

## **Mick Law - Alts. News Bulletin**

### **February 25, 2021**

In further effort to provide exceptional service to our client base, we offer this news bulletin, which is intended to inform you of recent news concerning alternative investment strategies, with our focus for this bulletin placed upon developments affecting qualified opportunity zones. This bulletin also provides industry related announcements of importance.

#### ***Opportunity Zones Activities Through 2020***

Novogradic & Company LLP (“**Novogradic**”) released its year-end 2020 report relating to qualified opportunity zone (“**QOZ**”) investment activities. Based upon its tracking of 659 qualified opportunity funds (“**QOFs**”) raising money since May 2019, Novogradic reported \$15.16 billion of QOF equity raised within these funds as of December 31, 2020. This represented a healthy 66% increase in raised equity from what was reported by Novogradic at year-end 2019 (i.e., \$5 billion).

As to the strategies of these QOFs, 188 (29%) concentrate exclusively on residential real estate acquisitions and developments (i.e., multifamily and affordable, workforce, student and senior housing), whereas 163 (25%) included at least one component of residential real estate within the program’s investment focus. Similar to what we saw in the 1031 DST market, the QOFs reporting a multifamily focus accounted for a majority of the QOF equity tracked by Novogradic through year-end 2020.

A summary of other findings mentioned in Novogradic’s report included the following:

- The average equity raised within the tracked QOFs was \$23 million per fund;
- Of the 659 QOFs, more than 80% reported equity raises at or below \$25 million;
- About 80% of the tracked QOFs utilize either a city-specific or regional investment focus, whereas 20% had an unspecified geographic focus;
- The leading states for capital deployments included California, New York, Ohio, Arizona, Texas, Washington, Colorado, and Florida;
- The tracked QOFs also reported a significant level of commercial real estate investments (e.g., office, industrial, mixed-use, and retail), with a majority of

the QOFs including one of the above commercial asset classes within their investment mandates; and

- Of the \$15.16 billion of tracked QOF equity, only 2.63% and 2.82% was raised by funds that provided capital for renewables or operating businesses, respectively.

Please note that Novogradic’s tracked QOFs do not include non-syndicated programs owned and managed by their principals. Inclusive of the non-syndicated funds, the White House Council on Economic Advisors estimates the total equity in QOFs to be about \$75 billion (as of August 2020).

### ***Opportunity Zone Deadlines Were Extended (January 2021)***

On January 19, 2021, the IRS issued Notice 2021-10 (the “**Notice**”), which extended several deadlines pertaining to QOF investments and compliance.

*Most notably, the notice extended the 180-day period for many taxpayers realizing capital gains in 2019 through assets held either individually or through partnerships.*

For capital gains realized on assets held outside of partnerships from October 4, 2019 through October 2, 2020, the 180-day investment period was replaced with a single deadline of *March 31, 2021*.

For taxpayers with capital gains realized through partnerships, the *March 31, 2021* deadline applies to capital gains recognized by the partnership on or after January 1, 2019. The Notice replaces and extends an earlier December 31, 2020 deadline that was put in place under IRS Notice 2020-39.

The Notice also extended several compliance related deadlines pertaining to substantial improvements, 90% asset test, working capital safe harbor, reinvestments, and qualified improvement properties. A summary of these other deadline modifications and rule changes is provided below:

*30-Month Substantial Improvement Requirement* – As you may recall, program property that doesn’t otherwise satisfy the original use test is treated as qualified opportunity zone business property (“**QOZBP**”) if it is substantially improved within a 30-month period after acquisition. The Notice allows a QOF or QOZ business (“**QOZB**”) to disregard the period between April 1, 2020 and Mar. 31, 2021 when calculating the 30-month period.

*Working Capital Safe Harbor* – The Treasury Regulations allow a QOZB to hold working capital if they follow a written plan to deploy the capital within 31 months. On this point, the shelter-in-place requirements imposed by most state and local governments place QOZBs in jeopardy of failing to meet the working capital safe harbor. The Treasury Regulations provide an automatic extension of the 31-month period of “not more” than 24 months if the QOZB is in a federally declared disaster area. The Notice clarifies that the extension is available to those QOZBs that hold working capital, since all opportunity zones are deemed to be located in federally declared disaster areas (effective Jan. 20, 2020). The regulations also allow a QOZB to pause its 31-month window if the project is delayed awaiting government approval.

*90% Investment Standard* – The Notice states that any failure by a QOF to satisfy the 90% investment standard for any taxable year that includes a testing date falling between April 1, 2020 and June 30, 2021 is to be disregarded for purposes of determining whether the QOF or any otherwise qualifying investments in the QOF satisfy the opportunity zone statutory and regulatory requirements for any taxable year.

*12-Month Reinvestment Rule* – A QOF has 12 months to reinvest proceeds from the sale of property or a return of capital without impacting the 90% investment standard. The regulations allow “not more” than an additional 12 months if the reinvestment is delayed due to a federally declared disaster, provided the QOF invests the proceeds in the manner originally intended before the disaster. This relief is authorized in cases where the reinvestment period includes June 30, 2020. As the extension is cumulative, the maximum reinvestment period is 24 months.

*Qualified Improvement Property (“QIP”) Correction* – Note that the CARES ACT corrected the depreciable life of QIP from 39 years to 15 years, which makes such property eligible for bonus depreciation treatment. Thus, QIP acquired and placed in service between Sept. 27, 2017 and Dec. 31, 2022 is generally eligible for 100% bonus depreciation. Thereafter, bonus depreciation is phased out through 2026. Please note that if a QOZB becomes an electing real property trade or business to prevent limitation of its interest deductions, it cannot claim bonus depreciation on its QIP. However, reducing the depreciable life of QIP to 20 years for taxpayers making the real property election may provide some income tax benefits for certain QOF investors.

*QOF Penalty Relief* – Finally, the Notice applies the statutory “reasonable cause exception” to prevent the imposition of QOF penalties for failing to meet the 90% investment standard for any taxable year during which the last day of the QOF’s first 6-month period or the last day of its taxable year falls within the period between and including April 1, 2020 and June 30, 2021. As a result, any calendar year QOF that self-certified prior to 2021 will be entitled to this relief for both 2020 and 2021.

### ***QOF Extension on Capital Gain Deferrals (Feb. 8, 2021)***

On February 8, 2021, a bill was introduced in the U.S. House of Representatives to extend the deferral on capital gains. *The Opportunity Zones Extension Act of 2021 proposes to extend the income tax deferral for taxpayers invested in QOFs through 2028, two years later than currently allowed.*

A press release issued by legislation sponsors Rep. Tim Burchett, R-Tennessee, and Rep. Henry Cuellar, D-Texas, said the extension “will attract private sector investment in underserved communities, building on pre-pandemic success and helping them come back stronger than before.”

### ***Private Placement Activities***

As of February 1, 2021, AI Insight covered 177 private placements raising capital, with an aggregate target raise of \$17.8 billion and an aggregate reported raise of \$8.6 billion reported within these programs (i.e., approx. 50% of the target raise).

Real estate-oriented funds, including 1031s, opportunity zones, and real estate pass throughs represent the largest component of AI Insight’s coverage, at about 75% of the funds and 59% of the target raise.

Of the private placements covered by AI Insight, 78% use the Rule 506(b) exemption, with 12% allowing general solicitation activities (and with 10% not reporting their exemption status yet).

While activities were down in general last month, AI Insight also reported that 14 private placements were closed in January 2021. The average time on the market for these closed funds was 300 days.

We note that Mountain Dell Consulting (“**Mountain Dell**”) recently released its 2020 Year-End Report relating to the securitized 1031 industry. Despite the headwinds of COVID 19, roughly \$3.2 billion was raised by 40 unique sponsors that closed 170 programs. Leading the way was Inland Private Capital Corp. (19%), which was followed by ExchangeRight Real Estate (12%), Capital Square Realty

Advisors (11%), Black Creek Group (8%), and Passco Companies (7%). As was the case in respect to the findings of Novogradic’s QOF report, multifamily properties accounted for the highest percentage of capital raised (\$1.631 billion, 51.12%), with retail (\$499 million, 15.64%), self-storage (\$231 million, 7.26%), and industrial (\$207 million, 6.50%) programs reporting healthy levels of raised capital in 2020.

Certain other findings of note from Mountain Dell’s year-end report included the following:

- Geographically, the Southeast Region of the U.S. (i.e., Alabama, Florida, Georgia, and Carolinas) accounted for 84 of the 170 1031 programs (approx. 50%):
- Offerings structured as DSTs: 161 (95%);
- Offerings structured as TICs: 9 (5%);
- Offerings registered as 506(b): 123 (72%);
- Offerings registered as 506(c): 47 (28%);
- Avg. year one cash-on-cash: 5.17%; and
- Avg. days on market: (200 days, with 164 days as the median).

### *AI Industry Announcements*

2021 Mick Law Energy & Global Alts Symposium  
May 16-18, 2021  
Dallas/Plano Marriott at Legacy Town Center

The National Due Diligence Alliance Spring Conference  
March 12-14, 2021  
Four Seasons Houston

ADISA’s Spring 2021 Conference  
May 10-12, 2021  
J.W. Marriot Scottsdale Camelback Inn & Resort  
Scottsdale, Arizona



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