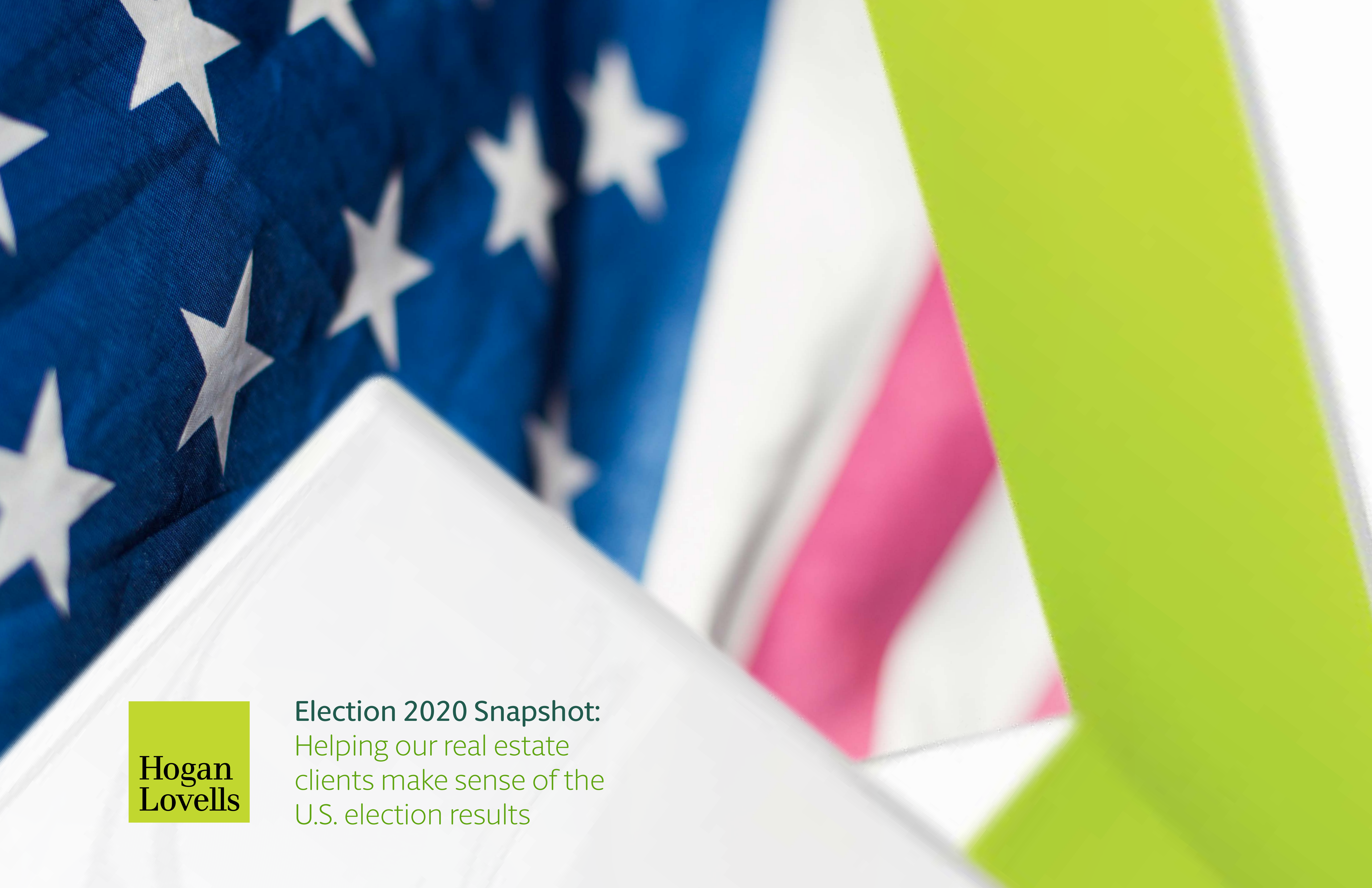


Hogan Lovells

Election 2020 Snapshot:

Helping our real estate clients make sense of the U.S. election results

While there is an anticipation of greater predictability under a President Joe Biden, which is critically important to the commercial real estate industry, expected and potential changes in trade, taxation, housing and health care policy are all factors that could affect the industry.

In November 2020, Democrat Joe Biden defeated incumbent Republican Donald Trump to become the President-elect of the United States. During the election cycle, the Biden campaign proposed policy changes that could have broad consequences for the real estate sector, including eliminating certain tax-advantaged treatments of real estate assets, and encouraging public and private investment in low-income housing, infrastructure projects and renewable energy. Whether the Biden administration can implement any of the goals of the Biden campaign will largely depend on two factors, (i) macro-economic trends and (ii) who wins the Georgia run-offs for two Senate seats on January 5, 2021.

Like most other major sectors of the economy, the future of real estate over the next year and beyond will be largely dependent on the success of COVID-19 vaccines and their distribution to a large percentage of the public and thereafter, and how fast the economies of the country and the world can bounce back from the pandemic. These factors would be accelerated if Washington is able to approve another meaningful COVID-19-related stimulus package.

The Biden administration has repeatedly discussed adopting a more cohesive national approach to COVID-19, and one of its first steps post-election was to appoint a task force to help the country better respond to the pandemic. So, there is some reason for optimism that a rebound in the sector may be coming soon.

The Georgia Special election on January 5, 2021 for two Senate seats will determine which party will control the Senate. If Democrats win both races, then the Senate would be split 50-50 with the Vice President-elect breaking any ties. If Republicans win one or both Georgia seats, then they will retain control of the Senate. Holding the presidency and a Democratic Senate and House would enable Biden to enact large portions of his agenda and implement policies that would affect the real estate sector. If Republicans retain the Senate, the Biden agenda will have a less impactful effect on the broader economy and commercial real estate.

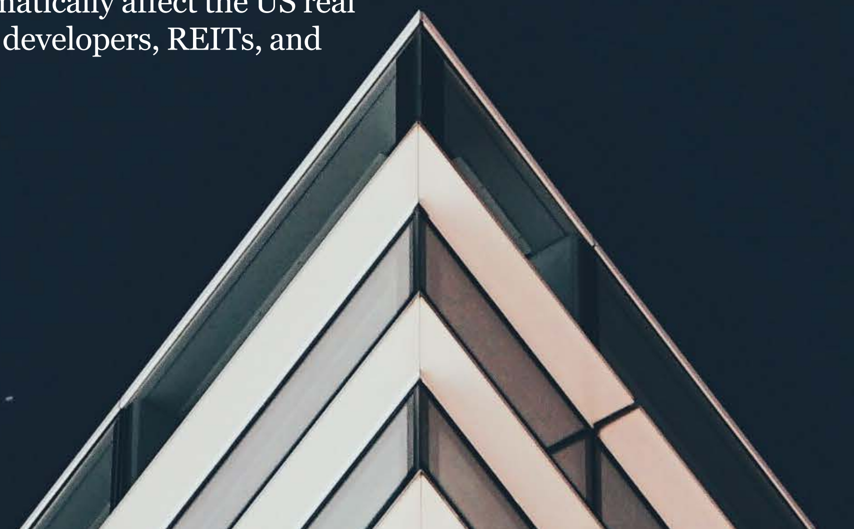
Taxation

President-elect Biden has generally proposed increasing taxes on the real estate industry. During the 2020 campaign, President-elect Biden proposed a number of changes to the Internal Revenue Code including raising individual and corporate income tax rates, increasing capital gains tax rates, eliminating 1031 like-kind exchange deferrals, investing in the Low Income Housing Tax Credit Program, and reforming the statutory rules relating to qualified opportunity zones. President-elect Biden will also seek to increase the tax rate on carried interest, at least for high-income taxpayers. While an increase in tax cost may lead some potential sellers to stay on the sidelines, tax impacts are typically just one of many factors motivating transactions.

Increases in corporate tax rates have historically been connected to increases in demand for tax credits, as companies look for new ways to reduce their tax liability. Accordingly, if a Biden administration is able to pass a corporate income tax increase, as well as legislation providing for investments in the Low Income Housing Tax Credit program, investors could see an increase in opportunities to develop and in invest in low income multifamily properties. Similarly, increases in the corporate income tax rate could also provide opportunities for investment in properties involving tax credits relating to energy efficiency or historic preservation.

Additionally, an increase in capital gains rates, coupled with the elimination of the like-kind (1031) exchange deferral, which allows property sellers to defer recognition of tax gain when sale proceeds are re-invested in like-kind properties, could even more dramatically affect the US real estate market. Many developers, REITs, and funds rely on 1031 exchanges to freely buy and sell properties, without having to worry about taxes resulting from such sales hurting cash flow. If 1031 tax deferral for these exchanges is eliminated, the tax cost would significantly hurt rates of return. Moreover, if a Biden administration is successful in increasing capital gains and Section 1231 tax rates, this would serve to further increase the amount of tax due on these real property sales. Finally, any restrictions added to the opportunity zones program, which offers deferral of capital gains or 1231 gains for sales proceeds invested in designated areas ("opportunity zones") of the country, or if this program is eliminated entirely, would further limit deferral options and increase tax cost.

It's worth noting that a number of these potential changes would likely have little to no impact on the tax liability of foreign investors into U.S. real estate. Foreign investors generally have limited U.S. capital gains, and are often subject to a withholding regime which makes it nearly impossible for them to take advantage of tax deferral programs like the Opportunity Zones Program. As such, an increase in capital gains rates and/or an elimination of 1031 exchange deferral may with respect to non-U.S. entities do little to cool the desirability of investing in U.S. Real Estate. With this said, any potential changes in the tax arena will likely be priced into the market, so even if investors find that these potential changes to the tax code have no substantial impact on their U.S. tax liability, they will still likely have an impact on the valuations of various investments and real estate assets.



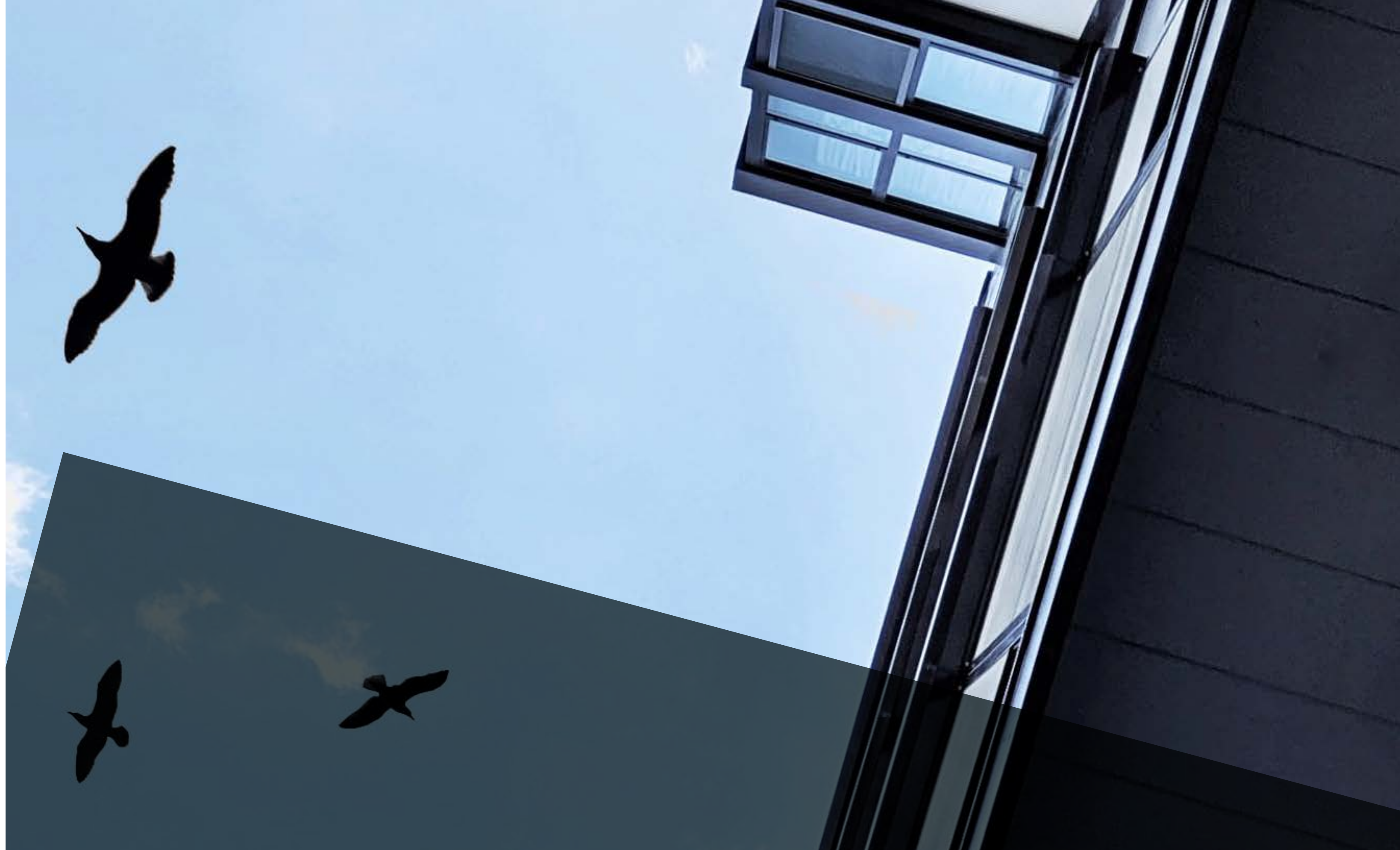
Foreign Investment

A Biden administration will have power to influence spending priorities and the regulatory environment and to enact trade policy. The Trump administration has generally taken a nationalistic approach to foreign investment and has not hesitated to publicly undermine, or attempt to block, foreign acquisitions of U.S. companies or investments into U.S. projects. In contrast, President-elect Biden has generally taken a less antagonistic view towards foreign investment and has emphasized the opportunities in international economic cooperation. This difference in approach could lead to substantial changes in how investments in certain U.S. companies and projects are reviewed, as well as increased opportunities for immigration-related investments such as those made pursuant to the EB-5 Program. The potential for less trade friction, especially with U.S. allies, may be a helpful factor as the economy pulls out of the pandemic-induced recession.

On February 13, 2020, the Council for Foreign Investment in the United States ("CFIUS") was granted new authority to review foreign direct investments into real estate assets located near military bases or critical infrastructure (including energy and IT-infrastructure), as well as investments into this infrastructure itself. Notably, CFIUS is under the purview of the executive branch and as such, the President has substantial authority over its approach to reviewing and approving foreign investment transactions. It is reasonable to expect that while CFIUS under a Biden administration will continue to scrutinize the flow of foreign capital into these critical assets, it will potentially take a much less antagonistic approach towards these investments, as compared to the Trump administration, unless they pose security risks. Thus, foreign investors may find it easier to invest in U.S. energy projects such as wind farms and powerplants, data centers, and other infrastructure projects. This could greatly increase the potential for investment opportunities if a Biden administration is also able to get an infrastructure bill through Congress. While a Biden administration will likely be no less aggressive in prosecuting and restricting Chinese interests than the Trump administration, it is anticipated that Chinese investments will be reviewed by CFIUS in a less public manner and that Biden will seek opportunities to reduce tensions in U.S.-China relations.

One of President-elect Biden's priorities has been modernizing America's immigration system and welcoming immigrants into the U.S. This stance could encourage more foreign nationals to reconsider attempting to obtain citizenship through programs like EB-5, which allows foreign nationals to obtain United States green cards by investing in job-creating real estate projects. Additionally, as part of this modernization of the immigration system, it is feasible that there could be changes to the EB-5 Program itself. Accordingly, it is possible that a Biden administration could provide a rejuvenation of EB-5 financing and lead to an increase in the number of projects financed by this capital source.

A Biden presidency will likely represent a departure, or attempted departure, from the Trump administration's policies in the realms of taxation and foreign investment.



Infrastructure

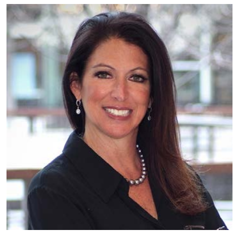
The Biden infrastructure proposal also has the potential to positively impact real estate property values and operations in the United States. Biden has advocated for the Federal Government to invest in the repair and creation of public transportation systems, green spaces, water systems, electricity grids, and broadband connections throughout the country. Owners and tenants of real estate in densely populated regions, such as New York City and the surrounding areas, could benefit greatly from the repair and modernization of high speed rail lines. Increased availability and capacity of broadband through high-speed fiber optic cables could significantly expand the geographic areas of the U.S. that are able to support the demands of modern businesses with increasing broadband communications and cloud storage needs. Without infrastructure spending by the Federal Government, state and local governments, as well as specific improvement districts set up to pay for infrastructure projects would be required to come up with the money themselves, often through additional taxes on real estate. Large, costly infrastructure projects can quickly become infeasible without contribution from the Federal Government. However, with a proposed $1.6 trillion of spending for infrastructure and R&D under a Biden administration, real estate demand for sectors such as office and industrial should be positively impacted. The residential real estate sector could see positive effects if housing policy initiatives, such as tying federal funding to zoning changes spur affordable housing development in suburban areas. Alternatively, the tax law changes necessary to achieve the infusion of federal funds for such additional spending could lower consumer spending in the luxury retail segment and some areas of the housing market. Increases in corporate taxes may impact capital expenditures by businesses and wage and job growth. Developers will also be keeping an eye on Biden's environmental agenda which may also have implications for commercial building operating costs in order to meet higher energy efficiency standards.

COVID

Possibly the largest single determinant of the health and vitality of the real estate market will be the timing of recovery from the COVID-19 pandemic. The pandemic has presented legitimate questions as to the projected investment outlook for various asset classes in the U.S. real estate market. The disruption and changes in the economy have inflated rents in some asset classes while creating distress in others. However, it is difficult to predict with certainty which, and to what degree, trends initiated or accelerated by COVID-19, such as remote working office policies and avoidance of retail centers, will become permanent. COVID-19 will continue to affect the U.S. real estate industry regardless of which administration controls the Federal Government. However, while the Trump administration has largely left specific decisions about the response to the pandemic to state and local government, Biden has campaigned on a different approach. He has proposed dedicating more federal resources to slow the spread of COVID-19, including increasing the number of drive-through testing sites, as well as hiring additional federal workers to coordinate contact tracing. He has also discussed additional COVID-19-related stimulus packages to individuals and businesses, though it is unclear what exactly those packages would include, or whether they could pass through a likely Republican-controlled Senate. A relief package of less than $2 trillion is expected under a Republican controlled Senate but the amount of stimulus could be higher and implemented in multiple phases if the Democrats gain control over the Senate.

If effective at slowing the spread of the virus, the incoming administration's policies may be helpful in stabilizing U.S. real estate values and operations. However, we note that the widespread rollout of an effective vaccine will be the most likely catalyst for a return to normal and initial indications are that such trend will occur, at best, by the end of the second quarter of 2021.

Key contacts



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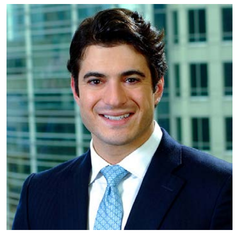

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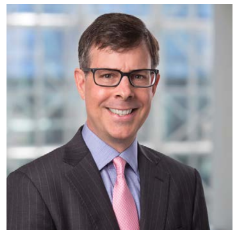

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