legal burdens on small businesses, especially those in the real estate industry.
- In 2021, The Roundtable and its coalition partners submitted detailed comments to FinCEN regarding the development, disclosure, and maintenance of a new federal registry that will contain beneficial ownership information.
- The real estate coalition's extensive comments emphasize the "scope of the CTA is far-reaching and will impact many commercial residential real estate businesses who are frequent users of the LLC structure for conducting business. If not implemented with a clear set of rules and regulations, the CTA could result in an outcome of confusion, missteps, and ultimately fines on law-abiding businesses."
- The Roundtable is also part of a broad coalition of business trade groups that supports a National Small Business Association legal challenge (*NSBA v. Janet Yellen*) on the constitutionality of the *Corporate Transparency Act (CTA),* which became law in Jan. 2021.

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# Beneficial Ownership & Corporate Transparency Act

- The coalition's comments detail "concerns and recommendations for establishing regulations to implement reporting requirements—as well as provisions regarding FinCEN's maintenance and disclosure of reported information effectively and fairly."
- The coalition raised several specific implementation issues, including how small companies targeted by the CTA will face compliance burdens. The time-consuming and challenging process of gathering required information on all beneficial owners of a reporting company that may have been created years ago is also addressed.
- In 2022, The Roundtable and its coalition partners submitted comments to the U.S. Department of the Treasury (DOT) and FinCEN that support efforts to thwart illegal money laundering in real estate, while encouraging policymakers to find a balanced approach that does not unfairly burden law-abiding businesses.
- The Roundtable is part of a broad coalition of business trade groups that supports a legal challenge by the National Small Business Association (*NSBA v. Janet Yellen*), which challenges the constitutionality of the CTA. The coalition stated, "It is clear whatever marginal benefit the CTA affords law enforcement will be far outweighed by the costs borne by small businesses and their owners."
- The Roundtable continues to work with industry partners to address the implications of FinCEN's proposed rules and the impact it could have on capital formation and the commercial real estate industry.

# SAFE Banking Act and CRBs

## Issue

Legal cannabis-related businesses (CRBs) face the challenge of obtaining bank accounts, and commercial property owners face legal challenges of taking on CRB tenants without safe harbor protections.

## The Roundtable's Position

- 47 states and DC currently legalize marijuana to varying degrees. Yet use, possession, and sale remains illegal under federal law.
- Real estate owners, lessors, brokers, and financiers need certainty when they transact with legitimate CRBs.
- The bipartisan *Secure and Fair Enforcement (SAFE) Banking Act*, (H.R. 1996) would eliminate the need for CRBs to operate on a cash basis, bring them into the banking system, and allow them to obtain accounts and credit cards. Commercial property owners would get a safe harbor if they lease space to a CRB, and their mortgages could not be subject to corrective action by a bank.
- To date, the *SAFE Banking Act* has passed the U.S. House numerous times, but it has yet to pass the Senate.

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# Restrictions on Foreign Investment in U.S. Real Estate

## Issue

Foreign investment is a major source of capital for U.S. commercial real estate, leading to job creation and economic growth for communities throughout our nation. A number of policy measures at the national and state level seek to restrict foreign investment in U.S. real estate. A number are already in effect. Most of these measures are intended to protect the homeland and ensure that such investments may enable a nefarious state actor from adversely impacting the nation's economic, military or civil interests.

At the **state level,** the Florida legislature recently passed Senate Bill 264 (SB 264), which Governor Ron DeSantis signed into law on May 8, 2023. SB 264 aims to limit and regulate the sale and purchase of certain Florida real property by "Foreign Principals" from "Foreign Countries of Concern." Twenty states have enacted restrictions on foreign investors in real estate and agricultural land. Eight states are considering similar measures. More are looking at the issue. So, the state-level restrictions have national implications.

While The Roundtable supports efforts to protect the nation's economic, military or civil security as well as the integrity of commercial real estate investments, we have concerns about rules that may hinder foreign investment in U.S. real estate by legitimate enterprises and capital formation by law-abiding entities.

## The Roundtable's Position

The Roundtable's Sept. 5 encourages state regulators to ensure that Senate Bill 264 does not deter investment into real estate in the state or undermine the economic benefits of this important industry. It also raises concerns about the technical aspects of SB 264 that could have unintended and negative consequences for investment in Florida and therefore limit the freedom of Florida's future growth.

The letter also cites the importance of foreign investment in U.S. real estate markets. In particular, many investment funds that are controlled or advised by regulated U.S. asset managers—including those that actively invest in Florida real estate—source investment capital in global capital markets.

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# Restrictions on Foreign Investment in U.S. Real Estate

With approximately $1.5 trillion of U.S. commercial real estate debt coming due in the next three years, foreign equity investments in U.S. assets are often an important source of capital as commercial real estate owners seek to restructure, refinance or sell their properties.

Consistent with Roundtable requests, the Florida Department of Commerce recently proposed a positive clarification to SB 264 that responds to a Roundtable request urging the Florida Real Estate Commission to consider specific concerns before implementing the new state law, which could impair capital formation and hinder the important role that legitimate foreign investment plays in U.S. real estate, the broader economy and job growth.

The proposed rule published on Sept. 21 addresses the implementation of Florida Senate Bill 264 (SB 264), Section 203, signed into law on May 8. The new law aims to limit and regulate the sale and purchase of certain Florida real property by "foreign principals" from "foreign countries of concern." The Florida Real Estate Commission will implement the new law. (SB 264 text).

Section 203 of the bill prohibits investment in real property near military installations and critical infrastructure. Importantly, the *de minimis* exemption has been re-drafted, which (1) fixes earlier drafting errors to the Registered Investment Advisor exemption, and (2) introduces a new category of *de minimis* interests that categorically exempts passive indirect investment. (See highlighted areas in the Notice of Proposed Rule)

The proposed rule clarification remains subject to change during a 21-day public comment period and may include a formal hearing.

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# EB-5 Reform and Integrity Act of 2022: Fact Sheet

## Issue

Congress passed a major overhaul of the EB-5 "regional center" investment visa program in March 2022. The EB-5 Reform and Integrity Act is found at "Division BB" of the Consolidated Appropriations Act of 2022. It represents the first major reforms to the EB-5 program since it was enacted in the early 1990s. Reforms include:

## Reauthorized EB-5 "Regional Center" Program

- 5-year extension through September 30, 2027.
- Reduces litigation risk from ~ 90,000 EB-5 investors who have seen no action by DHS on their petition since the regional center program expired on June 30, 2021.

## Expanded Targeted Employment Area (TEA Designations)

- TEA projects qualify for both lower investment levels and visa set-asides (see below):

**Prioritizing Rural Projects**

- In areas outside a Metropolitan Statistical Area, or within the outer boundary of any city or town with a population of 20,000 or more. (No change from prior law).
- U.S. Citizenship and Immigration Services (USCIS) must prioritize processing visas for investors in rural areas.

**New Criteria for Distressed Urban Area Projects ("High Unemployment Areas")**

- Codified the 2019 USCIS regulation ("donut" approach in which a project must be within a census tract—or any "contiguous" census tracts that "touch" the project's tract—where the average unemployment rate is 150% of the national average.
- DHS Secretary has the discretion to include a "directly adjacent" tract (to either the "anchor" tract or a "contiguous" tract) to satisfy the requisite 150% high unemployment criteria.

# EB-5 Reform and Integrity Act of 2022: Fact Sheet

- Distressed Urban TEA designations last for two years. These can be reviewed if the qualifying census tract(s) continue to meet "high employment" criteria.
- If a project was in an Urban TEA but falls out of high unemployment status, an "original" investor does not have to increase investment amounts to the non-TEA upper level.
- Only DHS can approve an Urban TEA "high unemployment" designation—unless the Secretary designates such authority to another federal official. No state or local official can approve.

**Defining "Infrastructure Projects"**

- A "capital investment project" administered by a "government entity"—that serves as the "job-creating entity" funded by EB-5 investors, and that contracts with a regional center—qualifies as an "Infrastructure Project."
- Must be a "public works project." No particular type of infrastructure "asset class" is specified.
- Only DHS can designate an Infrastructure Project—unless the Secretary designates such authority to another federal official. No state or local official can approve the designation.

## Qualified Investment Amounts & Adjustments

- 800,000 in TEAs
- $1,050,000 in non-TEAs
- On January 1, 2027, and every five years thereafter, investment amounts adjust for inflation.
    - Non-TEA level "adjusts up" for inflation.
    - TEA level "adjusts up" to 75% of the non-TEA level (with the goal of keeping the $250K delta between investment levels intact).

# EB-5 Reform and Integrity Act of 2022: Fact Sheet

## Clarifying Visa Set-Asides

- Set-asides are a percentage of the roughly 10,000 EB-5 visas available every year.
- 20% for Rural projects
- 10% for Distressed Urban/High Unemployment Area projects
- 2% for Infrastructure Projects
- Unused visas "carry over" in the same category in the following year.
- Unused visas in any "set aside" category made generally available for any project, in the year immediately following the "carry over" year.

## "Aging Out" Criteria

- An investor's "child" who is admitted to the U.S. on a "conditional" basis and who turns 21 shall continue to be considered a "child" if:
    - she/he remains unmarried and;
    - the principal investor is approved as a permanent resident and;
    - the principal investor files a petition for the child to remain in the U.S. no later than one year after the child's conditional status has terminated.
- The principal investor can only file one "aging out" petition after the child turns 21.

## Allowing the Broad Deployment of Capital

- DHS to enact regulations that allow the new commercial enterprise to deploy capital anywhere in the U.S. to keep the investment "at risk."

## Sovereign Wealth Funds

- Capital from a "bona fide" SWF may be stacked with EB-5 capital to finance a project.
- The SWF can be involved with the equity "ownership"—but not the administration—of the job-creating entity.

# EB-5 Reform and Integrity Act of 2022: Fact Sheet

- DHS to implement regulation for SWF funding in an EB-5 project.

## Job Creation Criteria

- 10 jobs must be created per investment (same as prior law).
- One job must be a "direct" job. It can be "modeled," and it is not necessary to produce a W-2 for a particular employee.
- The other nine jobs can be "indirect," modeled, and estimated (same approach under prior law).
- Construction jobs that last less than two years can satisfy 75% of the estimated "indirect" jobs.

## Allowing the Concurrent Filing of I-526 and I-485

- Investors can concurrently file their I-526 petitions (showing EB-5 compliance and investment) and their I-485 petitions (application for a "conditional" green card, which adjusts status from a "non-immigrant" to a conditional permanent resident). This can only be done if there is already a visa number available and current.
- Concurrent filing can reduce the time to adjust status once an I-526 is approved.

## "Grandfathering" Existing Investors

- If Congress fails to reauthorize regional centers after the Act's expiration on September 30, 2027, DHS will continue to process petitions filed on or before September 30, 2026.
- Applies to I-526 petitions and I-829 petitions (to remove conditional status and allow permanent residency without conditions).
- DHS may not deny an I-526 or I-829 simply because the regional program might expire in the future.
- An investor is eligible to file the I-829 two years after filing the I-526.

# EB-5 Reform and Integrity Act of 2022: Fact Sheet

## New "Integrity Measures" to Deter Fraud and Safeguard National Security

- USCIS to conduct an audit of each regional center at least once every five years.
- Explicit authority granted to USCIS to deny regional center "business plans" where an applicant has engaged in fraud, criminal conduct, or where plan approval would threaten national security.
- Confirms the application of U.S. securities laws over regional center offerings and investment advice.
- Regional center must submit annual statements of investment activities to USCIS. Failure to submit or falsify an annual statement results in sanctions that can include fines, temporary suspension, and a permanent "de-bar" of individual and regional centers that fail to comply with new oversight requirements.
- No person convicted of a crime (in the last 10 years) or fraud-related civil offense (that resulted in liability greater than $1M USD) can participate in EB-5 activities.
- With a limited exception for bona fide sovereign wealth funds, no foreign government representative may provide EB-5 capital or be involved in the administration or ownership of a regional center, new commercial enterprise, or job-creating entity.
- Requires fingerprints and other biometrics of persons involved in EB-5 activities to be submitted to USCIS.
- Strict new "source of funds" requirements to ensure that an investor's funds are derived from legitimate and lawful sources.
- Establishment of a new "EB-5 Integrity Fund," capitalized by regional center program feeds, to support amplified USCIS oversight and site visits.

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# SEC Proposed Rules: Private Fund Advisers, Form PF

## Issue

In 2022, the Securities and Exchange Commission (SEC) proposed two rules that would significantly overhaul the regulation of the private fund industry—a key capital source for income-producing real estate. The first proposed rulemaking would amend the Form PF reporting requirements for certain private fund managers and the second proposed rule would impose new investor reporting requirements on certain Private Fund Advisers under the Investment Advisers Act of 1940.

## The Roundtable's Position

- The SEC approved the two proposals despite strong dissents issued by Commissioner Hester Peirce, who voted no on each proposal and raised concerns that the rules would take away the SEC's resources for protecting retail investors. Chairman Gary Gensler, however, indicated that he views the rules as protecting retail investors whose retirement plans invest in private funds.
- With the stated goal of enhancing the Financial Stability Oversight Council's (FSOC's) monitoring and assessment of systemic risk and protecting investors, the SEC proposal would transform Form PF into a current reporting form for large hedge fund advisers and advisers to private equity funds, while maintaining the existing quarterly or annual reporting obligations applicable to private fund advisers regardless of size. The SEC's proposal also (1) expands Section 4 of Form PF by reducing the reporting threshold applicable to large private equity advisers from $2 billion to $1.5 billion in private equity fund assets under management, and (2) introduces a new large liquidity fund adviser reporting requirement that essentially requires such advisers to report the same information that money market funds report on Form N-MFP (as proposed to be amended in December 2021).

# SEC Proposed Rules: Private Fund Advisers, Form PF

- As stated in our March 21, 2022, Form PF comment letter, the proposed addition of new reporting requirements presents significant compliance and operational challenges for private real estate fund sponsors with no added benefit to investors and no relation to the intent of Form PF in monitoring systemic risk. As a result, the proposed amendments are not required and should not be adopted. At the very least, the SEC must provide adequate evidence that the proposed amendments bear some reasonable resemblance to systemic risk and provide meaningful cost-benefit analyses to support the increased burdens inherent in adopting the compliance infrastructure necessary for such reporting.
- The "Private Fund NPRM" would add new and amended rules under the Investment Advisers Act that the SEC believes would increase transparency and avoid adviser conflicts of interest. If adopted as proposed, a private fund adviser would need to adopt policies and procedures to comply with these requirements and evaluate whether its governing documents, offering memoranda, and side letters should be updated to reflect the new regulatory requirements and prohibitions. The proposed rules apply to exempt reporting advisers in some instances, but the SEC has posed questions for comment asking whether other parts of the proposed rules should apply to such advisers. The proposed rules have the potential to significantly increase regulatory burdens across registered and exempt private fund advisers.
- While we support efforts taken by the Commission to protect investors and monitor risk, our April 25, 2022 comment letter raises concerns that, if finalized, the private fund proposal could hinder real estate capital formation, the development and improvement of real properties, essential economic activity, and jobs.

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# SEC Proposed Rules: Safeguarding Advisory Client Assets

## Issue

On February 15, 2023, the Securities and Exchange Commission (SEC) proposed changes to require SEC-registered investment advisers to put all their clients' assets, including all digital assets like Bitcoin, with "qualified custodians".

The proposal would also require a written agreement between custodians and advisers, expand the "surprise examination" requirements, and enhance recordkeeping rules. These rules were originally designed for digital assets. "Reasonable" safeguarding requirements is ambiguous as applied to real estate. The SEC's release indicates that deeds evidencing ownership of real estate can be held at a qualified custodian—this is not accurate.  Deeds are recorded with a government authority. Land and buildings cannot be physically absconded. Lenders and other interested parties have an interest in ensuring no misappropriation of real estate.

## The Roundtable's Position

The Roundtable sees no policy reason to impose the proposed rule on real estate – real estate cannot readily be stolen. Lenders and others have an interest in ensuring no misappropriation of real estate. Title insurance protects real estate investors against covered title defects, such as a previous owner's debt, liens, and other claims of ownership. It's an insurance policy that protects against past problems, whereas other insurances usually deal with future risks. Titles are recorded in the name of the acquiring entity by a government entity.

The SEC's release indicates that deeds evidencing ownership of real estate can be held at a qualified custodian—this is not accurate.  Deeds are recorded by a government authority. Conditions to the exemption for real assets are problematic. Auditor verification of transactions is costly and not negotiated for by fund investors.

"Reasonable" safeguarding requirements is ambiguous as applied to real estate. Different jurisdictions present even more challenges. Different laws for title exist between not only states but also countries. The rule applies to registered investment advisors regardless of where the asset is located.

For these reasons, we believe that the SEC's policy reasons for imposing the rule on real estate seem irrelevant.

Capital and Credit

# NASAA's Proposed Revisions to its Statement of Policy Regarding REITs

## Issue

On July 12, 2022, the North American Securities Administrators Association, Inc. (NASAA) announced it is seeking public comment on proposed revisions to the NASAA Statement of Policy Regarding Real Estate Investment Trusts (the "REIT Guidelines"). The Roundtable has serious concerns about the Proposal and urges NASAA to withdraw the Proposal.

## The Roundtable's Position

- The Proposal could have a profound impact on the $20.7 trillion U.S. commercial and multifamily real estate market, approximately 9.4% of which is comprised of real estate investment trusts (REITs).
- It could have the unintended and unnecessary impact of impeding real estate capital formation, undercutting economic growth, and weakening the strength and stability of U.S. real estate capital markets. Investing in real estate supports economic growth; helps to grow the much-needed supply of housing, particularly in the multi-family, workforce, and affordable housing sector; enhances the infrastructure of industrial space, and supports state and local communities across the country.
- Since 1996, the Securities Act of 1933, as amended, has provided a preemption of the substantive state securities law requirements for several types of securities and offerings. However, certain securities offerings, including publicly offered REITs that do not list their securities on a stock exchange ("non-traded REITs"), remain subject to state securities law registration requirements. In addition, they remain subject to review by state securities regulators and the Securities and Exchange Commission (SEC). The REIT Guidelines have been adopted by several state securities regulators or used by their staff in reviewing such offerings.
- The REIT Guidelines were last amended in 2007 and set out requirements for REIT sponsors, advisers, and persons selling REITs, including provisions dealing with the suitability of investors, conflicts of interest, investment restrictions, and rights of shareholders as well as disclosure and marketing.
- NASAA has proposed revisions to the REIT Guidelines in four areas:

# NASAA's Proposed Revisions to its Statement of Policy Regarding REITs

- The proposed revisions would update the conduct standards for brokers selling non-traded REITs by supplementing the suitability section with references to the SEC's best interest conduct standard.
- The proposal includes an update to the individual net income and net worth requirements—up to (a) $95,000 minimum annual gross income and $95,00 minimum net worth, or (b) a minimum net worth of $340,000—in the suitability section through adjusting upward to account for inflation occurring since the last adjustment in 2007.
- The proposal would add a uniform concentration limitation prohibiting an aggregate investment in the issuer, its affiliates, and other non-traded direct participation programs that exceeds 10% of the purchaser's liquid net worth. Liquid net worth would be defined as that component of an investor's net worth that consists of cash, cash equivalents, and marketable securities. [NOTE: There is no carveout for accredited or other sophisticated investors.]
- The proposed revisions also include, in multiple sections, a new prohibition against using gross offering proceeds to fund distributions, "a controversial product feature used by some non-traded REIT sponsors . . . having the potential to confuse and mislead retail investors."

- In the request for comment, NASAA points out that if adopted, the revisions to the REIT Guidelines have the potential to influence updates to other Guidelines, including those for Asset-Backed Securities, Commodity Pools, Equipment Leasing, Mortgage Programs, and Real Estate Programs (other than REITs) and the Omnibus Guidelines.
- We are concerned that the Proposal appears to be substantially based on a flawed and outdated impression of the PNLR sector and PNLR products. Many of the issues that NASAA highlights to justify the Proposal—such as liquidity concerns, fee transparency, and sources of distributions—are largely, if not completely, ameliorated with respect to the NAV PNLRs[8] that are now being offered to investors.
- We are working on this issue with a number of other groups and submitted a comment letter raising concerns about the proposal.

[8] REITs that are registered with the SEC but whose shares intentionally do not trade on a national securities exchange. NAV PNLRs, which comprise the majority of PNLRs marketed today, are permanent entities that provide shareholders with regular ability to sell shares back to the REIT at the current Net Asset Value (NAV).