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From the Editor

*Robert G. Koen**

Data Centers

One of the most important, and in some places one of the most strongly debated, type of real estate project under construction across the country today is the data center. The first few opening articles in this issue of *The Real Estate Finance Journal* focus on data centers. And, as you will see, we have a great deal more for you here.

DATA CENTER CONSTRUCTION

The lead article in this issue, titled, "A Customized Approach to Data Center Construction," is by James P. Bobotek, Arielle L. Murphy and Robert A. James, attorneys with Pillsbury Winthrop Shaw Pittman LLP.

In this article, the authors detail customized considerations for drafting, negotiating and administering data center design and construction agreements.

A PAUSE REPEALED

The article that follows, titled, "Facing a Federal Lawsuit, Texas County Repeals Blanket Pause on Data Center Construction, Adopting New Approval Procedures Instead," is by Thomas G. Allen, Austin D. McCarty, Tad J. Macfarlan and Robert M. Smith, attorneys with K&L Gates LLP.

In this article, the authors discuss a construction moratorium on new data centers enacted by a Texas county, the federal lawsuit that followed, and the county's decision to rescind the moratorium and to adopt a new approval process instead of the blanket prohibition.

AN EPA PROPOSAL

Then, in the article titled, "EPA Proposes to Loosen New Source Review 'Begin Actual Construction' Limits: What It Could Mean for Data Centers and Other Capital Projects," Karl F. Kumli and John D. Surma, attorneys with Fisher Phillips, discuss a new proposal from the U.S. Environmental Protection Agency that could speed up large construction projects, especially data centers.

REIT COMPENSATION

Edward L. Glazer, William T. Goldberg, Yoel Kranz, H. Neal Sandford, Ettore A. Santucci and Christopher L. Versfelt, attorneys with



Robert G. Koen, Esq., the editor of *The Real Estate Finance Journal*, is a partner in the New York Real Estate Finance practice of Carter Ledyard & Milburn LLP, where he focuses on commercial real estate acquisitions, complex financing and restructurings for both lender and borrower entities.

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Goodwin Procter LLP, are the authors of the next article, titled, "It's True: Long-Term Incentive Plan Unit Compensation Is a 'Win-Win' for REIT Shareholders and Management."

Here, the authors discuss operating partnership unit-based compensation for chief executive officers of public real estate investment trusts.

THE SEC

In the article titled, "U.S. Securities and Exchange Commission's Registered Offering Reform Proposal: A Potential Game-Changer for Public Non-Traded REITs," Mary Katherine Rawls and Heath D. Linsky, attorneys with Troutman Pepper Locke, discuss a proposal that would preempt state "blue Sky" registration and qualification requirements for all Securities and Exchange Commission registered offerings, including those of non-traded REITs.

VALUATIONS

Dharminder Kalsi and David Emma of Cohn-Reznick are the authors of the article titled, "Valuations of Ownership Interests in Early-Stage Developments."

Here, the authors explain how to value early-stage development interests using a disciplined, market-based analysis.

CALIFORNIA

The next article is titled, "California's OHCA Publishes Draft Regulations to Capture Health Care Transactions With Private Equity, Hedge Funds and MSOs." In this piece, Paul A. Gomez, Ashley N. Osak and Matthew T. Lin, attorneys with Polsinelli, discuss proposed regulations that, among other things, demonstrate the interest of California's Office of Health Care Affordability in details of the arrangements between private equity groups and California health care entities and the impact of transactions on real estate where health care is delivered.

A NEW YORK TAX

Stuart M. Saft, a partner in Holland & Knight LLP, next analyzes the new pied-à-terre tax enacted by New York in his article, titled, "New York State Enacts Pied-à-Terre Tax on Expensive Non-Primary New York City Residences."

SEQRA REFORM

The article that follows, by Christopher B. Fisher and Maximillian Mahalek, attorneys with Cuddy & Feder LLP, is titled, "What Housing Developers Need to Know About SEQRA Reform in New York."

In this article, the authors discuss reforms to New York's State Environmental Quality Review Act that will have practical implications for housing developers in New York State, including greater regulatory certainty and investment potential for qualifying projects.

THE USDA

The article titled, "U.S. Department of Agriculture Proposes Major Overhaul of Agricultural Foreign Investment Disclosure Act of 1978 Rules," is by Marisa N. Bocci, Kari L. Larson and Jeffrey C. Thomson, attorneys with Arnold & Porter Kaye Scholer LLP.

In this article, the authors explain how a proposed rule published recently by the U.S.

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acquisition, financings, and development; commercial project development; and real estate loan and investment workouts and restructurings. He may be contacted at koen@clm.com.

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Department of Agriculture could affect a wide range of real estate market participants, including institutional investors in farmland and timberland; commercial and rural-land developers; renewable energy and infrastructure developers; foreign persons and U.S.-organized entities with upstream foreign ownership; and even wholly domestic owners who lease to foreign tenants.

SAUDI ARABIA

Malek Al Rifai, Nabil A. Issa, Alexander Barker and Abdulrahman Albilal, all with King & Spalding LLP, follow with their article, titled, "Saudi Arabia Issues Implementing Regulations for White Land Fees and Vacant Properties Fees: What Property Owners and Investors Need to Know."

Here, the authors discuss the key provisions of new Saudi Arabia regulations addressing undeveloped land and vacant buildings and their practical implications.

EUROPEAN HOTELS

In the article titled, "Forward Purchasing Hotels in Europe: Managing Risk in a Rebounding Market," Martin Smith and Samuel Cramer, attorneys with Goodwin Procter LLP, review some of the key commercial considerations investors should keep in mind when entering into forward purchase hotel transactions in Europe.

THE EUROPEAN COURT OF JUSTICE

The article titled, "Court of Justice of the European Union Rules That Portuguese Real Estate Transfer Tax on Restructurings Violates EU Law - Signal Effect for Germany," is by Florian Schiefer and Merlyn von Hugo, attorneys with McDermott Will & Schulte.

In this article, the authors review a decision by the Court of Justice of the European Union holding that the Portuguese real estate transfer tax on restructurings violates EU law.

NEPA REVIEW

The article that follows, titled, "One Year After *Seven County*: Trends in NEPA Review and Litigation Risk," is by Tommy P. Beaudreau, H. David Gold, Caroline McHugh, Barak Kamelgard and Ethan McKenzie, attorneys with Wilmer Cutler Pickering Hale and Dorr LLP.

In this article, the authors analyze court decisions in the year following the U.S. Supreme Court's opinion in *Seven County Infrastructure Coalition v. Eagle County*, finding that agencies are prevailing in the vast majority of post-*Seven County* cases, but that litigation risk remains where challengers can identify concrete regulatory or record-based deficiencies.

HUD

Then, in the article titled, "U.S. Department of Housing and Urban Development Pulls the Plug on Emotional Support Animal Guidance: 5 Steps for Education Housing Administrators," Joshua D. Nadreau and Shiloh Theberge, attorneys with Fisher Phillips, discuss the decision by the U.S. Department of Housing and Urban Development permanently rescinding prior guidance on emotional support animals in housing, effectively ending nearly two decades of federal protection for those who rely on emotional support animals.

Enjoy the issue!

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A Customized Approach to Data Center Construction

*James P. Bobotek, Arielle L. Murphy and Robert A. James**

In this article, the authors detail customized considerations for drafting, negotiating and administering data center design and construction agreements.

Data center construction projects are, to put it mildly, distinct. They differ from traditional construction in a host of manners, and are particularly distinctive because the value of the facility depends on unique measures of performance. A center that cannot meet uptime, cooling, redundancy or connectivity standards will not achieve its mission, whether or not the structure itself meets standard industry contract-form "substantial completion" or "mechanical completion" definitions.

Owners, developers, lenders, operators and hyperscalers—especially hyperscalers!—want it all. They seek favorable and stable pricing, accelerated delivery and sophisticated components, all of which are evolving in "real project time." Standard construction contract forms deserve extensive modifications to align clauses with expectations, with a heightened focus on systems integration, commissioning, and allocation of special risks. This article details customized considerations for drafting, negotiating and administering data center design and construction agreements.

THE INTEGRATED SYSTEMS CONTEXT

Digital infrastructure facilities, driven by artificial intelligence workloads, depend critically on sophisticated procurement of power, cooling, connectivity and components. Constraints such as utility capacity and interconnection limits, long-lead equipment backlogs and labor shortages are routine, especially in the regions where data center construction is most intense.

Most large infrastructure projects are delivered these days using either design-build or engineering, procurement and construction contracting structures (collectively, EPC). Owners and their stakeholders value EPC for the single point of responsibility. Unlike traditional design-bid-build delivery, EPC permits overlapping design and construction, facilitating early procurement. They are not panaceas, though. The design professional works for the contractor instead of the owner, and the price and schedule must be fixed when the time is right. In a perfect world, this is when designs have evolved and key procurement risks have

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been bought out. (We do not live in a world that is always close to perfection.)

COMPLETION = OPERATIONAL READINESS, NOT JUST OCCUPANCY

The laser-beam focus for any data center EPC should target operational performance. In ordinary commercial construction projects, "substantial completion" victory is declared when the owner can occupy the building and individual mechanical systems are tested, even if punchlist work remains. That standard is inadequate for data centers, where completion should instead be tied to total operational readiness, requiring every integrated system to perform to specification under realistic load conditions.

In a data-center contract, generic "substantial completion" language should be set aside in favor of well-defined milestones. Criteria may include, in no particular order: integrated systems; redundancy and "failover" testing; energization and frequency regulation testing; and connectivity testing in accordance with quantitative standards. These requirements should not be framed as aspirational goals, or defer generally to "industry standards." Specifics such as N+1 or 2N redundancy systems,[1] Power Usage Effectiveness (PUE) targets,[2] and uptime levels should be considered.

Consequences for failure to achieve metrics should be practical and enforceable. Liquidated damages for schedule delay and nonperformance look great in an owner's first draft of a contract; alas, they need to be negotiated, agreed upon and implemented with savvy counterparties, who will propose caps, carveouts and veiled warnings of price increases. Furthermore, some aspects of performance depend on items outside the EPC scope, such as owner-furnished equipment, utility hookups and third-party systems. Thus, cooperative responses to emergent problems are needed, necessarily involving all potentially responsible parties—the owner included.

PRICING STRUCTURES AND COST MANAGEMENT

The digital infrastructure boom has strained all kinds of input markets. Traditional lump-sum contracting is increasingly difficult when pricing for electrical equipment, copper and labor can fluctuate dramatically. Utility interconnection constraints, power-delivery uncertainties and entitlement challenges can create additional schedule and cost risks that may not be within the contractor's control. As a result, many jobs now use target prices, guaranteed maximum prices, or hybrids with elements of fixed pricing. For any price structure with "teeth," the drafter's attention should be trained on the trio of moving parts—allowances, contingencies and escalations.

Allowances should be tied to identifiable scope items, not serve as placeholders for incomplete designs or matters within the contractor's sole control. Contingencies should specify who controls drawdowns and when funds may be used. Escalations can be based on commodity price or labor wage indices, subject to collars like caps or locked-in time periods. Contracts should also clearly specify assumptions regarding utility availability, interconnection milestones and other power-related prerequisites, as well as the parties' respective entitlement to schedule relief or compensation if those assumptions prove inaccurate.

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OWNER-FURNISHED EQUIPMENT

Hyperscalers often direct procurement of their preferred equipment or systems to their preferred vendors. This is far more prevalent in data center projects than others, where owner-furnished equipment is typically limited to fixtures or finishes. Owner-furnished equipment provisions should address allocation of coordination, delivery, receipt, storage, installation, integration, and warranty roles and risks. The data center agreement should also address entitlement to schedule relief and compensation resulting from late delivery, defective equipment, incomplete vendor information or integration failures associated with owner-furnished equipment.

COMMISSIONING AND INTEGRATED TESTING

Data center commissioning is not just spending a long weekend testing individual components. Integrated validation is essential because the practical exposures often reside at the crevices, the interfaces between systems. Power, cooling, controls and connectivity must function seamlessly under simulated operational conditions. On top of normal experience, commissioning should stretch to cover failover scenarios, redundancy validation and peak-load conditions.

Consequences of problems encountered during commissioning should be practical and staged. Before employing contractual "sticks" such as damages, the contract should accommodate retesting and reperformance rights during crisply defined cure periods, and require the involvement of all potentially responsible parties.

Many times, portions of a data center are to be turned over before overall commissioning. The agreement should address access, security, operational coordination, liability risks, and procedures governing and mitigating concurrent and potentially interfering activities during this period of overlap.

TECHNOLOGY EVOLUTION AND CHANGE MANAGEMENT

The digital infrastructure industry is rapidly evolving, not just from project to project but also in the real time of a given contract's lifetime. An initially conceived facility may see material modifications before completion because of evolving artificial intelligence workloads, cooling technologies, rack densities or tenant requirements. The construction contract should treat technology-driven modifications as expected, not extraordinary.

Predetermined unit rates, with all extended-overhead charges included, can reduce disputes while the parties negotiate a ceiling on their respective exposures to a change. Modifications stemming from evolving owner requirements may deserve different treatment than those resulting from changes in the input markets such as upgrades or unavailability of equipment or systems. If equipment or system substitutions become necessary because of supply chain constraints, the contract can define whether the substitute must be strictly equivalent or merely commercially reasonable. Modules for discrete expansions, such as additional racks, can be handled as a second phase without requiring fundamental changes to the first phase.

CYBERSECURITY AND PHYSICAL SAFEGUARDS

Heightened security is a business essential

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and legal mandate. Traditional construction contracts rarely address cybersecurity, including only basic physical security provisions such as site fencing and, maybe, access badges. Data center projects require far more: The cybersecurity and physical security provisions of the construction contract must be consistent with the sponsors' obligations. NIST (National Institute of Standards and Technology), ISO (International Organization for Standardization)[3] or other specifications can be referenced and applied. These and other obligations should be flowed down from the prime contractor into vendor agreements and subcontracts.

Temporary systems, open network ports, default credentials and uncontrolled site access can create significant vulnerabilities before turnover occurs. Contracts should therefore impose credential controls, secure configurations and documentation requirements throughout construction and commissioning.

RISK ALLOCATION

Standard consequential damages waivers, indemnity clauses and liability caps must be examined in light of unscheduled downtimes and other exposures that are unique to data centers.

Owners frequently seek broad remedies tied to lost revenue, hyperscaler service level agreement (SLA) penalties, or tenant claims. Yet those same owners and their stakeholders seek favorable price and schedule commitments. Contractors naturally resist these impositions, seeking limits on their liability and also consequential damages waivers. This battle should be expected. The negotiators on both sides should come to the table armed with well-defended positions on carveouts and collars. Particular attention should be paid to the interaction between performance guarantees and consequential damages waivers, as owners frequently seek meaningful remedies for failures affecting uptime, redundancy, cooling capacity or power availability.

Insurance should be viewed with data centers specifically in mind. Products include not only builder's risk property and commercial general liability coverage, but also professional liability, cyber and excess policies. Owner-controlled insurance programs and contractor-controlled insurance programs (OCIPs and CCIPs) covering liability risks for all onsite contractors and subcontractors should be evaluated.

CONTRACT ADMINISTRATION AND DISPUTE RESOLUTION

The successful project starts with good drafting but ultimately depends on good administration by trained staff and legal advisers on both sides of the contract. Contemporaneous documentation is critical. Disputes often involve overlapping causes such as utility delays, procurement disruptions, design evolution and commissioning failures. Without disciplined recordkeeping, parties may struggle to establish causation years later.

Structured escalation provisions can help reduce formal disputes by requiring executive-level negotiations before claims escalate to arbitration or litigation. Consistency should be sought among the forum and joinder clauses in construction, services and data-center tenancy agreements.

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Effective data center construction agreements will anticipate the integrated aspects of these complex facilities. Performance standards should be specific, commissioning tests should be measurable, responsibility allocations should be crisp, assumptions should be express, and remedies should be practical.

NOTES:

[1] https://constructandcommission.com/data-center-redundancy-n-n1-n2-2n-2n1-2n1-explained/.

[2] https://www.vertiv.com/en-us/about/news-and-events/articles/educational-articles/what-is-pue-power-usage-effectiveness-and-what-does-it-measure/.

[3] https://sharedassessments.org/blog/nist-vs-iso/?sa_silent_sso_checked=1.

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Facing a Federal Lawsuit, Texas County Repeals Blanket Pause on Data Center Construction, Adopting New Approval Procedures Instead

*Thomas G. Allen, Austin D. McCarty, Tad J. Macfarlan and Robert M. Smith**

In this article, the authors discuss a construction moratorium on new data centers enacted by a Texas county, the federal lawsuit that followed, and the county's decision to rescind the moratorium and to adopt a new approval process instead of the blanket prohibition.

As anti-data center sentiment grows nationwide, the legal strategies necessary to protect project investments are continually evolving. A construction moratorium on new data centers enacted in Hill County, Texas, was emblematic of a nationwide public backlash against data center development. The Hill County moratorium subsequently became the subject of a federal lawsuit filed in the U.S. District Court for the Western District of Texas. Thereafter, in response to that suit, the county rescinded the moratorium, adopting a new approval process instead of a blanket prohibition. While the new requirements may still be onerous for developers, the county's rush to amend its moratorium in the face of the lawsuit appears to validate the suit's premise that Texas counties lack broad authority to halt projects altogether. It also signals that regulators can act nimbly to sidestep legal challenges, all of which reinforces the need for an integrated legal strategy.

THE HILL COUNTY MORATORIUM AND THE LARGER TREND OF PUBLIC OPPOSITION

In early May, by a 3-2 margin, Hill County officials enacted a one year moratorium on new data center construction in unincorporated areas. The measure followed significant public opposition to the rapid influx of proposed data center projects. Residents expressed concern about the potential impacts on water use, electricity demand, infrastructure, and quality of life. The Hill County moratorium is part of a broader pattern of organized and official resistance to data center development. In our prior coverage, we identified several ways that public opposition is manifesting itself, in Texas and nationally, as a major risk factor for data center development.

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THE INDUSTRY PUSHES BACK

The Hill County moratorium predictably faced legal challenges. The first significant challenge arrived in the form of a federal lawsuit by a company claiming its once valuable purchase rights to acquire 800 acres in Hill County were rendered valueless by the moratorium. The plaintiff is challenging the county's authority to enact the measure and seeking compensation for an alleged taking in violation of the US Constitution, among other claims.

The suit is captioned *RCM Hill LLC v. Hill County*.[1] The complaint asserts a multipronged constitutional and state-law challenge to the moratorium, combining:

(i) federal and state declaratory judgment claims that the moratorium is ultra vires and void, including parallel claims for prospective injunctive relief against the county and its officials;

(ii) federal regulatory takings and inverse condemnation claims under the Fifth Amendment and Fourteenth Amendment (via 42 U.S.C. § 1983), alleging that the moratorium effects both a per se taking and, alternatively, a Penn Central taking by eliminating economically viable use and destroying investment-backed expectations;

(iii) a § 1983 due process claim (procedural and substantive) premised on arbitrary, unauthorized government action that allegedly alters property and entitlement rights without lawful authority or adequate process; and

(iv) parallel Texas constitutional claims including inverse condemnation under Article I, § 17, denial of due course of law and arbitrary and capricious government conduct under Article I, § 19, and impairment of contracts/retroactivity under Article I, § 16, all tied to the alleged retroactive imposition of a new approval regime that frustrates pre-existing contractual and development rights.

The *takings* claims may garner the most attention for their potential national application as a compensation mechanism for categorical data center prohibitions. However, in Texas specifically, whether a Texas county has the authority to impose such sweeping regulations is a central question. The complaint against Hill County alleges that Texas counties are creatures of statute with no inherent police power, and therefore, they may act only when authority is expressly granted or necessarily implied by statute or the state constitution—and no such authority exists for a data center (or any) development moratorium.

THE COUNTY ALTERS ITS APPROACH

In response to the lawsuit, Hill County has pivoted from an outright moratorium on data center development to a process-driven regulatory regime, rescinding the ban and replacing it with a formal development checklist and major industrial development review framework that compels developers to submit detailed, project-specific disclosures regarding infrastructure, traffic, and resource impacts before proceeding. Rather than prohibiting projects, the county's new approach functions as a front-end screening and information-forcing mechanism that subjects large-scale industrial developments to heightened scrutiny,

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transparency requirements, and compliance obligations—effectively shifting from categorical restriction to a structured review process that can influence project feasibility, timing, and cost without formally blocking development. Questions persist regarding whether the county has the authority to implement this new process and whether plaintiffs will continue their lawsuit in some amended form.

PRACTICAL TAKEAWAYS

Project participants, including developers, purchasers, investors, equipment suppliers, and contractors, need to anticipate prolonged risks from community opposition. Project participants should understand the benefits and risks of using litigation as a means of challenging local and state action that unduly restricts development and for potentially recouping investments.

Hill County's shift illustrates that categorical prohibitions invite ultra vires and takings challenges, causing local governments to possibly pivot to process-driven regulatory layering—leveraging disclosure requirements, infrastructure reviews, and public transparency mandates to influence (and potentially slow or deter) development without formally banning it.

For project participants, the takeaway is straightforward: risk allocation must now account not only for outright regulatory bars, but also for incremental, information-based approval regimes that can alter project economics and timelines just as materially.

SPOTLIGHT ON FOREIGN EQUITY INVESTORS

Federal and state regimes now treat data centers—and the land they occupy—as critical infrastructure tied to sensitive data, energy grids, and strategic assets. Laws like Texas SB 17 illustrate this shift by regulating not just how land is used but who is allowed to own or finance it, aligning with federal frameworks like the Committee on Foreign Investment in the United States, which scrutinize foreign investment in infrastructure for national security risks. Modern data center restrictions are as much about capital origin and geopolitical risk as traditional zoning or environmental concerns. As data center opposition evolves, expect more focus on the extent to which foreign participants could face restrictions.

Foreign stakeholders should also take care to investigate whether their investments qualify for investment treaty protections. Where applicable, investment treaties may offer stronger protection than domestic law for compensation for government interference in data center projects. Companies that operate in jurisdictions that have investment treaties with the United States should examine their deal structures to maximize treaty protections. Critically, once the dispute arises, it will be difficult to restructure an investment for the purpose of obtaining treaty protections. The key period for structuring investments for treaty protections is ideally prior to the investment being made but, in any case, before a dispute becomes reasonably foreseeable.

NOTES:

[1]RCM Hill LLC v. Hill County, No. 6:26-cv-00340 (W.D. Tex.).

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EPA Proposes to Loosen New Source Review "Begin Actual Construction" Limits: What It Could Mean for Data Centers and Other Capital Projects

*Karl F. Kumli and John D. Surma**

In this article, the authors discuss a new proposal from the U.S. Environmental Protection Agency that could speed up large construction projects, especially data centers.

A new proposal from the U.S. Environmental Protection Agency (EPA) would allow construction projects to conduct more site work before the New Source Review (NSR) permitting process, a change that could speed up large construction projects, especially data centers. EPA recently rolled out a proposed rule that would revise the NSR permitting regulations for new construction under the Clean Air Act to narrow what counts as prohibited pre-permit construction activity. This article discussed the proposal and four steps to consider now.

IN A NUTSHELL

In practical terms, the EPA is proposing to allow more site activity and construction of non-emitting infrastructure before an owner or operator obtains an NSR permit. However, the proposal would still require a permit before physical construction begins on equipment or components that emit or have the potential to emit regulated NSR pollutants. If finalized, the proposal could materially affect how developers plan large projects, which could grease the wheels of fast-moving data center developments, semiconductor facilities, energy infrastructure, and other industrial builds that often face friction between construction schedules and permitting timelines.

WHAT THE EPA PROPOSED

The EPA said the current NSR definitions of "begin actual construction" and related terms have been interpreted to bar certain permanent on-site work before a permit is issued. Types of work that have fallen into that category include: installation of supports and foundations, laying underground pipework, and construction of permanent storage structures. The EPA also explained that the existing approach has created "uncertainties, delays, and regulatory burdens" and does not reflect what the agency now views as the best reading of the Clean Air Act.

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To solve these issues, the EPA proposed to revise the definition of "begin actual construction" to mean, in general, the "initiation of physical on-site construction of pollutant-emitting activities on a stationary source."

The new definition would exclude several activities, allowing them to begin prior to the permitting process including:

- engineering and design planning,
- geotechnical investigation,
- clearing vegetation,
- grading, surveying, soil compacting and stabilization,
- excavation,
- ordering equipment and materials, storing equipment, and
- temporary construction trailers, and paving surfaces.

The EPA also proposed a new definition of "pollutant-emitting activities." Under that proposed definition, pollutant-emitting activities would include equipment or components in a process or operation that emit or have the potential to emit a regulated NSR pollutant.

The proposal would exclude several categories of structures and systems that were previously subject to at least a portion of the regulation, including:

- office buildings, retail stores, certain storage buildings,
- certain concrete pads and building foundations,
- walls, and roofs not specifically configured to support emitting equipment,
- HVAC for human workspaces,
- utility-service wiring and piping, and
- certain sealed junctions or tie-ins.

The EPA's stated policy objective is to move away from a test focused on whether work is "permanent" or "costly" and instead require a permit only before construction begins on components or equipment that emit air pollution.

WHY THIS MATTERS FOR DATA CENTER PROJECTS

For data center developers, the proposal could be significant for projects that need to move quickly while air permitting for emissions-related equipment is still pending. The EPA specifically stated that the rule is intended to allow construction of non-emitting components such as utility service infrastructure, concrete pads, and some buildings and building components before an NSR permit is obtained. The EPA also acknowledged that the proposed changes are intended to help owners and operators expedite completion of construction projects and to manage seasonal construction constraints more effectively.

For large developers, this could offer more schedule flexibility, preserve procurement windows, reduce weather-related delay, and better align commissioning schedules. That said, the proposal would not eliminate NSR permitting obligations for emissions-related units, and the EPA repeatedly emphasizes that the owner or operator is still responsible for compliance with applicable regulations for any pre-permit construction allowed under the rule.

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That caveat matters in the data center context. If later permitting requires design changes, additional controls, or reconfiguration of emissions-related systems, the EPA's proposal makes clear that prior site investment should not justify permit issuance. So, while the proposal could improve schedule optionality, it does not prevent permitting authorities from requiring redesign or denying a permit if the Clean Air Act's criteria are not satisfied.

BROADER IMPLICATIONS BEYOND DATA CENTERS

The proposal is not data center-specific and industries unrelated to data centers may see similar opportunities and risks.

For example, advanced manufacturing, semiconductors, life sciences, logistics, food processing, energy, chemicals, and other sectors often build substantial non-emitting infrastructure before or alongside installation of emissions-related equipment. The EPA also noted that stakeholders have raised concerns for years that the current rule delays projects and frustrates staged construction schedules, including where seasonal conditions constrain construction windows. Those concerns are hardly unique to data centers.

KEY CAUTIONS FOR PROJECT SPONSORS

Even if finalized, the rule would not give project sponsors a blank check to build first and permit later. The EPA made clear reviewing authorities will still need to make case-by-case, project-specific judgments, because it will be difficult to draw a regulatory line that addresses every circumstance. The EPA also stressed that other federal, state, and local requirements may continue to limit pre-permit activity, including other Clean Air Act requirements, other environmental statutes, and non-EPA permitting or licensing requirements.

If finalized, the rule is likely to become an important project-planning tool - but not a substitute for careful air permitting strategy. Working with subject matter experts in the environmental permitting space to collaborate with onsite planning will be key if the proposal goes into effect.

Accordingly, companies planning large construction projects should consider:

1. reassessing project sequencing assumptions for non-emitting site and structural work;
2. identifying which components may be viewed as specifically and uniquely configured to serve emitting equipment;
3. preserving flexibility in design and procurement in case permit conditions later require changes; and
4. evaluating state and local implementation issues, especially where approved SIP rules, delegated programs, or local interpretations may affect how quickly any federal revisions translate into practice.

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It's True: Long-Term Incentive Plan Unit Compensation Is a "Win-Win" for REIT Shareholders and Management

Edward L. Glazer, William T. Goldberg, Yoel Kranz, H. Neal Sandford,

*Ettore A. Santucci and Christopher L. Versfelt**

In this article, the authors discuss operating partnership unit-based compensation for chief executive officers of public real estate investment trusts.

In its May 31, 2026, report on Executive Compensation and Corporate Governance, research firm Green Street Advisors highlights numerous favorable trends in the public real estate investment trust (REIT) sector. The report notes that growth in chief executive officer (CEO) compensation in the REIT sector over the past five years has been less than that of S&P 500 companies and that annual pay for top executives at public REITs accounts in the aggregate for only 0.10% of enterprise value. At roughly one-fourth of total G&A, the report underscores that the G&A load for public REITs is smaller than that imposed by other real estate vehicles, such as non-traded REITs or private equity funds. In a companion "Heard on the Beach" column published the same day, Green Street also addressed executive compensation structures at public REITs, noting that operating partnership (OP) unit-based compensation is generally economically equivalent to traditional restricted stock awards with substantially similar accounting attributes, and the use of such compensation generally looks like a "win-win" for REIT shareholders and management teams.

A CRITICISM

After acknowledging these favorable trends and highlights, Green Street then advances a categorical criticism of OP unit-based compensation generally, arguing that it may create misalignment between management and shareholders. Green Street speculates that accumulated tax deferrals embedded in OP unit-based awards — so-called "tax time bombs" — might disincentivize affected executives from pursuing value-maximizing transactions. In the governance report, Green Street promptly acted on its view by increasing the weight given to the form of compensation in its governance framework, giving preference to companies with minimal usage of

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OP unit compensation practices. Governance scores relating to the use of OP unit compensation increased from 0% to 7% of the total score, resulting in overall REIT governance scores trending lower on average.

Green Street's governance scoring serves a valuable function in the public REIT sector and its annual executive compensation study is a genuinely useful resource for the REIT investment community. But corporate governance in the REIT sector is not one-size-fits-all, and Green Street has applied its revised methodology here with too broad a brush. Properly structured Long-Term Incentive Plan (LTIP) Unit compensation serves as a superior vehicle for aligning management and shareholder interests in the vast majority of cases. There are numerous variants in OP unit-based compensation for public REITs, including a variety of structuring alternatives and examples. Green Street's new check-the-box, one-size-fits-all approach seemingly penalizes a majority of its coverage universe overnight.

Specifically:

- *Available deal-structuring toolkit undermines the M&A friction argument*. The possibility of "tax time bombs" is a narrow, theoretical risk that is exceedingly unlikely to ever amount to "poor governance." In today's sophisticated deal-making environment, UPREIT go-private transactions are regularly structured to avoid LTIP gain recognition without any price reduction, using techniques similar to those deployed to avoid triggering tax protection liability for property contributors. Focusing solely on hypothetical — and in practice remote — risks ignores this entire toolkit and presents as a systemic governance problem what sophisticated practitioners resolve as a routine deal-structuring question.

- *The entrenchment argument has no empirical foundation*. The research report offers no case studies, no regression analysis, and no evidence that any REIT has rejected a value-maximizing transaction because of accumulated LTIP Unit gains, and makes no attempt to show that accumulated LTIP Unit gains are material relative to enterprise value, deal premiums, or change-of-control payments. Indeed, the theoretical entrenchment concern would apply with equal force to the vastly broader universe of corporate insiders holding unrealized gains in restricted stock, stock options, and deferred compensation — yet no governance rating agency penalizes those. There does not appear to be any principled basis for singling out LTIP Units or the REIT sector specifically.

- *LTIP Units are not the same as contributor OP units*. The reports appear to conflate OP unit compensation with OP unit contribution transactions. In addition to the fact that OP unit contribution transactions typically represent a much higher dollar value than LTIP awards, another important distinction is that LTIP Units generally do not have "negative capital accounts" or negative basis to the same extent as is commonly found in OP Unit contributions. Negative capital account recapture in OP unit contribution transactions can lead to tax liabilities that substantially diminish the economic return to an OP contributor. This is not the case with LTIP Units.

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- *Penalizing tax efficiency has no precedent in governance practice*. Green Street's governance scoring has always appropriately focused on *how much* an executive receives, not *how that receipt is taxed*. Penalizing LTIP Unit use based on the latter question imports a notion of mandatory tax equivalence between executives and shareholders that has no precedent in governance practice and no rational basis in the broader compensation market.

- *A uniform approach is simply the wrong analytical tool*. Green Street shifted five governance points from "Business Dealings with Management" to "Divergent Tax Basis of Insiders" on the grounds that divergent insider tax bases are "more widespread than previously thought." That methodological change penalizes 59% of Green Street's coverage universe without regard to the type, terms or design of the awards. The appropriate framework would be to evaluate the type of LTIP Unit instruments granted and a host of other factors. A check-the-box, one-size-fits-all approach cannot substitute for that analysis.

MITIGATING CONCERNS

In particular, the following features of LTIP Units both mitigate the concerns articulated by Green Street and amplify the alignment between REIT executives and shareholders:

- *Distinctions between different instruments*. LTIP-based compensation generally includes both awards designed to replicate restricted stock and awards designed to replicate options, and these have materially different economic profiles and alignment dynamics. Both variations can be designed with the full panoply of performance and/or time-vesting features to create maximum alignment between management and shareholders without the economic compulsion of liquidating incentive equity upon tax gain recognition at vesting. Thus, LTIP Units intrinsically increase "skin in the game" for management. In addition, awards designed to replicate options have zero value unless the stock price increases, making them more shareholder-aligned than restricted stock. A single framework that treats these instruments identically misses the mark.

- *Grant sizing dynamics can favor shareholders*. Because LTIP Units carry book-up risk (i.e., the risk that the unit never achieves economic parity with a common unit), they typically carry a lower GAAP fair value than comparable stock awards. No-sale covenants post-vesting further reduce FFO burn. On a pound-for-pound dilution basis, LTIP grants frequently represent both lower economic cost and lower dilution to shareholders than equivalent share-based awards. Green Street's penalty focuses, in part, on the failure of tax savings to trickle down to shareholders through reduced G&A expenses, which is the wrong lens through which to evaluate LTIP Unit compensation.

- *The book-up mechanic and high water mark provisions directly refute the entrenchment argument*. Standard high water mark provisions restrict book-gain allocations to LTIP Unit holders unless the

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stock price exceeds its level at grant. Underwater LTIP Units may be economically worthless, and upon a change of control, vested FVLTIP Units whose book capital accounts have not reached the target balance will suffer an economic loss that would not have occurred with restricted stock. The executive may receive nothing for those units in a take-private. The entrenchment dynamic Green Street posits therefore runs the other way: underwater LTIP Units give executives an incentive to push for a higher deal price, not to block a transaction.

- *Holding period requirements reinforce alignment*. LTIP plans typically require recipients not to transfer units for at least two years from grant, and long-term capital gain treatment may require a three-year holding period under the carried interest rules. These constraints make LTIP Unit holders structurally more committed to long-term REIT performance to avoid the carried interest rules risk than restricted stock recipients, who can sell shares at vesting to cover taxes and monetize the balance of their award far sooner.

- *Deferral of taxation further strengthens alignment*. Executives who defer tax recognition maintain deeper, longer-dated exposure to REIT stock performance than those in traditional awards who have already monetized shares at vesting and may be incentivized to diversify.

CONCLUSION

Green Street's governance scoring serves a highly valuable function in the public REIT sector. Nevertheless, the merits of including OP unit currency in the incentive equity programs of public REITs should be discussed.

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U.S. Securities and Exchange Commission's Registered Offering Reform Proposal: A Potential Game-Changer for Public Non-Traded REITs

*Mary Katherine Rawls and Heath D. Linsky**

In this article, the authors discuss a proposal that would preempt state "blue Sky" registration and qualification requirements for all Securities and Exchange Commission registered offerings, including those of non-traded REITs.

BACKGROUND: THE CURRENT BLUE SKY REQUIREMENTS FOR NON-TRADED REITS

Public non-traded real estate investment trusts (non-traded REITs) that register their offerings with the U.S. Securities and Exchange Commission (SEC) under the Securities Act of 1933, as amended (Securities Act), have long been subject to a fragmented patchwork of state securities regulation. Under current law, Section 18(a) of the Securities Act restricts states from imposing registration or qualification requirements only on covered securities. Exchange-listed securities enjoy this protection, while unlisted securities, including shares of non-traded REITs, do not.

As a result, sponsors and issuers of non-traded REIT programs have been required to register or qualify their offerings in each state where securities are offered and sold, navigate state-specific merit review standards, comply with varying investor suitability requirements, and pay state-level registration fees — all in addition to the SEC registration process. States such as Iowa, Kansas, Kentucky, Nebraska, and New Jersey historically have imposed concentration limits and minimum net worth thresholds on non-traded REIT investors, creating compliance complexity that can slow deal timelines and add material cost to capital raises.

These requirements have long been viewed as inconsistent with the level of federal oversight already applicable to registered offerings, and as creating an unlevel playing field relative to other investment vehicles, such as private placements under Rule 506 of Regulation D or registered closed-end funds, to which state-level preemption applies.

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THE PROPOSED RULE: HOW PREEMPTION WOULD WORK

The Statutory Mechanism: Qualified Purchaser Definition

Release No. 33-11418 (the Offering Release)[1] uses a targeted statutory mechanism to achieve blanket preemption. Section 18(b)(3) of the Securities Act provides that a security sold to a qualified purchaser is a covered security exempt from state Blue Sky registration and qualification requirements. While Congress granted the SEC authority to define qualified purchaser by rule, the Commission has not previously exercised that authority with respect to registered offerings.

The Offering Release proposes to change that by defining "qualified purchaser" to mean "any person to whom securities are offered or sold pursuant to an offering registered under the Securities Act." By using this expansive definition, every investor in any SEC-registered offering, whether listed or unlisted, would become a "qualified purchaser," thereby rendering all such securities "covered securities" shielded from state registration and qualification requirements.

The proposed definition is intentionally broad and is not limited to any particular issuer type, securities class, or registration form. Non-traded REITs registering on Form S-11 would benefit equally alongside other issuers of unlisted securities.

IMPACT ON NON-TRADED REITS: WHAT CHANGES?

Cost Savings and Operational Efficiencies

If the proposal is adopted, non-traded REIT sponsors and their counsel can expect meaningful operational and financial benefits, including:

- *Elimination of multistate Blue Sky counsel costs*. Sponsors currently engage specialized securities counsel to advise on, prepare, and file registration or qualification documents in each state of offering. This engagement would largely be eliminated for the compliance filing function.
- *Reduction in offering delays*. State merit review timelines — which can vary significantly from state to state — have been a consistent friction point for non-traded REIT capital raises. Preemption would remove this bottleneck.
- *Simplified investor eligibility determinations*. The myriad of state-by-state investor suitability requirements and concentration limits would be replaced by a uniform federal standard, simplifying the subscription process for dealers, advisors, and transfer agents.
- *Reduced ongoing compliance burden*. Annual Blue Sky renewal filings, supplemental state filings triggered by offering updates, and tracking of varying state-level expiration dates would no longer be required.

Offering Prospectus and Subscription Document Changes

Non-traded REIT offering documents currently contain extensive state-specific disclosure, including the investor suitability requirements and concentration limits imposed by individual state regulators, sometimes spanning multiple pages in a front section of the

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prospectus. If preemption is adopted, these disclosures and related subscription document provisions would no longer be required as a regulatory matter, substantially streamlining offering documents.

NASAA REIT Guidelines and Charter Provisions

Most non-traded REITs are required to adopt charter provisions based on the NASAA REIT Guidelines to satisfy the requirements of state securities regulators in connection with Blue Sky registration. If the SEC's proposed definition of "qualified purchaser" in the Offering Release preempts state registration and qualification requirements for non-traded REIT offerings, sponsors will need to evaluate whether, and to what extent, those NASAA-based charter provisions remain necessary or appropriate from a regulatory and market perspective.

While the proposal would eliminate the need to conform charters to state merit-review positions as a condition of qualification, it would not, by itself, amend or override existing charter terms that have already been incorporated into organizational documents. Sponsors should consider, in consultation with counsel, whether future charter amendments or new program formations should continue to track the NASAA REIT Guidelines in whole or in part, taking into account investor expectations, exchange-listing considerations, and any residual state law or corporate law requirements.

BROADER CONTEXT: PART OF A SWEEPING OFFERING REFORM PACKAGE

The Blue Sky preemption proposal is one component of the most significant overhaul of the registered offering framework since the SEC's 2005 Securities Offering Reform. The broader Offering Release also proposes to:

- Dramatically expand Form S-3 eligibility by eliminating public float and seasoning requirements, allowing more issuers to access the short-form shelf registration process.
- Streamline shelf registration procedures and extend enhanced communication and registration accommodations to a broader range of issuers.
- Modernize Form S-1 to reduce administrative friction in the IPO and initial registration process.
- Align these changes with a companion rulemaking (Release No. 33-11419, the Filer Status Proposal) that would overhaul the Exchange Act filer status classification system, which is the most significant update to that framework in over two decades.

SEC Chair Paul Atkins has framed this package as part of a broader agenda to revitalize the U.S. public markets, reduce unnecessary regulatory friction, and make registered offerings more accessible to a wider range of companies and investors.

IN SUMMARY

- The SEC has issued the Offering Release proposing sweeping amendments to the registered offering framework.
- Among the most consequential changes for the real estate industry: the proposal

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would preempt state "Blue Sky" registration and qualification requirements for all SEC-registered offerings, including those of non-traded REITs.

- If adopted, sponsors and issuers of non-traded REIT programs would no longer face the significant costs and administrative burdens of multistate Blue Sky compliance.

CONCLUSION

The Offering Release represents a potentially transformative development for the non-traded REIT industry. If adopted as proposed, it would deliver long-sought relief from the costs and administrative complexity of multi-state Blue Sky compliance, placing non-traded REIT offerings on equal regulatory footing with other registered and private investment vehicles.

NOTES:

[1] https://www.sec.gov/files/rules/proposed/2026/33-11418.pdf.

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Valuations of Ownership Interests in Early-Stage Developments

*Dharminder Kalsi and David Emma**

In this article, the authors explain how to value early-stage development interests using a disciplined, market-based analysis.

Valuing ownership interests in early-stage real estate development projects requires discipline, economic clarity, and a careful understanding of how risk evolves over time. Too often, development-stage interests are treated as if they exist in a static condition of heightened uncertainty simply because construction has not yet been completed. That framing is incomplete. Development risk is not binary - it is dynamic, milestone-driven, and progressively reduced over time. Valuation approaches that fail to reflect this progression risk producing conclusions that are economically inconsistent with how investors actually price these assets.

When capital is first raised for a development project, risk is typically at its highest point. During conceptual underwriting and feasibility analysis, investors are evaluating projections, preliminary budgets, and assumptions that remain subject to regulatory approval, financing availability, and execution feasibility. Land may not yet be fully controlled, entitlements may be pending, construction pricing may not be locked, and financing may be indicative rather than committed. At this stage, investors demand elevated target returns precisely because multiple layers of uncertainty remain unresolved.

As the project advances, that uncertainty does not remain constant. Site control eliminates acquisition uncertainty, entitlements reduce regulatory risk, binding debt commitments mitigate capital availability concerns, execution of guaranteed maximum price contracts narrows cost-overrun exposure, and full equity funding eliminates fundraising risk. Each milestone removes a discrete layer of risk and uncertainty that was previously embedded in required returns. When uncertainty declines and projected economics remain intact, required rates of return compress. If expected cash flows are unchanged, value logically increases as risk is reduced.

WHY CONSTRUCTION ALONE DOES NOT JUSTIFY STEEP DISCOUNTS

Despite this progression, it is sometimes suggested that once a project is under construction, the equity should be significantly discounted because of "construction risk." That

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position oversimplifies the risk profile. A project that has secured land, obtained permits, closed on construction financing, fully raised equity, and commenced vertical development is materially less risky than it was at inception. Construction risk - while real - typically consists of execution risk, schedule risk, and budget performance within a defined framework.

VALUATION DISCIPLINE IN ESTATE AND GIFT PLANNING

This analytical framework becomes especially important in estate and gift planning contexts. In recent years, there has been a noticeable increase in transfers of early-stage development interests as part of intergenerational wealth planning. The rationale is understandable. Development projects often experience meaningful appreciation upon successful completion and stabilization. Transferring interests earlier in the lifecycle may shift future appreciation to the next generation while potentially minimizing use of lifetime exemption amounts. From a planning standpoint, such strategies may be entirely appropriate.

However, valuation discipline does not change simply because a transfer is tax-motivated. Fair market value remains defined under Revenue Ruling 59–60 as the price at which property would change hands between a hypothetical willing buyer and a willing seller, where: (i) both parties have reasonable knowledge of all relevant facts and are acting in their respective best interests, and (ii) neither party is under any compulsion to buy or sell. The ruling emphasizes consideration of the nature of the business, its financial condition, earning capacity, and, importantly, actual arm's-length transactions involving the subject interest. Statement on Standards for Valuation Services No. 1 similarly requires that the analyst consider relevant data and avoid unsupported assumptions. These principles are especially critical when a valuation is performed shortly after capital formation.

THE IMPORTANCE OF MARKET EVIDENCE - AND THE RISK OF DOUBLE COUNTING

If, for example, equity was raised in June at negotiated arm's-length pricing among informed investors who fully understood development risk, and a gift valuation is performed in November, the presence of a recent transaction becomes highly probative. Investors who contributed capital were aware that the funds would be deployed into a development project subject to construction risk, financing risk, illiquidity, and minority position constraints. Those risks were not newly discovered after closing; they were the foundation of the pricing decision.

To conclude that the same interest is materially worth less only months later, solely because construction has commenced, requires a compelling economic explanation. Absent a material intervening event such as cost overruns, financing deterioration, entitlement loss, or adverse market shifts, discounting below recent subscription pricing risks double counting uncertainties that investors explicitly accepted and priced only months earlier.

ILLIQUIDITY AND THE MYTH OF "NO MARKET"

Another common argument in support of steep discounts is the perceived absence of a secondary market for early-stage development interests. Companies sometimes assert that because minority interests in projects under

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construction rarely trade, there must be "no market," and therefore significant discounts are justified. That reasoning conflates illiquidity with lack of value. This is a critical distinction that is often misunderstood in practice. The more analytically sound question is not whether transactions are occurring, but why they are not occurring.

Development capital is intentionally patient capital. Investors contribute funds with the expectation of remaining invested through completion, lease-up, stabilization, and eventual exit via refinance or sale. An investor who contributes capital in June is not entering the transaction with a November exit strategy in mind. The absence of secondary transactions during the natural lock-in period of a development project often reflects alignment with the originally contemplated hold period, not a lack of economic value. Lack of observed trades is not evidence that no buyer would exist at a market-clearing price. It may simply reflect transfer restrictions, sponsor consent requirements, lender approval provisions, or investor preference to remain invested until the business plan has been executed.

It is important not only to recognize the difference between a lack of evidence and evidence demonstrating the absence of value, but - more critically - to avoid conflating the former with the latter. The fair market value standard assumes a hypothetical willing buyer and willing seller. It does not require proof that frequent transactions occur. Many valuable assets trade infrequently. Illiquidity may justify a marketability discount, but the magnitude of that discount must be grounded in empirical analysis and must reflect the actual expected holding period. Penalizing an investment for behaving exactly as designed - remaining illiquid during construction - does not align with economic reality.

LIMITATIONS OF LIQUIDATION-BASED VALUATION APPROACHES

A related analytical shortcut is the reliance on a hypothetical liquidation approach as a primary valuation framework. Under this framework, the analyst asks what each equity layer would receive if the project were liquidated immediately during construction. While liquidation analysis can serve as a sensitivity, it should not define valuation unless distress or abandonment is a realistic outcome. No investor contributed capital assuming that the project would be liquidated mid-construction. The investment thesis was based on completion, stabilization, and realization of projected cash flows. To disregard that income-based framework and value the interest solely on a forced liquidation premise ignores the economic basis upon which capital was raised.

The distortion becomes particularly evident when examining general partner promote or carried interest structures. In many development partnerships, sponsors participate only after preferred returns and capital have been returned to limited partners. Under a hypothetical mid-construction liquidation scenario, the promote layer might receive nothing. Yet it is difficult to find evidence in the marketplace that a sponsor would transfer its promote interest for zero consideration while the project remains on track. The sponsor's entitlement to future upside is tied to the successful execution of the development plan. That contingent upside is precisely what motivated the sponsor to assemble the site, secure entitlements, raise capital, and manage execution. A liquidation-only framework artificially sup-

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presses that economic potential unless distress or abandonment is probable.

None of this suggests that liquidation analysis is irrelevant. If a project faces credible abandonment risk, financing failure, or material impairment, a liquidation premise may be appropriate. Professional standards require that valuation reflect known or knowable conditions as of the valuation date. But where development is proceeding consistent with the business plan, the valuation premise should reflect continuation, not premature termination.

ALIGNING VALUATION WITH ECONOMIC REALITY

Ultimately, valuation must mirror how informed market participants analyze development opportunities. When capital is raised, investors price risk based on forward-looking income expectations. As milestones are achieved, uncertainty declines. Recent arm's-length transactions provide powerful evidence of value. Illiquidity during the intended hold period does not equate to worthlessness; And hypothetical liquidation during construction does not define economic reality in a non-distressed project.

A DEFENSIBLE AND COHERENT VALUATION FRAMEWORK

Early-stage development interests can be effective vehicles for intergenerational wealth transfer but fair market value must be grounded in disciplined analysis. Professional standards do not prohibit discounts. They require that discounts be supported, coherent, and economically justified.

Critically, any value conclusion should be tested against the implied yield on equity at the concluded value to make sure that construction and development risk has not been overstated.

When investors subscribe to a development partnership at arm's-length pricing, they do so with full knowledge that the project will enter construction, that capital will be illiquid during the build period, and that cash flow realization is contingent on successful completion and stabilization. Construction risk is not a condition that emerges after closing - it is the central premise of the investment and is already embedded in the return expectations that informed the original pricing.

To then conclude, months later, that the interest has materially declined in value solely because the project is now under construction is to penalize the investment for doing exactly what it was designed to do.

If the project is progressing on schedule and on budget, with no material adverse change in market conditions, financing, or entitlements, the burden falls on the analyst to explain what economic event justifies a departure from the pricing established by informed participants.

A valuation that applies elevated discount rates to capture construction and lease-up risk in the projected cash flows, and then applies further entity-level discounts that implicitly reflect the same uncertainties, risks producing an implied return requirement that no rational market participant would demand for a performing development asset - a clear signal that risk has been double-counted.

In real estate, where risk is progressively retired as milestones are achieved and where the capital stack directly governs cash flow priority, this type of cross-check is not merely

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academic, it is essential to producing a conclusion that a hypothetical willing buyer would find credible.

A defensible valuation tells a consistent story; one that aligns milestone-based risk progression, market evidence, income expectations, and the legal rights of the equity holder into a conclusion that reflects economic substance rather than opportunistic interpretation.

AN ILLUSTRATIVE EXAMPLE

The implications of this framework are best illustrated in a practical context. (This example is provided solely for illustrative purposes and is not based on any specific transaction, client engagement, or actual event. Any resemblance to real projects or circumstances is purely coincidental.)

> Consider a multifamily development where equity is raised in June 2025 at par, based on a conventional development pro forma assuming a three-year hold, stabilized assumptions and cap rates supported by market conditions, and a target IRR that compensates investors for entitlement, construction, lease-up, and exit risk. At the time of closing, investors understand that the project is illiquid, subject to construction risk, and dependent on future market conditions. These risks are embedded in the underwriting and reflected in the required return.
>
> By November 2025, the project has achieved several milestones: land acquisition has closed, entitlements are in place, construction financing has been executed, and a guaranteed maximum price contract has been signed in line with initial underwriting budgets. No adverse events have occurred, and projected cash flows remain unchanged. While construction is underway and the investment remains illiquid, several key sources of uncertainty have been eliminated.

In this context, concluding that the same equity interest is worth materially less than its recent subscription price - absent new negative information - requires the analyst to identify which risks have increased since the initial investment date. Applying an incremental discount, simply because construction has commenced, may result in double counting risks that investors explicitly accepted and priced only months earlier. A defensible valuation would instead consider how milestone achievement affects required rates of return. See Table 1.

This example highlights the central issue: absent new negative information, applying incremental discounts to subscription pricing simply because development has progressed risks distorting value rather than refining it.

GROUNDING VALUATION CONCLUSIONS IN ECONOMIC REALITY

Appropriately supported discounts may still be significant; the focus should be making sure they are analytically defensible and aligned with how market participants would price the interest. Given the technical and fact-specific nature of these valuations, engaging seasoned professionals is essential to developing an analysis that is rigorous, well documented, and defensible under IRS scrutiny.

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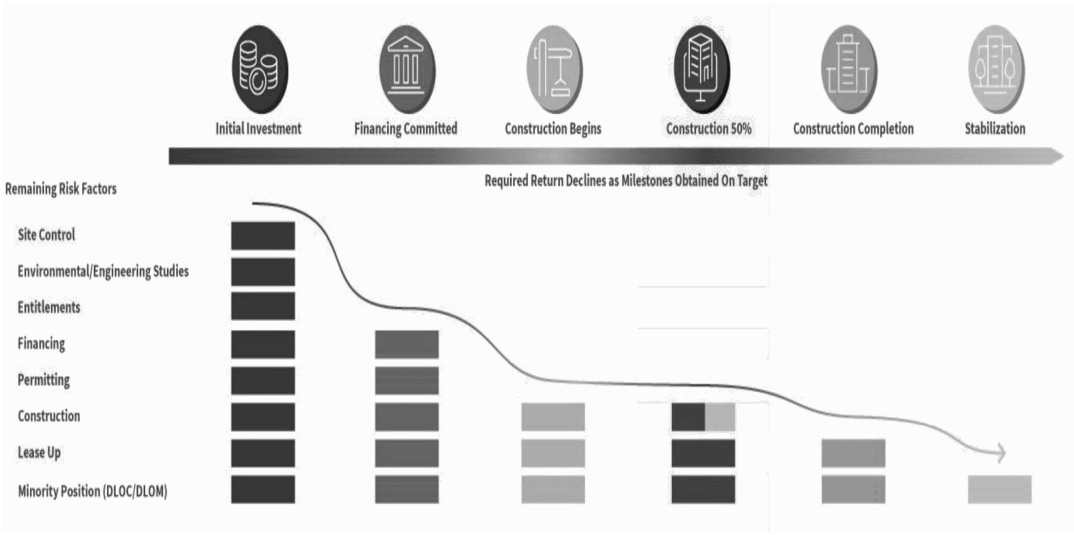
Table 1



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California's OHCA Publishes Draft Regulations to Capture Health Care Transactions With Private Equity, Hedge Funds and MSOs

*Paul A. Gomez, Ashley N. Osak and Matthew T. Lin**

In this article, the authors discuss proposed regulations that, among other things, demonstrate the interest of California's Office of Health Care Affordability in details of the arrangements between private equity groups and California health care entities and the impact of transactions on real estate where health care is delivered.

California's Office of Health Care Affordability (OHCA) has published draft regulations that would implement the expansion of its jurisdiction to address private equity, hedge funds and certain management services organizations (MSOs). The regulations are meant to hone the filing requirements expanded by statute in AB 1415, which went into effect at the beginning of the year, but OHCA has also taken the opportunity to revise certain requirements and procedures that are not captured by AB 1415. The expanded scope of OHCA's regulations will capture a greater number of transactions in California, and will require that investors consider potential transaction timeline impacts and the scope of diligence related to anticipated investments, among other strategic considerations. The initial draft of the proposed regulations demonstrates a maximalist expansion of OHCA's jurisdiction and will likely be further revised in the coming months to refine the language and resolve conflicts in the current draft.

OHCA's proposed changes are described below.

PROPOSED CHANGES TO DEFINITIONS, THRESHOLDS AND REPORTED MATERIAL CHANGE TRANSACTIONS

- "Management Services Organization" would be defined to include entities providing services described in AB 1415 (i.e., entities providing management and administrative support services for a provider, as that term is defined by OHCA) and require one of the following factors: (1) it is owned by a hospital and has two or more physician organizations as clients or affiliates; (2) it employs the

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physician-owner of one or more physician organizations, or otherwise has an agreement with the physician-owner or one or more physician organizations that defines the services to be provided and compensation for such services; (3) it shares directors, officers, investors or other natural persons with the ability to exercise control with respect to a health care entity; or (4) it is affiliated with at least two of the following: (A) a health plan, (B) two or more physician organizations, or (C) a hospital. It is worth noting here that references to physician organizations do not appear to pertain only to those with 25 or more physicians—assuming that is correct, an entity might qualify as a "management services organization" for OHCA purposes even if it manages one or two small physician practices, depending on the circumstances.

- "Submitter" would include both health care entities and noticing entities. Further, it would also include entities that are referred by another California state agency to provide notice. This implies that OHCA may seek to obtain notices from parties that are otherwise excluded by OHCA's governing law if it obtains a referral for notices from other agencies.

- Asset and revenue thresholds for health care entities would be largely preserved (generally requiring the health care entity to have $25 million or $10 million in California assets or revenues), but the language was expanded to address transactions involving private equity groups, hedge funds and MSOs. However, although not entirely clear, the regulations appear to exempt MSOs for the thresholds in transactions where a private equity group or hedge fund is acquiring 5% or more of the assets, equity, debt or liabilities of an MSO. The proposed regulations would benefit from more clarity on this point.

- A new type of material change transaction would be added for private equity or hedge fund acquisitions of health care entities or MSOs. The change specifically captures transactions resulting in a private equity group or hedge fund holding 5% or more of the assets, equity, debt or liabilities of a health care entity or an MSO. The change also captures transactions resulting in the acquisition of assets, equity, debts or liabilities where the private equity group or hedge fund has the authority to do any of the following: (1) appoint, or replace leadership or governing body members of the health care entity or MSO; (2) vote on decisions made by a health care entity or MSO; (3) alter operations by expanding or reducing health care services offered by the health care entity or changing arrangements with MSO or payers; (4) purchase the real property of a health care entity where services are provided and lease the property back to the health care entity; (5) cause, require, approve or veto the incurrence of indebtedness by the health care entity or MSO; (6) manage or operate a health care entity or MSO, such as through management agreements, consulting agreements, administrative services agreements or affiliated MSOs; (7) charge fees to the health care entity or MSO; or (8) spend the capital and net

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income of a health care entity or MSO, such as by approving, directing, restricting or controlling budgets, capital expenditures, distributions or the use of net income or tax reserves.

- A new type of material change transaction would be added for transactions involving MSOs, including transactions that result in (1) an MSO providing management and administrative support services for a health care entity with at least $25 million in California assets or revenue; (2) an MSO providing management and administrative support services for two or more providers that collectively generate $10 million annually from California patients; or (3) involve the transfer of control, responsibility or governance, in whole or in part, of the MSO, or the change in 25% or more of the MSO's ownership. At present there appears to be some potential overlap and duplication with the prior MSO-related type of material change transaction noted immediately above.

- A new type of material change transaction would be added for real estate transactions where a health care entity provides health care services, including transactions involving the sale or transfer of such real estate to an entity other than the entity acquiring health care entity or its direct parent and that require the surviving health care entity to lease or pay rent for the real estate.

PROPOSED CHANGES TO DISCLOSURE REQUIREMENTS

- Required information in notices to OHCA would be updated to address private equity, hedge funds and MSOs. Among others, the additional disclosed information includes: the owners of any real property involving the transaction where services are provided; the types of services provided by an MSO and its geographic service area; the names of health care entities or MSOs owned or financed by the participating asset managers and funds managed by private equity groups or hedge funds; names of all affiliates, parents and subsidiaries of the submitter; names of all members of the submitter's governing body; each party to a transaction's affiliation with an MSO and other parties to the transaction; anticipated cost savings, quality investments, price reductions or services expansions as a result of the transaction; descriptions of post-transaction changes to the identification of all entities or persons with 5% or more ownership in each entity, including intermediate entities, entities controlled by the acquiring entity and any such entities or persons with 5% or more ownership that will exist post-transaction; changes to voting rights, decision-making authority and management and compliance structures of the submitter and parties to the transaction; and changes to real estate where health care services are provided, including sales, transfers to affiliates, encumbrances or updates to landlord-tenant agreements.

- OHCA added new documents to be submitted with notices to address private equity, hedge funds and MSOs. These new documents include copies of lease-back agreements; organizational charts

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for any party to or subject of a transaction up through the ultimate parent entity and including any subsidiaries, organizational charts for any health care entity or noticing entities that show all entities or persons with 5% or more ownership in the entity, and proposed post-transaction organizational charts. Private equity groups and hedge funds are also required to provide documentation showing names of all health care entities and MSO in the portfolios of participating asset managers, as well as documentation showing the ratio of debt to enterprise value or ratio of debt to equity, the source of any debt and the post-recapitalization debt ratio for any acquired health care entity or MSO.

PROPOSED CHANGES TO COST AND MARKET IMPACT REVIEWS

- The procedure for requesting expedited review of notices of material change transactions was mostly unchanged. However, OHCA added that it would consider urgent situations not of the submitter's own making, such as a public health emergency, natural disaster or legal mandate, in which the public interest would be best served by an expedited review.
- In deciding whether to conduct a CMIR, OHCA added that it would consider as a factor the involvement of a real estate investment trust (REIT) in a transaction that could weaken the financial status of the health care entity or risk access to care.
- If a party requests review of the determination to conduct a CMIR, OHCA's director would be allowed to remand the determination upon receipt of new information submitted in the party's request for review, upon which OHCA would have 30 days to conduct an additional review as directed in the remand order. The 30-day review period could be tolled if needed to review voluminous information or if additional information or documents are needed.
- During a CMIR, OHCA may request the production of additional documents and information as part of its review. The party subject to the review would be permitted to request confidentiality of the documents in accordance with OHCA's current procedures for requesting confidentiality.

IN SUMMARY

- OHCA has published draft regulations that expand its pre-transaction notice requirements to transactions involving private equity groups, hedge funds, certain management services organizations and newly created entities entering into transactions with health care entities.
- OHCA also proposed revised standards and procedures in its existing regulations, including adding information and documents to be disclosed and refining the procedures for conducting Cost and Market Impact Reviews.
- Among other focuses, the proposed regulations demonstrate OHCA's interest in details of the arrangements between private equity groups and California health care entities and the impact of

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transactions on real estate where health care is delivered. Some of the new standards and requirements bear a notable resemblance to language used in some terms of the recent proposed settlement between the California Attorney General and a private equity owned dental services organization, suggesting that the Office of the California Attorney General and OHCA may be in communication on this front to help ensure more broad review of certain key elements of some health care transactions.

- The proposed new submission requirements would impose significant additional burdens on private equity and hedge fund investors as well as California health care entities that would like to receive investments of capital and enter into transactions with them, potentially deterring further investment in some cases. Greater scope of review by OHCA and significant additional submission burdens placed on private equity and hedge funds in the health care sector may result in longer review times, further delayed investments and higher transaction costs for health care investors and providers in California.

CONCLUSION

Many of OHCA's proposals may dissuade or delay investment by private equity groups and hedge funds in California's health care market. The proposal sets low thresholds for new potential filing requirements and would require an increased amount of information to be provided in transaction notices. While OHCA still does not have the authority to approve or disapprove a transaction, the long delays and expansive disclosure requirements will likely impact considerations by health care investors and providers as they evaluate entering into or expanding their presence in the California market. The thresholds and disclosure requirements for MSOs should also be further refined to add clarity as to the types of transactions involving MSOs that are subject to notice.

Investors and providers in the California health care industry should continue to monitor the development of these regulations to evaluate whether future transactions may be subject to pre-closing notice and if so, balance the potential additional time and cost-related burdens against the expected benefits and value of pending or anticipated transactions on the horizon for later this year and beyond.

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New York State Enacts Pied-à-Terre Tax on Expensive Non-Primary New York City Residences

*Stuart M. Saft**

In this article, the author analyzes the new Pied-à-Terre Tax enacted by New York.

The New York State Legislature has enacted the 2026–2027 New York State Budget Bill, Part HH of which amends Article 30-C of the New York State Tax Law by adding Sections 1350 to 1356 titled "City Surcharge on Property That Does Not Serve as a Primary Residence." Also amended are the New York City Administrative Code and City Charter to provide the mechanism to collect the "surcharge" and enforce the new law.

To avoid confusion, this article will describe the surcharge[1] as a Pied-à-Terre Tax (PAT Tax). This article is subject to clarification by the New York City Department of Finance (DOF), the agency that will interpret the new law, enforce it and issue regulations explaining it. The law likely will be the subject of state and federal court litigation as a result of the speed in which the PAT Tax was enacted and the absence of public scrutiny prior to its enactment or a public hearing. Like the Housing Security and Tenant Protection Act of 2019, which applied parts of the landlord-tenant law to co-ops, and radically changed the law, there was no transparency prior to its enactment.[2]

It is not certain that all legislators were given the opportunity to review the legislation before they voted on it because several members, before voting, told their constituents that what was in the bill was not in the bill, and it seems those legislators were incorrect in their claim.

EFFECTIVE DATE AND OVERVIEW

The PAT Tax Law (PAT Law) became effective July 1, 2026 (but because it applies to obligations that have occurred since January 1, 2026, it has a retroactive aspect) and sunsets on June 30, 2031, unless extended by the Legislature. Because tax laws rarely get rescinded, it is likely a permanent addition to the taxes owed to the state and city that already have the highest taxes in the country - a standing that was made worse when the U.S. Congress eliminated New Yorkers' ability to deduct most of their state and local taxes payment on federal tax returns - leaving most highly paid individuals paying more than 50 percent of their income in city, state and federal taxes.

The PAT Tax applies to any "covered owner"

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of a "covered property" that does not qualify as a primary residence. A covered owner includes owners of Class 1 (1–3 family) residential property, tenant-stockholders of cooperative corporations, owners of residential condominium units, beneficial owners of trusts that are the sole beneficiaries holding such property, and majority partners, shareholders or members of partnerships, corporations or limited liability companies (LLCs) holding such property. (Note: There is an open question as to whether the individual owner of an entity that owns an entity owning property is exempt.) For the sake of clarity, the co-op and condo units will be referred to in this article as "Apartments."

Owners of primary residences located in New York City are not impacted, even if they own multiple homes, because they already pay (or should pay) New York City and New York state income tax. However, an owner of a primary residence in New York state, but outside of New York City, with a non-primary New York City residence will be impacted if they do not pay New York City taxes.

"Covered property" includes non-excluded residential property classified as Class 1 property (e.g., 1–3 family homes) other than vacant land, Class 2 residential cooperative property in which at least one apartment meets the value threshold and is not a shareholder's primary residence and Class 2 residential condominium apartments. Excluded property to which the PAT Tax does not apply includes (1) property lacking a required certificate of occupancy, and (2) newly developed condo or co-op units subject to a General Business Law Section 352-e Offering Plan that have not yet been sold or transferred by the sponsor.

THE PAT TAX'S 2 PHASES

Because of the apparent desire to collect tax based on the property's fair market value, with co-ops and condos not presently assessed based on value, the PAT Tax will be rolled in over two phases. Phase 1 is from July 1, 2026, through June 30, 2028, and Phase 2 is from July 1, 2028, through June 30, 2031 (or whenever the PAT Law terminates). The PAT Law does not indicate what will happen if DOF has not established a basis for Phase 2 by June 30, 2028.

From July 1, 2026, through June 30, 2028 (Phase 1), the PAT Tax would be based on existing DOF valuations, although current assessments are based on comparable rental property, which is not an assessment that is based on value. Phase 2 presumes that by June 30, 2028, New York City will implement a new comparable sales-based valuation methodology, which the city has not been able to do in the 30 years since New York State Real Property Tax Law Section 467-a, the Co-Op and Condo Abatement, was enacted as a temporary measure. It must be noted that the reason the city has not been able to change the system incorporated in the Real Property Tax Law is because of the difficulty implementing it, which the PAT Law got wrong. It was also the hole in the middle of Mayor Bill de Blasio's Blueprint for Tax Reform.

Phase 1: July 1, 2026-June 30, 2028

- Class 1 (Single-Family/1-3 Family Homes): Market value of $5 million or more
- Class 2 Condominiums and Co-Ops: Market value of $1 million or more

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Phase 2: July 1, 2028-June 30, 2031, or When the PAT Tax Expires

The Phase 1 tax rates for condos and co-ops are significantly higher than the Phase 2 rates because of the different ways of calculating assessed value. It is presumed that the Phase 1 values are 20 percent of market value, but no basis for that assumption is given.

In Phase 2, the PAT Tax applies "phase two market value," a new DOF valuation methodology that is based on comparable sales of condos and co-ops without regard to the statutory discounts under Real Property Tax Law § 581 or Real Property Law § 339-y. In Phase 2, the threshold for the PAT Tax becomes $5 million of market value for all property.

The foregoing is encapsulated in Table 1, which describes the two phases and how each class will be taxed during each phase.

Table 1

	Phase 1	Phase 2
Market Value Method (MV)	**Class 1:** DOF assessed market value (existing method) **Class 2 Condo:** DOF market value (existing method) **Class 2 Co-Op:** Imputed cooperative Phase 1 market value	DOF determines market value using arm's length sales of comparable condos/co-ops, ignoring statutory valuation restrictions (RPTL § 581; RPL § 339-y)
	$5 Million to $15	
Class 1 Single-family homes, 1–3 family residences **Threshold:** MV of $5 million or more	**Million:** Rate of 0.8 percent **$15 Million to $25 Million:** Rate of 1.05 percent **Over $25 Million:** Rate of 1.3 percent	**Same Rates as Phase 1:** But using comparable sales MV
Class 2 Condominiums **Threshold:** Phase 1 MV of $1 million or more	**$1 Million to $3 Million:** Rate of 4 percent **$3 Million to $5 Million:** Rate of 5.25 percent **Over $5 Million:** Rate of 6.5 percent	**Rates Reset to Same as Class 1:** Threshold rises to $5 million (comparable sales MV)
Class 2		**Threshold Rises to $5 Million (Comparable Sales MV)** **$5 Million to $15 Million:** Rate of 0.8 percent **$15 Million to $25 Million:** Rate of 1.05 percent

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	Phase 1	Phase 2
Cooperative Apartments **Threshold:** Imputed Phase 1 MV of $1 million	**Same Rates as Condos (Using Imputed MV):** Tax billed to co-op; board collects from shareholder	**Over $25 Million:** Rate of 1.3 percent PAT Tax billed to co-op; board still collects tax from shareholder

CALCULATION OF IMPUTED COOPERATIVE PHASE 1 MARKET VALUE

Because co-op buildings are assessed as a single-tax lot rather than individual tax lots for each Apartment, there is no market value assigned to each Apartment during Phase 1. As described below, the PAT Law creates the "imputed cooperative phase one market value" in order to allocate a portion of the building's assumed market value to each Apartment.

The Imputed Apartment Value is the Total Building Market Value as determined by DOF, which is allocated based on each shareholder's share of the co-op's shares.

This calculation is incorrect because co-op shares are *never* calculated based on the value of the apartments but rather the size and location of each apartment. If the state's assumption was accurate and the allocation of shares is based on value, then the shares of all the apartments in a building, proportion of maintenance allocated to each apartment would have to change each time an apartment was redecorated or sold. There would be chaos in the industry because of the changes in the percentages. One has to ask how such a simple mistake could have been made.

DETERMINATION OF A PRIMARY RESIDENCE

The next issue to consider is whether the house or apartment is the primary residence of (1) one or more covered owners (or an immediate family member, defined as the owner's spouse, child, sibling, parent, grandparent or grandchild), provided such owners are natural persons, and (2) one or more lessees (or sublessees under a valid sublease pursuant to RPL § 226-b) the right of a tenant to sublease or assign a lease, provided the lessee is a natural person, occupying under a bona fide arm's length lease of at least one year. Pursuant to the PAT Law, DOF is required to make an annual determination, based on information available to it, that a qualifying property is not a primary residence. For the fiscal year starting July 1, 2026, the notice (PAT Notice) must be issued to the owner no later than August 30, 2026. This means that, by the end of the second month that the PAT Law is in effect, DOF has to notify property owners that the property has been accruing a tax for the prior two months. Upon receiving the notice, an owner has the opportunity to submit proof of primary residence. If an owner fails to submit proof of primary residence within the DOF-established deadline, the initial determination becomes final and is not subject to challenge through the standard Tax Commission review process. Not responding eliminates an owner's right to contest non-primary status for that fiscal year. If the owner is traveling, they are just out of luck.

It is important to note that there are an

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estimated 14,000 apartments and homes that could be subject to the PAT Tax, and DOF is somehow going to certify that they are not their owner's primary residences. How would that happen? DOF would need to notify 14,000 New Yorkers that they have to prove they are New York residents. What stops DOF from advising every New York City resident that DOF does not think their home is their primary residence? Is there a good faith or reasonable standard that DOF has to meet or any standard at all? Given these points and others described herein, it is possible that there will be a great deal of litigation. However, the PAT Law precludes anyone going to any court other than the Tax Commission (not a court), as described below, which means that the Legislature has decided to suspend the Due Process rights of at least 14,000 New Yorkers. If DOF thinks it will go after only co-op and condo owners who do not get the Co-op and Condo Tax Abatement (Abatement), that will not work because several years ago the basis for the Abatement changed, and no one in the building could qualify if the Apartment was owned by an entity or the co-op or condo did not pay prevailing wages to the Building-Service employees (i.e., belong to the union), so many co-op and condo owners ceased to qualify for the Abatement. Interestingly, the Abatement requires owners to use the apartment as their primary residence, but Rent Stabilized tenants were not required to prove their qualification.

In its investigation of primary residents, DOF may require the following evidence that the house or apartment is a primary residence:

(1) proof that the owner listed the property as their permanent address on their New York state resident income tax return for the prior calendar year;

(2) evidence that the property received a New York School Tax Relief exemption under RPTL § 425, which has not been given since 2015;

(3) proof that the owner received a NYC Enhanced Real Property Tax Credit under Tax Law § 606(eee); or

(4) evidence that a qualifying lessee or immediate family member occupies the property as their primary residence.

DOF may audit any certification within six years of submission, which, as discussed below, creates serious problems in transferring apartments. In the event that the owner fails to respond to the initial determination by DOF, the PAT Notice becomes a final determination not subject to challenge (except through the Tax Commission review process described below).

THE TREATMENT OF CLASS 1 (1–3 FAMILY HOUSES)

The PAT Law defines "primary residence" to include use by a qualifying lessee under a bona fide arm's length lease of at least one year. However, the PAT Law does not address how multi-unit Class 1 houses are analyzed when different portions of the house have different occupants. The key question the PAT Law leaves open is whether the PAT Tax analysis is applied at the apartment level (such as a co-op) or at the whole building level. A question that needs to be addressed is whether the owner's occupancy as its primary resident exempts the entire house, or is the PAT Tax imposed on the portions of the house that are

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non-primary residences? If the PAT Tax applies, is it to the entire house, or is the tax prorated?

COOPERATIVE BOARDS AND THE PAT LAW

The PAT Law creates a significant and unprecedented administrative and financial burden and risk for cooperative boards and their shareholders, which the boards probably do not have the legal authority to fulfill. These risks include litigation exposure, possible liens against their building, interest, penalties, involvement in enforcement actions over a shareholder's residency and financial consequences and challenges by shareholders as to the board's authority.

DOF will be billing the aggregate PAT Tax for all qualifying non-primary resident apartments to the co-op corporation's statement of account in the same manner as Real Property Taxes because a co-op is only one block and lot. The co-op board is then required to forward it to the affected shareholder "as soon as practicable." This creates a timing risk: DOF's deadline runs from issuance of the Notice, not from the shareholder's receipt. A board may take days to forward a Notice or fails to identify which Apartment is affected, which may forfeit the shareholder's ability to appeal, and its managing agent or treasurer would be responsible for remitting payment of the PAT Tax to the city. The Legislature's assumption is that the co-op would pay the PAT Tax for all of its shareholders and then seek reimbursement from the shareholders.

First, few co-ops have the reserves to pay the City PAT Taxes for its shareholders.

In addition, the co-op has no way of knowing if the shareholder owes the money, and if it just assumes that the money is owed and the co-op is wrong, it likely will be sued.

Third, how does the co-op board have the authority to take corporate funds and pay a tax that may be owned by a single shareholder? Would the Business Judgment Rule protect the board?

The PAT Tax will also become a lien on the cooperative's building. If the co-op board fails to pay DOF, the entire building is at risk of enforcement action by New York City including potential lien sale even if the failure is due to a nonpaying or uncooperative shareholder. Upon receipt of a notice of PAT Tax from DOF, the co-op corporation must provide the notice to the shareholder(s) of the subject unit as soon as practicable. How does the co-op board determine primary vs. non-primary residence status for its shareholder units, which may require requesting information from shareholders. The board has no way to challenge the assessment but will be at risk of being sued by its shareholder if it does nothing or if it acts pursuant to the PAT Law. In the rush to push through an unworkable law, no one thought to include an indemnification for boards. Did the legislators that represent co-op buildings consider these risks? This is what happens when there is no transparency.

The co-op could be liable for the legal and administrative costs of compliance, including litigation with shareholders and enforcement of payment obligations, and review of primary residence certifications will be the responsibility of all shareholders.

(The board does not have the authority to comply under the typical corporate documents. This is the section of the PAT Law about which

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members of the legislature indicated that the author was incorrect.)

The PAT Law does not address how the co-op boards were supposed to do this, which is not a surprise since the legislators did not seem to know or care that the requirement was there. The issue is much more significant than the Legislature considered because the PAT Law requires the co-op corporation to violate Business Corporation Law Section 501 as well as the Internal Revenue By-Laws Code, thereby jeopardizing every shareholder's tax deductions as well as the Basis Adjustment when shares are sold.

As a defensive measure, boards should immediately amend their Proprietary Leases and deal with these issues. Of course, Proprietary Leases require a two-thirds to three-quarters affirmative vote to be amended, which is never easy to achieve.

Another issue not addressed in the PAT Law: What will happen when the co-op's lender declares a mortgage default because of the lien that the city imposes on the building or the bankruptcy risk that arises if paying taxes that the corporation does not owe renders the co-op insolvent? There is no way to identify all the potential risks because nothing like this has ever happened before.

ADDITIONAL RISKS ON THE SALE OF CO-OPS AND CONDOS

There is an additional risk that the attorneys representing boards and purchasers and sellers of co-ops and condos that the legislature ignored: What about DOF's determination that a PAT Tax should have been paid by a former owner after an apartment or unit closes? The PAT Law provides DOF with the authority to impose a lien for years after a closing. DOF can also audit any primary residence certification within six years of submission. The city and state need to collect transfer and mortgage recording taxes at closings, but how can anyone close without an assurance that no tax will be a lien later? Will DOF give estoppel certificates to facilitate closings? Will DOF hire hundreds of new employees to handle all of these issues? Did the authors of the bill run it by the state's attorney general to see if it is even legal?

DOF ENFORCEMENT POWER

The law authorizes DOF to promulgate rules imposing penalties of up to 50 percent of the PAT Tax imposed on the property in the following situations: any certification or documentation submitted to DOF contains inaccurate or misleading information that (1) is material to the determination of whether the PAT Tax applies, and (2) was submitted negligently or in bad faith or a covered condominium property has been divided into more than three units to avoid application of the PAT Tax and such division was made in bad faith. In addition to a lien foreclosure, the New York City Corporation Counsel is authorized to enforce payment, and the DOF Commissioner can issue warrants directed to the city sheriff to levy upon and sell real and personal property. The DOF Commissioner can also subpoena witnesses and compel production of books and records relevant to the PAT Taxes.

NO DUE PROCESS

Shockingly, the property owners have no recourse to the courts. An owner may apply to the New York City Tax Commission, which is not a court,[3] and the review by the Tax Commission is limited to correction of:

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(1) the Phase 1 or Phase 2 market value;

(2) an initial DOF determination that the property is not a primary residence if the owner also challenges the market value); or

(3) a final DOF determination that the property is not a primary residence.

The grounds for review are that the market value is excessive or unlawful or that the property is a primary residence. Because it takes years to get the Tax Commission to rule on Tax Cert Petitions, who will be paying interest on the money the co-op has to borrow to pay the tax? Will New York City owe punitive damages for gross negligence if there was no basis for the determination?

After Tax Commission review, a property owner may seek judicial review under Article 7 of the Real Property Tax Law, which has limited jurisdiction.[4] No other legal proceeding may be brought to challenge PAT Tax liability. Worse, DOF has been granted broad rulemaking authority and most critical operational details are left to DOF rules rather than specified in the statute.

Though the law includes trust and LLC owners as potential "covered owners," the definition requires sole beneficial ownership (trust) or majority interest (entity). What happens in more complex ownership structures where, for instance, there are multiple beneficiaries, tiered entities or minority interests?

To be clear, this is not a tax on second homes. It is a tax on every owner of a home in New York City that is worth a certain amount if the city determines that the owner did not use the home as their primary residence and does not file New York City and New York state tax returns. It is also a tax on retirees living out of New York most of the year who never sold their New York City home that they bought decades ago, which has appreciated in value and they use it part of the year and wanted to leave the family home to their children. The PAT Tax is based on the value of a piece of real estate and not the wealth of the owner. As such, in some instances, it is the most regressive tax that could be charged. This is not "Tax the Rich." It is a tax on someone who owns a valuable asset and could be living on a fixed income and will now be forced to sell that asset to pay the tax.

KEY TAKEAWAYS FROM CITY COMPTROLLER'S REPORT

In preparing this article, the author also reviewed the April 30, 2026, report by the City Comptroller titled "The Pied-à-Terre Tax and Its Potential Revenues" (Comptroller's Report).[5] The Comptroller's Report makes the following points:

- *Revenue Is Uncertain*. The $500 million estimate may fall to an estimated $340 million to $380 million depending on assumptions (p. 2).
- *Behavior Matters*. Revenue is "critically dependent" on renting, selling or occupancy changes (p. 2).
- *Valuation Is Flawed*. Assessed value is a poor proxy for market value (p. 10–11).
- *Results Will Be Inconsistent*. Similar properties may be taxed differently due to valuation gaps (p. 10–11).
- *Co-Op Valuation Is Imprecise*. Unit values must be derived from building-level data (p. 8).

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- *Key Categories Are Unresolved*. LLCs, trusts and multi-unit homes lack clear treatment (p. 18–19).
- *Co-Op Collection Is Questionable*. Feasibility of passing tax through boards "should be carefully evaluated" (p. 19).
- *Administrative Burden Is Significant*. Audits, valuations and enforcement require expanded capacity (p. 20).
- *Appeals Will Increase*. Gaps in administration may drive disputes and litigation (p. 20).
- *Uncertainty Drives Everything*. Outcomes depend on unresolved inputs, not settled analysis (p. 20–21).

Finally, the PAT Tax is not a surcharge because it is not applicable to all the owners as real property taxes are but only to a small subset of owners who are considered by New York City to be primary residents of New York City while they consider themselves to be primary residents of another state or country. This raises a question as to whether New York City and New York state have the right under the U.S. Constitution to tax residents of other states.

IN SUMMARY

- The New York State Legislature recently enacted the 2026–2027 New York State Budget Bill, part of which adds Sections 1350 to 1356 of the New York State Tax Law titled "City Surcharge on Property That Does Not Serve as a Primary Residence."
- The surcharge is described as a "Pied-à-Terre Tax," which applies to any "covered owner" of a "covered property" that does not qualify as a primary residence.
- Owners of primary residences located in New York City are impacted, if they own multiple homes, because only one home can be their primary residence. They will owe the Pat Tax even if they already pay New York City and New York state income tax.

CONCLUSION

New York City's 2026–2027 Budget is $115.9 billion, and New York state's is $269 billion. Assuming that the tax raises $500 million (although the City Comptroller thinks it instead may be closer to $350 million), the PAT Law is undermining the operation and solvency of co-ops, likely reducing the transfer tax and mortgage tax, and will impact sales prices of all housing - all for 0.19 percent of the state budget and 0.43 percent of New York City's budget.

Is the disruption the PAT Tax will cause worth the relatively insignificant revenue it will produce?

NOTES:

[1]According to Google, a surcharge is an additional fee added by a business to recover specific costs, such as credit card processing or fuel. A new tax called a surcharge is a revenue-generating fee levied by the government, often calculated as a percentage of your base tax. Since the PAT Tax is not based on the Real Property Tax, it is a misnomer to refer to it as a surcharge.

[2]The New York State Constitution does not require public hearings before the Legislature enacts legislation. Instead, public hearings are left to the discretion of the legislative leaders and specific committees to which bills are assigned.

[3]The New York City Tax Commission is not a court but rather an independent administrative review agency. Its primary function is to provide an independent forum for property owners to appeal real property tax assess-

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ments set by the New York City DOF or to dispute improper denial of tax exemptions. Though it holds hearings and makes determinations, it is not part of the state Unified Court System. If you are unsatisfied with a determination made by the Tax Commission, you must file a lawsuit in the New York State Supreme Court to pursue further legal recourse.

[4]Article 7 of the New York Property Tax Law is the legal framework property owners used to challenge real property tax assessments. It grants taxpayers the right to seek judicial review if they believe their property is over-assessed or incorrectly classified, provided they first exhausted their administrative remedies for the local board of assessment review.

[5] https://comptroller.nyc.gov/wp-content/uploads/documents/The-Pied-a-Terre-Tax-and-Its-Potential-Revenues-1.pdf.

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What Housing Developers Need to Know About SEQRA Reform in New York

*Christopher B. Fisher and Maximillian Mahalek**

In this article, the authors discuss reforms to New York's State Environmental Quality Review Act that will have practical implications for housing developers in New York State, including greater regulatory certainty and investment potential for qualifying projects.

New York Governor Kathy Hochul recently signed the FY2026–2027 State Budget, which includes "Let Them Build" reforms to the State Environmental Quality Review Act (SEQRA).[1] New York's housing crisis has been exacerbated by development delays that can substantially add time and cost to the entitlement process as compared to other states. These most recent SEQRA amendments, as codified in state law, are a major policy win for the real estate sector and will have practical implications for housing developers in New York State including greater regulatory certainty and investment potential for qualifying projects.

EXEMPTIONS

SEQRA now exempts, without the need for further administrative rulemaking, various housing projects across the State of New York at specified thresholds of density. Outside of New York City, housing developers and local governments can now cite to State law-level SEQRA exemptions where:

(1) the project does not exceed 300 dwelling units in urbanized areas, as defined by the United States Census Bureau or 100 dwelling units in non-urbanized areas (20 dwelling units in municipalities without zoning laws);

(2) the project is connected to an existing community or public water and sewage system at the commencement of habitation;

(3) the project is located at a previously disturbed site;

(4) the project contains no more than 20% commercial, retail, community facility, or other non-industrial non-residential uses by gross floor area; and

(5) the project does not include solely the construction of single-family residences on parcels of 1 or more acres.

New SEQRA exemptions were also codified into State law for construction on previously developed portions of public parks, certain water and wastewater infrastructure projects, and

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retrofitting of existing structures to incorporate green infrastructure.

One of the key considerations to invoking the new SEQRA exemptions for any new qualifying project requires application of the term "previously disturbed" to the land and project in question. That specific term was codified and defined to mean land that:

(1) has been substantially altered by an occupied, formerly occupied, or demolished building, or by another improvement or use at least 2 years prior to the application being filed;

(2) if located outside of an urban area as defined by the United States Census Bureau, abuts, adjoins, or is opposite from another parcel that is or has been occupied or formerly occupied by a building, or demolished building, or another improvement or use at least 2 years prior to the application being filed (if the abutting parcel is not occupied by an industrial or agricultural use);

(3) is not located in a 100-year flood zone as determined by FEMA or a special flood hazard area (unless the relevant municipality has adopted a law requiring new construction to be elevated above the base flood elevation as defined by FEMA);

(4) is not currently being used for agricultural purposes and has not been used for such purposes within the last 2 years (or 3 of the last 5 years) before the application was filed; and

(5) is not located in a designated coastal erosion hazard area.

ELIGIBILITY

To be eligible for a statutory "qualified exemption," the responsible agency has the obligation to determine exemption from SEQRA pursuant to the above criteria and conditions within 120 days. Projects that are qualified as SEQRA-exempt will only be subject to those local zoning and other local and state permitting requirements typical for housing development.

The Governor's legislative package also adopted SEQRA procedural reforms that now establish timelines for any action which is subject to SEQRA's requirements and the potential need for more substantive environmental review. These include:

(1) a 1-year limit on a responsible agency deciding if an environmental impact statement (EIS) is required for actions that are subject to SEQRA;

(2) a 2-year timeline for completion of any EIS, running from the date it was determined an EIS is required (with limited extensions permitted); and

(3) confirmation that the time to bring an Article 78 SEQRA challenge begins "when the agency determination to approve or disapprove the action becomes final and binding upon the petitioner or the person whom the petitioner represents in law or in fact."

While there is no specific enforcement mechanism identified in the legislation, development projects will certainly benefit from more timely SEQRA determinations of significance within 1 year of application filing, and completion of an EIS in less than 2 years from

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the date of a positive declaration issued by a lead agency.

Urban core and suburban areas of New York where multi-family zoning is already in place just received a reverse infusion of SEQRA capital. While there are limitations inherent in any legislative change, including the lack of an administrative default remedy, the Governor's Let Them Build Agenda sets the stage to enable faster permit reviews for qualifying residential projects, cutting red tape, and spurring investment in housing starts throughout New York State.

CONCLUSION

The Let Them Build Agenda is a refreshing and welcomed advancement by the State. Particularly for SEQRA, a statute that was intended to thoughtfully require disclosure and assessment of environmental impacts and not be weaponized against projects, particularly those meeting the most basic needs of the public like diverse housing. As the first major legislative streamlining of SEQRA since its adoption in 1975, only time will tell if these SEQRA reforms produce a "field of dreams" for developers and housing advocates across New York State. Stay tuned.

NOTES:

[1]See New York Senate Bill S9008C Part R (2025–2026 Session).

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U.S. Department of Agriculture Proposes Major Overhaul of Agricultural Foreign Investment Disclosure Act of 1978 Rules

*Marisa N. Bocci, Kari L. Larson and Jeffrey C. Thomson**

In this article, the authors explain how a proposed rule published recently by the U.S. Department of Agriculture could affect a wide range of real estate market participants, including institutional investors in farmland and timberland; commercial and rural-land developers; renewable energy and infrastructure developers; foreign persons and U.S.-organized entities with upstream foreign ownership; and even wholly domestic owners who lease to foreign tenants.

The U.S. Department of Agriculture (USDA) recently published a proposed rule, Docket No. USDA-2026-0001; RIN 0560-AI70, that would significantly reshape the regulatory framework under the Agricultural Foreign Investment Disclosure Act of 1978 (AFIDA). The proposed rule would broaden what counts as "agricultural land," narrow long-standing reporting exemptions, expand beneficial ownership disclosure, increase penalties, and move administration of the program to USDA's Office of Homeland Security. A wide range of market participants could be affected, including institutional investors in farmland and timberland; commercial and rural-land developers; renewable energy and infrastructure developers; foreign persons and U.S.-organized entities with upstream foreign ownership; and even wholly domestic owners who lease to foreign tenants.

The public comment period closed on August 10, 2026, during which the USDA received an exceptionally high volume of comments from affected industries, more so than in response to any previous USDA proposed rules.

WHO COUNTS AS A "FOREIGN PERSON"?

Before turning to the proposed changes, it is worth pausing on a threshold point that is easy to overlook: AFIDA's reporting obligations turn on whether a filer is a "foreign person," and that term is defined far more broadly than many U.S. owners assume. A "foreign person" includes not only foreign individuals, foreign governments, and entities organized outside the United States, but also U.S.-organized entities in which foreign persons hold a "significant interest or substantial

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control." A domestic entity can therefore be treated as a foreign person, and be drawn into AFIDA reporting, based solely on its upstream ownership. The proposed rule makes this more likely by lowering the aggregate-ownership threshold from 50% to 10%, and by counting beneficial owners and any interest held by a foreign adversary. A U.S. fund, partnership, or holding company should not assume AFIDA is inapplicable simply because it is organized domestically; the question turns on who holds direct and indirect interests in the entity. Separately, a wholly domestic landlord whose tenant is a foreign person may find that the tenant carries its own independent reporting obligation.

A NATIONAL SECURITY INITIATIVE

The proposed rule is expressly framed as a national security measure rather than the data-collection exercise AFIDA has historically been. USDA ties the rulemaking to a January 2024 Government Accountability Office report finding that USDA had not shared timely or reliable AFIDA data with the Committee on Foreign Investment in the United States (CFIUS), and to the July 2025 National Farm Security Action Plan, which declares that "farm security is national security" and makes reform of the AFIDA process a top action item. A recurring theme throughout the proposed rule is improving the flow of AFIDA data to CFIUS and applying heightened scrutiny to foreign adversaries. It bears emphasis, however, that AFIDA remains a disclosure statute: it does not authorize USDA to block, condition, or unwind a transaction. National security review of farmland transactions continues to rest with CFIUS, which generally reaches agricultural land only where the land qualifies as "covered real estate" (for example, by proximity to a military installation) or forms part of a covered transaction.

KEY PROPOSED CHANGES

Expanded Definition of "Agricultural Land"

The proposed rule significantly broadens the definition of "agricultural land," replacing the decades-old Standard Industrial Classification codes with current North American Industry Classification System (NAICS) codes and adding: solar and wind energy generation on agricultural land; pipeline transportation corridors; farm product warehousing and processing; conservation land that could be used for farming, ranching, forestry, or timber production; and agricultural research and development activities. The proposed rule would also eliminate the current exemption for tracts of 10 acres or less generating under $1,000 in annual receipts and, for the first time, make easements and rights-of-way for non-agricultural use reportable. Importantly, land meeting the definition would be treated as agricultural land regardless of local zoning classification. Owners of farmland, timberland, conservation land, renewable energy and pipeline interests, and path-of-growth real estate holdings may wish to reassess their portfolios for potential filing obligations.

Lease Exemption Dramatically Narrowed

Currently, leaseholds of less than 10 years are exempt from AFIDA reporting. Under the proposed rule, that exemption would be reduced to leases of less than one year for most foreign persons, and eliminated entirely for entities from or controlled by foreign adversary countries (China, Russia, Iran, North Korea,

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and others designated by the Secretary of State). Short-term agricultural leases, crop production arrangements, and energy site leases that are currently exempt may become reportable.

Enhanced Beneficial Ownership and Structural Disclosure

Foreign persons that are neither individuals nor governments, including funds, partnerships, and corporate entities, would face substantially expanded disclosure requirements. The proposed rule would lower the threshold at which aggregated foreign interests constitute "significant interest or substantial control" from 50% to 10% (USDA has asked for comment on a 5% threshold) and would eliminate the current reporting exemptions for certain shareholders. The proposed rule would require: identification of all persons holding 10% or more of any interest (individually or in aggregate); identification of all "beneficial owners," defined broadly to include anyone exercising decision-making authority over the land regardless of percentage held; ownership diagrams depicting the relationship between all interest holders; tax identification numbers and passport numbers for all foreign persons; and disclosure of shell corporation structures at all intermediary tiers. Filers would also have to submit a digital, open-source geospatial map delineating the land and its uses, together with current acreage. The proposed definition of "shell corporation" is broadly drawn and may capture holding vehicles common in institutional real estate structures.

Stricter Penalties: Restructured and Increased

The proposed rule significantly increases civil penalties and removes the existing provisions allowing downward adjustment of penalties. It would create three separate late-filing penalty schemes (for acquisitions and holdings, for transfers and inheritances, and for newly reportable holdings), each beginning with an initial $250 penalty assessed on the 91st day. Thereafter, penalties accrue on two tracks: entities designated as foreign adversaries or foreign-adversary-controlled entities would accrue 2.5% of fair market value per week, and all other foreign persons 1.5% per week. For portfolios holding multiple parcels, exposure could compound substantially.

Electronic Filing and New Portal

All AFIDA filings would have to be submitted through USDA's new online portal - afida.landmark.usda.gov - which requires a Login.gov account. The paper FSA-153 form would be phased out, and the proposed rule removes form-specific references so that USDA can deploy a new electronic form. Filers who cannot access the portal could seek assistance from their local Farm Service Agency (FSA) office.

Administration Transferred to Office of Homeland Security

Administration of AFIDA is moving out of FSA. A separate final rule issued April 13, 2026 already transferred AFIDA authority from FSA to USDA's Assistant Secretary for Administration, and this proposed rule would codify the sub-delegation of day-to-day administration to USDA's Office of Homeland Security (OHS), a change that reflects the program's more explicit national security orientation. FSA would remain the initial point of contact for filers and would assist with fair market value

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determinations. The proposed rule also overhauls penalty appeals: the response window would shrink from 60 to 30 days; the options to submit a written statement contesting liability or to request a hearing would be eliminated in favor of a single review by the OHS Director; payment would be required electronically through pay.gov; and decisions would be administratively final, with unpaid penalties referred to the U.S. Department of Justice.

INTERACTION WITH STATE LAW

AFIDA operates alongside a growing patchwork of state laws. Roughly two dozen states now restrict foreign ownership of agricultural land or impose their own reporting requirements, and these vary widely in scope, triggers, and penalties. Compliance with AFIDA does not satisfy these separate state obligations. The proposed rule states that conflicting state and local laws would be preempted, while also reminding filers that they must continue to comply with applicable state and local restrictions and that USDA will keep sharing filings with state departments of agriculture. That tension, together with pending constitutional challenges to certain state foreign-ownership statutes, leaves the federal-state landscape unsettled.

WHAT THIS MEANS FOR INVESTORS AND LANDOWNERS

If finalized, the rule would likely require many parties that are currently exempt, or that have never considered themselves subject to AFIDA, to evaluate new disclosure obligations. The proposed rule includes a limited safe harbor period to allow parties time to make compliant filings if deemed necessary. Different categories of market participants could be affected in different ways:

- *Institutional investors in farmland and timberland*: Assess whether holdings fall within the expanded definition of agricultural land and whether fund, joint venture, or trust structures cross the lowered 10% aggregate threshold or trigger the new beneficial-ownership and ownership-diagram disclosures. Also, whether the reduced acreage area and changes to leasehold reporting requirements have expanded prior reporting obligations.

- *Commercial and rural-land developers*: Pre-development or path-of-growth parcels that were farmed or grazed within the prior five years may qualify as agricultural land even if rezoned for another use; this proposed rule clarifies that the filing obligation would apply regardless of local zoning.

- *Renewable energy and infrastructure developers*: Solar, wind, and pipeline interests, as well as easements and rights-of-way, may be reportable, including under site-control leases that were previously exempt.

- *U.S. entities with upstream foreign ownership*: These parties face the most extensive new disclosure, including ownership diagrams, identifiers, and geospatial maps. Where a foreign adversary is involved, they also face the higher penalty track and the loss of lease exemptions.

The proposed rule provides a 90-day window after the final rule's effective date for newly reportable holdings to come into compliance, along with a one-year reduced-penalty transition period. The proposed changes could

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have important implications for foreign investors, agribusinesses, lenders, renewable energy companies, and other organizations with interests in U.S. real estate.

THE COMMENT RECORD AND EMERGING THEMES

USDA received 39 substantive comment letters during the comment period, which closed August 10, 2026. The commenters represented a broad cross-section of affected stakeholders, including energy-sector trade associations representing solar, wind, oil and gas, and pipeline interests; institutional investors and fund-industry organizations; agricultural organizations and farm bureaus; national-security-focused policy institutes; law firms and industry coalitions representing high-volume filers and renewable energy developers; and individual researchers. While no commenter opposed AFIDA modernization itself, the record reflects sharp divisions on the scope and implementation of the proposed changes.

The comments organized around several recurring themes. The most heavily commented issue was the expanded definition of "agricultural land," with energy-sector and pipeline-industry commenters uniformly opposing the inclusion of NAICS codes for solar generation, wind generation, and pipeline transportation, while farm organizations and national-security advocates generally supported the broadening of the definition. The reduction of the aggregate foreign-ownership threshold from 50% to 10% drew near-universal opposition from industry commenters, who argued it is impractical for publicly traded companies and would sweep in passive pension-fund investors from allied nations. The penalty overhaul, which would increase accrual rates from 0.1% to 1.5% of fair market value per week (2.5% for foreign adversaries), eliminate downward adjustments, and reduce the appeal period from 60 to 30 days, was the second-most-commented issue, with virtually every industry commenter urging retention of penalty mitigation for good-faith, non-adversary filers. Additional themes included the narrowing of the lease exemption from 10 years to one year and elimination of the easement and right-of-way exemption; implementation concerns regarding geospatial mapping requirements and the readiness of USDA's electronic filing portal; widespread criticism of the proposed 90-day transition period for newly reportable holdings as operationally infeasible; and calls to distinguish between allied-nation investors and foreign adversaries across all provisions of the rule, not merely in the penalty and lease-exemption contexts.

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Saudi Arabia Issues Implementing Regulations for White Land Fees and Vacant Properties Fees: What Property Owners and Investors Need to Know

*Malek Al Rifai, Nabil A. Issa, Alexander Barker and Abdulrahman Albilal**

In this article, the authors discuss the key provisions of new Saudi Arabia regulations addressing undeveloped land and vacant buildings and their practical implications.

Saudi Arabia's regulatory framework governing idle real estate has entered a new phase. Following the enactment of the White Land and Vacant Properties Fees Law (the Amended Law) by Royal Decree No. (M/244) in May 2025, the Ministry of Municipal, Rural Affairs and Housing (the Ministry) has issued two sets of implementing regulations addressing undeveloped land and vacant buildings.

The Implementing Regulations for White Land Fees (the White Land Regulations) were issued on 28 Safar 1447 AH (22 August 2025), establishing detailed rules for the imposition of fees on undeveloped land. The Implementing Regulations for Vacant Properties Fees (the Vacant Properties Regulations) were approved on 26 Dhul Qi'dah 1447 AH (13 May 2026) and published in the Official Gazette (Umm Al-Qura). The White Land Regulations are now substantially complete. The Vacant Properties Regulations have been formally issued, but their practical operation remains contingent on a series of supplementary ministerial decisions, including decisions on application zones, thresholds, and penalties.

Taken together, the two regulations indicate a clear policy direction: to discourage the underutilization of undeveloped land and completed buildings in urban areas. For developers, landowners and institutional investors, the main immediate implication is the need to assess exposure, update compliance processes and monitor the supplementary decisions required to make the vacant properties regime operational.

This article examines the key provisions of each regulation and their practical implications.

WHITE LAND FEES

The White Land Regulations were issued on 28 Safar 1447 AH (22 August 2025) by the Minister of Municipal, Rural Affairs and Housing, implementing the provisions of the

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Amended Law as they relate to undeveloped land. Under the White Land Regulations, the person liable for the fee is the "Obligor," defined as the natural or legal person (excluding State-owned properties) in whose name the land ownership document is registered at the time of issuance of the fee invoice, including any successor in title by operation of Sharia or law.

The determination of whether land falls within the urban boundary and its designated use is made exclusively by reference to urban boundary demarcation maps and detailed plans issued by the competent authorities. Informal assessments of land classification have no regulatory standing.

TIERED FEE RATES OF UP TO 10% PER ANNUM

White land is classified into five tiers based on the priority of urban development within a given city. The annual fee rate ranges from 2.5% for the lowest priority tier to 10% for the highest priority tier, calculated on the assessed value of the land. Land falling within the fifth tier (outside the priority zones) is not subject to an annual fee; however, it is still counted toward the total white land holdings of the Obligor within the city boundary. This counting rule matters because fifth-tier land may still contribute to the aggregate area calculation relevant to fee-bearing parcels in the same city.

The Ministry may also, following its annual review, suspend the application of the fee in a city or geographical scope, in addition to its power to amend the area subject to the fee. Both outcomes are possible following the annual review of supply, transaction volumes, prices and monopolistic practices.

The land value used as the fee base is adjusted by a coefficient reflecting the availability of public services and utilities connected to the land. This coefficient is determined per service or utility based on its necessity and its impact on land value, and is applied uniformly within each city. The Ministry may periodically revise the coefficient weightings in line with urban development priorities.

DEVELOPMENT OR CONSTRUCTION SUSPENDS THE FEE AND ENABLES REFUNDS

The fee ceases to apply once the land has been developed or built upon within the statutory payment period. For these purposes, "construction" means the complete erection of structures on the land (excluding fencing) in accordance with building permits, and "development" means the complete implementation of infrastructure in accordance with approved permits and regulatory requirements. Partial completion does not extinguish the fee on the undeveloped remainder.

The fee also ceases where an impediment prevents the Obligor from disposing of the land, or where an obstacle prevents the issuance of the necessary licences and approvals for development or construction, during the statutory payment period, provided in each case that the Obligor has not caused or contributed to the creation of such impediment or obstacle.

An Obligor who completes development or construction after having already paid the fee is entitled to a refund of the amounts paid for those periods. The technical committee also has discretion to grant additional time to complete development, taking into account the size and nature of the land. This gives some

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operational flexibility for larger projects with longer delivery timelines.

FEE ASSESSMENT AND THE TECHNICAL COMMITTEE

Land values for the purpose of calculating the fee, and the periods required for development or construction, are determined by a technical committee formed within the Ministry by Ministerial decision. The committee must comprise no fewer than three members with expertise in real estate valuation and land development procedures, including licensed valuers accredited by the Saudi Authority for Accredited Valuers (SAAV). Decisions are made by majority vote. Committee members serve three-year terms, renewable or extendable. The rules, procedures and valuation standards applied by the committee must conform to SAAV-approved standards.

MINIMUM THRESHOLD OF 5,000 SQUARE METRES

The fee applies only where the aggregate area of white land owned by the same Obligor reaches at least 5,000 square metres. Article 7 of the White Land Regulations states that this condition is assessed "within the scope of the city." Two further conditions must also be satisfied: the land must be physically capable of development or construction, and its designated use must be one of the uses specified in the relevant Ministerial Decision for the applicable city. Land that fails either criterion is not subject to the fee even if the area threshold is met.

The White Land Regulations do not expressly state whether the calculation of total area is performed separately for each city. The phrase "within the scope of the city" may be read as a spatial condition defining where the land must be located, rather than as a rule requiring separate calculation per city. Equally, the broader structure of the regulations, which treats each city by separate announcement and specific geographic zones, may support a city-by-city reading. This should therefore be treated as an interpretive issue rather than a settled point, and stakeholders should monitor further guidance or clarification from the Ministry.

The regulations also contain anti-evasion provisions that empower the Ministry to verify ownership data and investigate whether title has been distributed among related parties, including family members, nominees or affiliated entities, in a manner designed to keep individual holdings below the 5,000 square metre threshold. The Ministry may coordinate with relevant authorities, including real estate, corporate and civil status registries, to verify the accuracy of ownership records and assess whether a pattern of fragmentation exists.

Where the Ministry identifies such a pattern, it may attribute the holdings to the same beneficial owner and apply the fee accordingly. For family offices, multi-entity groups and asset managers holding white land across several vehicles, existing ownership structures should be reviewed to assess whether ostensibly separate holdings could be aggregated and whether that aggregation could trigger fee exposure across the portfolio.

FEE INVOICES, NOTIFICATION AND OBJECTION RIGHTS

The Ministry issues fee invoices on specified dates for each parcel subject to the fee. Each invoice must contain at minimum the Obligor's name and statutory information, the

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ownership document number, the land location, the legal basis for the fee, the fee rate and amount, the payment deadline, the means of payment, the consequences of non-payment and the Obligor's right to object, including the applicable objection period.

Notifications are legally effective if served through any of the following channels: the Ministry's electronic portal, the Obligor's authenticated mobile number, the Obligor's authenticated email address, or the Obligor's national address as registered with the National Information Centre or approved electronic systems. Obligors should ensure their contact data across these channels is current, because valid service through any one channel starts compliance periods running.

The Minister also has power to unify the dates for issuance of annual fee invoices for each city. Where invoice dates are unified, payment periods and development periods may be adjusted accordingly. Investors should therefore monitor city-specific invoice date decisions, as they directly affect compliance timelines.

SALE BEFORE COMPLETION OF DEVELOPMENT TRIGGERS IMMEDIATE PAYMENT

If an Obligor wishes to sell white land before completing its development, the payment deadline is immediately accelerated, and all accrued fees must be settled in full before the transfer of ownership can be completed. Investors should therefore factor accrued fees into the cost and timing of any exit, particularly where the land may have been subject to the fee for several years.

New owners of white land whose acquisition occurs after the initial registration grace period must submit ownership documents and land data to the Ministry within 30 days of transfer of ownership.

RETROACTIVE ASSESSMENT OF FEES

The Ministry has authority to assess fees retrospectively from the date on which the land first became subject to an application decision in the relevant city. Where a fee invoice is issued for prior years, it takes effect from the date of issuance, and payment is due within 90 days of notification. The collection of retroactive fees does not preclude the imposition of penalties for failure to pay or to submit required documentation, which can materially increase exposure for owners who delay registration or compliance.

PENALTIES

The Ministry is required to establish a schedule of violations and penalties, to be issued by Ministerial decision following approval by the Ministerial Committee. Until that schedule is published, the specific quantum of penalties for non-compliance remains uncertain. Fees and penalties are collected in accordance with the procedures specified in the State Revenues Law and its executive regulations. The Ministry may engage the private sector for collection purposes.

VACANT PROPERTIES FEES

The Vacant Properties Regulations, issued by Ministerial Resolution No. (4700822503/1) dated 26/11/1447 AH, establish the framework for imposing fees on developed but unoccupied buildings. They apply pursuant to Article 13 of the Amended Law and set out the

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structure for identifying vacancy, calculating fees and enforcing compliance. Their practical operation, however, remains dependent on further ministerial decisions.

SCOPE OF APPLICATION AND MINIMUM OWNERSHIP THRESHOLD

The fee does not apply to every vacant property. It is triggered only where the number of vacant properties owned by a single person within a designated application zone meets a minimum threshold, to be determined by the Minister according to the type of use. Both the designation of application zones and the minimum vacancy thresholds are the subject of separate supplementary ministerial decisions yet to be issued. Until those decisions are issued, the regime has no operative effect in any city.

The regulations appear designed to permit city-specific implementation, given the structure used under the White Land Regulations and the need for separate designation of application zones and thresholds. Pending those decisions, investors with larger portfolios are more likely to be affected once the regime becomes operative, while smaller owners may remain outside scope unless their vacant holdings exceed the prescribed threshold.

FEE CAP AND FINANCIAL IMPACT

The fee is calculated as a percentage of the equivalent rental value of the property. This rental-value-based fee is subject to a maximum cap of 5% of the property's market value per annum. The 5% of market value operates as a ceiling rather than the primary base, so in markets where rental yields are modest relative to capital values the effective fee may be lower than the cap. Both the equivalent rental value and the market value are determined by a specialised technical committee comprising no fewer than three members, including valuers licensed by the Saudi Authority for Accredited Valuers.

CRITERIA FOR DETERMINING VACANCY

The Vacant Properties Regulations employ a multi-criteria system for determining whether a building is vacant. The fee regime applies only to buildings that are fit for occupancy or that hold a valid occupancy certificate. Within that scope, a building is classified as vacant where either of the following criteria is satisfied:

- Temporal criterion: the building has not been utilised for a continuous or cumulative period of six months during the reference year.
- Consumption criterion: the building fails to meet the minimum consumption thresholds for utilities and services allocated to its type of use, such as electricity and water.

Each criterion operates independently: satisfaction of either criterion is sufficient to classify a building as vacant. "Occupancy" is defined as the absence of all vacancy criteria in respect of a building. The precise consumption thresholds have not yet been issued and are to be determined by a subsequent ministerial decision, subject to the approval of the Ministerial Committee.

EFFECT OF SALE ON THE FEE AND THE QUESTION OF LIABILITY

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ported by an official deed suspends the application of the fee on the relevant property. However, the Vacant Properties Regulations link the payment obligation to the Obligor, being the registered owner, rather than to the property itself, which obliges the Obligor to settle the fee, including in proportion to its share in the case of co-ownership. The Ministry also retains authority to assess fees retrospectively from the date on which the property became subject to an application decision, together with any applicable penalties.

The Vacant Properties Regulations do not expressly address whether accrued fees constitute an encumbrance that attaches to the property and transfers to the buyer, or whether they remain a personal obligation of the former owner. Given the general requirement under Saudi property law for rights in rem to be registered to bind third parties, and absent any express provision designating fee liabilities as registrable encumbrances, one possible interpretation is that unregistered fee liabilities remain personal to the former owner. That issue should, however, be treated as unresolved. Investors acquiring properties within designated application zones should therefore carry out due diligence on potential accrued fees and include express contractual provisions allocating liability for any outstanding amounts. Lenders taking security over such properties should similarly seek appropriate representations from borrowers.

DISCLOSURE OBLIGATIONS AND PENALTIES

The Obligor is required to disclose the status of its buildings at least once during the reference year and to submit the requisite documentation. New owners are similarly required to submit documentation upon the transfer of ownership. The Ministry may request additional documents, carry out field inspections to verify occupancy status, and coordinate with relevant authorities to validate the accuracy of the data provided. The collection of fees for prior years does not preclude the imposition of penalties arising from failure to pay or to submit required documentation, meaning that delays in compliance may compound the financial burden.

The penalty schedule for the Vacant Properties Regulations has not yet been issued and will require a separate Ministerial decision following Ministerial Committee approval. Until issued, the specific quantum of penalties for non-disclosure or non-payment under this regime remains uncertain.

CURRENT STATUS OF IMPLEMENTATION

Although the Vacant Properties Regulations have been approved and published, their effective application depends on a series of supplementary ministerial decisions. Those decisions are expected to address, among other things, the precise consumption thresholds, the technical criteria for geographic application zones, the list of recognised impediments that suspend the fee, the designation of cities and zones subject to the regime, the minimum number of vacant properties that triggers liability, and the violations and penalties schedule.

At this stage, the immediate risk is therefore preparatory rather than fully operative. Investors should review the status of potentially affected vacant properties, map likely exposure scenarios and monitor the supplementary de-

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cisions required before enforcement can begin in any designated city.

PRACTICAL IMPLICATIONS

The combined effect of the White Land Regulations and the Vacant Properties Regulations is to extend regulatory pressure across the real estate life cycle, from undeveloped land to completed buildings. The practical implications for owners, developers and investors include the following:

1. The cost of holding idle assets may increase materially. White land may be subject to fees of up to 10% annually, while vacant properties may ultimately be subject to a fee capped at 5% of market value; however, the vacant properties regime remains dependent on supplementary decisions before it becomes operative in any city.

2. Retroactive exposure requires careful due diligence. Both sets of regulations permit retrospective fee assessment from the date a property first became subject to an application decision, so prospective buyers should verify whether any accrued fee liabilities may exist before completing an acquisition.

3. Disclosure and documentation obligations are ongoing. Obligors must disclose the status of their holdings and provide supporting documentation, and noncompliance may lead to further penalties once the relevant schedules are issued.

4. Several issues remain interpretive. These include the aggregation methodology for white land holdings and the treatment of accrued fee liability on a sale of vacant property. Those issues should be monitored closely because they may affect structuring, diligence and drafting positions.

5. Ownership structures merit review. The anti-evasion provisions permit the Ministry to investigate fragmentation of title among related parties, creating possible aggregation risk across family, nominee or affiliated holdings.

6. Sale documentation should address fee allocation expressly. That is particularly important for vacant properties, where the regulations do not yet resolve all questions relating to the allocation of accrued liability as between buyer and seller.

7. Notification compliance is important. Fee invoices and notices served through the prescribed channels are legally effective and may trigger compliance periods even if internal contact information is out of date.

8. Developers retain some flexibility under the White Land Regulations. Refunds may be available on completion, and additional time may be granted for larger projects in appropriate cases.

CONCLUSION

The White Land Regulations are now substantially operational, subject to the usual need for ongoing city-specific application decisions and enforcement practice. By contrast, although the Vacant Properties Regulations have been issued and published, they do not yet create a fully operative fee regime in any city until the required supplementary ministerial decisions are made.

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The immediate focus for investors should therefore be on implementation risk, not only on headline fee levels. Property owners, developers and investors with holdings in Saudi Arabia should audit portfolios, assess where exposure may arise under existing and future application decisions, and put in place processes to monitor further ministerial action, maintain current notification details, and address fee allocation and diligence issues in transaction documents.

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Forward Purchasing Hotels in Europe: Managing Risk in a Rebounding Market

*Martin Smith and Samuel Cramer**

In this article, the authors review some of the key commercial considerations that investors should consider when entering into forward purchase hotel transactions in Europe.

Capital is flowing back into the European hotel sector at pace. Across the UK and Europe, transaction volumes rose sharply in 2024 (as we await full 2025 data), reaching levels not seen since before the pandemic. Investor appetite has returned, driven by resilient trading performance, record room rates, and availability of more favourable debt terms.

Alongside this resurgence, there is an increased use of forward purchase and forward funding structures for hotels still under development. For investors, these structures offer early access to high-quality stock in supply-constrained markets. For developers, they provide certainty for capital recycling and reduced risk.

This article reviews some of the key commercial considerations that investors should consider when entering into forward purchase hotel transactions in Europe.

"HOTEL OPENING": A CRITICAL COMPLETION TRIGGER

For most hotel forward purchase agreements, completion is conditional upon the hotel "opening" (as opposed to practical completion of the development, as would be the case in many other asset classes). While this sounds straightforward, in practice it is not and can be heavily negotiated.

For an investor, completion should occur only once the hotel is genuinely operational — not merely physically complete. The hotel must be capable of trading in line with underwriting assumptions, with systems, staff, and the operator fully mobilised and all aspects of the hotel trading. Aligning completion of the purchase with conditions under the hotel management agreement (HMA) ensures that the operator is contractually required to open and operate the hotel at agreed minimum standards. This reduces the risk of acquiring a hotel that is technically open but commercially underprepared, which could impact income. If there will be any delay to opening any food and beverage offerings or other key guest facilities, such as spas and gyms, these should be factored in so that the investor acquires the fully operational hotel.

However, developers face a different risk

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profile. If "hotel opening" is defined too tightly, particularly where brands impose detailed brand standards, even relatively minor operational issues could delay the hotel's opening, postponing the release of capital or, worse, pushing the transaction beyond the agreed long stop date.

The commercial balance typically therefore turns on the balance between:

- *Room availability*: public can book and pay for all or a significant majority of rooms; and
- *Soft opening*: limited guest operations to test systems and staff readiness; or
- *Full launch*: fully operational hotel meeting all brand standards and trading criteria and a certain period of time thereafter to address snagging.

Developers must avoid conditions that create unnecessary completion risk, while investors only want to hand over payment for a fully functioning hotel. Achieving clarity at the drafting stage avoids any disputes as to what determines completion and who pays for any unforeseen bills.

OPERATIONAL COMPLEXITY: ACQUIRING A BUSINESS, NOT JUST REAL ESTATE

Hotels differ from most other real estate assets in one fundamental respect: They are an operating business and the most complex of the operational real estate classes.

Upon completion of the purchase, the buyer inherits not only a building but a complex operating business that may include commitments to capital funding obligations, employees and staffing structures, management, service and supplier contracts, brand standard, and franchise obligations.

This transfer is more straightforward on a share acquisition as generally, all the benefits and liabilities of the operating business transfer immediately and seamlessly. Share transfers are therefore more common than asset deals where the need to separately transfer benefits and liabilities can cause additional complication and timing issues. The parties require individual agreements governing the assignment and novation of various business assets and obligations, including employees, intellectual property, customer contracts, and licences. The developer may need consent for these processes from other parties, and this can create a delay and create many hurdles to completion. This can jeopardise the long stop date.

Buyers frequently seek consent rights over material pre-completion actions taken by the developer. From an investor perspective, this is understandable — operational commitments entered into ahead of completion can materially affect value and future operations. However, excessive oversight can impede the developer's ability to achieve defined hotel opening efficiently. Overly restrictive investor consent mechanisms risk delay and friction, which are not in either party's interest; aligning with owner consent rights under any hotel management agreement can be an effective compromise.

Alignment of interests between the developer, investor, and operator is essential, and there should be clearly defined materiality thresholds for buyer consents, regular reporting, and inspection meetings so the buyer is fully informed.

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CONSTRUCTION RISK: DEVELOPMENT EXPOSURE DOES NOT DISAPPEAR

A forward-funded structure inherently involves development risk for both parties, although investors look to minimise it. All the usual development risks in achieving practical completion of the construction are combined with the additional steps in achieving hotel opening. If both practical completion and hotel opening are not achieved by the agreed deadline, then the investor will typically have the ability to walk away from the transaction, which is not a palatable end result for either party. With that in mind, the parties may negotiate step-in rights for the investor if the long stop date is at risk, but this can lead to additional worries. If the investor steps in, it may be exposed to increased and unforeseen costs, or it may wish to make changes to the specifications which will affect the investor's original underwriting. The developer will also be hesitant to pay for any costs after the investor has stepped in, given it is no longer in control of the development.

Importantly, while hotels generally open shortly after practical completion of the construction work, ongoing snagging issues, incomplete finishes, or defects are not simply legal and construction matters; they directly impact the guest experience in the crucial opening and stabilisation phase of the hotel.

Such issues need to be handled carefully, and key risk questions include:

- Who bears the cost of unresolved construction disputes at practical completion, and who solves them?
- How long is the gap between hotel opening and completion to allow the developer time to handle sensitive snagging issues while the hotel is occupied, and what obligations are placed on the developer to diligently carry this out?
- Will the investor (or its operating partner) be able to confidently step into the relationship with the hotel operator to manage the snagging items?

These questions may become more pertinent depending on what triggers "hotel opening" as aforementioned.

CONTRACTOR INSOLVENCY AND DEFECTS PROTECTION

The insolvency of a main contractor late in the development cycle is one of the most significant risks in a forward purchase transaction. It affects timing, funding, and certainty of delivery.

A replacement contractor is unlikely to assume liability for defects in the original contractor's work, which likely includes all of the design, unless commercially incentivised by way of a large, off-market fee increase. Developers will typically seek a clean exit at completion and do not want to give longstanding indemnities to cover warranty gaps. Buyers, on the other hand, will be reluctant to inherit a structure with gaps in warranty/defects protection and, even if willing to take that risk, may struggle to persuade its lender to do so. The developer may therefore be called upon to stand behind defects, with any cap amount and duration being key points for negotiation. The benefit of the guarantee will be impacted by the creditworthiness of the guarantor and the ability of the investor to offer protection to its lender or a future purchaser.

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Construction law frameworks vary significantly, and investors should avoid assuming that protections common in one jurisdiction will automatically apply elsewhere. In the UK, contractors typically remain liable during a 12-month defects rectification period, with latent defects potentially covered for up to 12 years depending on contract structure. In other jurisdictions, the structure may rely more heavily on insurance-backed guarantees rather than ongoing contractor liability (or both) and may offer more of a clean break for the developer even if the contractor does become insolvent.

These structural differences materially affect how risk is assessed, priced, and negotiated. Cross-border transactions should ensure local counsel is engaged for the construction elements as well as the other local legal issues.

CONCLUSION: STRUCTURING FOR CERTAINTY IN A RECOVERING MARKET

Forward purchase hotel transactions are an increasingly important feature of the European investment landscape. They provide developers with capital efficiency and investors with early access to prime hospitality product, but they come with risks that sit at the intersection of construction delivery, contractor covenant strength, jurisdiction-specific legal frameworks, and hotel opening.

As the European hotel market continues to strengthen, well-structured forward purchase arrangements will remain popular, but many commercial issues need to be carefully balanced for the agreements to sufficiently benefit and protect all parties.

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Court of Justice of the European Union Rules That Portuguese Real Estate Transfer Tax on Restructurings Violates EU Law - Signal Effect for Germany

*Florian Schiefer and Merlyn von Hugo**

In this article, the authors review a decision by the Court of Justice of the European Union holding that the Portuguese real estate transfer tax on restructurings violates EU law.

By judgment of June 4, 2026, in case C-837/24 "Nova Iberomoldes," the Court of Justice of the European Union (CJEU) held that the Portuguese real estate transfer tax on restructurings infringes the Capital Duty Directive (Directive 2008/7/EC). The question was whether real estate transfer tax may be levied where the capital of a newly established company is raised by way of an in-kind contribution of shares in companies holding real estate. According to the CJEU, the real estate transfer tax constitutes an indirect tax, the levying of which infringes the Capital Duty Directive in such a constellation.

The judgment is likely to be transferable to German real estate transfer tax, for the following reasons:

- In Germany, too, the transfer/consolidation of at least 90% of the shares in companies holding real estate is subject to real estate transfer tax.
- Where shares in companies holding real estate are transferred in the context of restructurings (including mergers, spin-offs, and contributions), an exemption from tax is available under § 6a GrEStG (German Real Estate Transfer Tax Act). However, the granting of this exemption applies only to certain measures and is subject to meeting shareholding thresholds (95%) as well as strict pre- and post-holding periods (five years each).
- The principles of the "Nova Iberomoldes" judgment should be transferable to German real estate transfer tax. For share transfers in the course of restructurings, the levying of real estate transfer tax could constitute an infringement of EU law contrary to the Capital Duty Directive.

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In that case, compliance with the requirements for the exemption under § 6a GrEStG would no longer be relevant.

FACTS: ESTABLISHMENT OF A HOLDING COMPANY IN RETURN FOR A CONTRIBUTION OF INTERESTS IN REAL ESTATE COMPANIES

The judgment was based on a group restructuring carried out in 2019. Nova Iberomoldes was incorporated as a Portuguese company limited by shares. Its entire share capital was raised by contributions in kind made by the sole shareholder. The contributions consisted exclusively of interests in other companies, some of which held real estate located in Portugal.

The Portuguese tax administration treated the transaction as subject to the municipal real estate transfer tax (Imposto Municipal sobre a Transmissão Onerosa de Imóveis; IMT). Under the IMT legislation, not only direct transfers of real estate are taxable, but also the acquisition of shares in certain companies holding real estate, if this causes a shareholder to reach at least a 75% shareholding threshold. As the tax administration considered these requirements to be fulfilled, it imposed IMT by way of an additional assessment.

The Portuguese tax arbitration court referred to the CJEU the question whether the levying of real estate transfer tax in such a constellation infringes the Capital Duty Directive.

CAPITAL DUTY DIRECTIVE AND CLASSIFICATION AS A RESTRUCTURING

The CJEU explains that indirect taxes on the raising of capital and taxes on restructurings are to be largely abolished by the Capital Duty Directive. The aim is to avoid discrimination, double taxation, and obstacles to the free movement of capital. The Directive fully harmonizes this area and allows taxation only in exceptional cases.

Article 3 lit. a also covers the incorporation of a company as a capital contribution. Article 4 para. 1 lists certain restructurings in addition, including, in lit. b, the acquisition of a majority of the voting rights in another company limited by shares in return for the granting of shares in the acquiring company at least in part.

Accordingly, the incorporation of Nova Iberomoldes in principle falls under Article 3 lit. a, but at the same time fulfils Article 4 para 1 lit. b: The newly established company acquires majority shareholdings in other companies limited by shares, while the contributing sole shareholder receives shares in the acquiring company in return. The CJEU therefore classifies the transaction as a restructuring and not as a mere capital contribution.

Article 5 para. 1 lit. a and lit. e prohibit Member States from levying indirect taxes on capital contributions and restructurings. A transaction such as the case at issue is therefore in principle exempt from tax, unless an exception under Article 6 applies.

IMT AS A PROHIBITED INDIRECT TAX ON A RESTRUCTURING

According to the CJEU, the IMT qualifies as an indirect tax on a restructuring, on which Member States may not levy any indirect taxes pursuant to Article 5 para. 1 lit. e. The fact that the tax base is determined by reference to a reference value of the real estate concerned

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does not change this. The triggering event is not an isolated transfer of real estate, but the corporate contribution in kind of shares.

The CJEU emphasises that Article 6, as an exception to the prohibition of taxation under Article 5, must be interpreted strictly. Thus, the exception in Article 6 para. 1 lit. a does not apply, as it was not an isolated securities trade that was taxed, but the establishment of a holding company with contributions in kind. Nor do the exceptions in Article 6 para. 1 lit. b and lit. c, for transfer taxes, apply. According to the relevant case law, transfer taxes require a transfer of ownership in real estate, which is not present in the case of the contribution of shares in a company holding real estate. In the view of the CJEU, the strict interpretation of Article 6 also precludes the economic approach, based on a fictitious transfer of real estate, put forward by the German government.

The CJEU therefore concludes that the Capital Duty Directive precludes a national provision under which a tax such as the Portuguese IMT is levied on a transaction that qualifies as a restructuring within the meaning of Article 4 para. 1 lit. b. For such transactions, Member States may not levy any indirect taxes pursuant to Article 5 para. 1 lit. e.

RELEVANCE TO GERMAN REAL ESTATE TRANSFER TAX

The decision is of particular interest for German real estate transfer tax law because the Portuguese IMT regime shows clear parallels to the German share deal provisions. Pursuant to § 1 Abs. 2a, 2b, 3, and 3a GrEStG, transactions are also subject to real estate transfer tax in which no real property is directly transferred, but rather shares in a company owning real property are transferred or consolidated to an extent that confers significant influence (90%). In practical terms, economic changes of ownership in real estate are thus captured via share transfers.

Where shares in companies holding real estate are transferred in the context of restructurings (including, inter alia, mergers, spin-offs, and contributions), there is the possibility of a tax exemption under § 6a GrEStG. However, this tax exemption is subject to strict conditions. In addition to the existence of a privileged measure, shareholding thresholds (95%) as well as pre- and post-holding periods (five years each) must be fulfilled. In practice, the tax exemption therefore often does not apply (for example, in the case of the contribution of shares in a company holding real estate into a newly established holding company), because the pre-holding period is not fulfilled.

In its judgment of 25 September 2024 (II R 36/21), the German Federal Fiscal Court (BFH) had still taken the view that § 1 para. 3 GrEStG does not infringe the Capital Duty Directive and had not considered a reference to the CJEU to be necessary. The BFH classified the real estate transfer tax triggered by the transfer of shares as a permissible transfer tax within the meaning of Art. 6 para. 1 lit. b.

In light of the "Nova Iberomoldes" judgment, this view is likely to be obsolete. On the one hand, the CJEU interprets the scope of application of the Directive broadly by classifying the establishment of a holding company with a contribution of shares in real estate companies as a restructuring within the meaning of Art. 4 para. 1 lit. b and subjecting it to the comprehensive prohibition on levying taxes in Art. 5 para. 1 lit. e. At the same time, it narrows the

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scope of the exceptions to the prohibitions on levying taxes in Art. 6 para. 1 lit. b by emphasizing that a transfer tax presupposes an actual transfer of ownership in real property and cannot be extended to mere share transfers by way of legal fictions or an economic approach. These principles should also be applicable to restructuring transactions that trigger taxation under § 1 para. 2a, 2b, 3, and 3a GrEStG.

At present, another case on the compatibility of the real estate transfer tax share deal provisions with the Capital Duty Directive is pending before the BFH under case number II R 8/23. It remains to be seen whether the BFH will revise its previous view or refer the question of the compatibility of the German real estate transfer tax rules with the Capital Duty Directive to the CJEU for a preliminary ruling. Pending cases should be kept open with reference to the judgment in "Nova Iberomoldes" as well as the pending BFH proceedings. For assessed real estate transfer tax, it should be examined whether a legal remedy is available.

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One Year After *Seven County*: Trends in NEPA Review and Litigation Risk

*Tommy P. Beaudreau, H. David Gold, Caroline McHugh, Barak Kamelgard and Ethan McKenzie**

In this article, the authors analyze court decisions in the year following the U.S. Supreme Court's opinion in *Seven County Infrastructure Coalition v. Eagle County*, finding that agencies are prevailing in the vast majority of post-*Seven County* cases, but that litigation risk remains where challengers can identify concrete regulatory or record-based deficiencies.

A little more than one year ago, on May 29, 2025, the U.S. Supreme Court issued its unanimous decision in *Seven County Infrastructure Coalition v. Eagle County*, which established a "course correction" to bring agency compliance and judicial review under the National Environmental Policy Act (NEPA) back in line with the statutory text.[1] The Court aimed to rein in practices by agencies and lower courts that over time had expanded the NEPA process beyond its statutory basis and to clarify that courts must afford substantial deference to agency decision-making in implementing this procedural statute.[2]

Federal courts have since applied *Seven County* consistently across a broad range of NEPA disputes. Based on a review of dozens of district and circuit court decisions applying *Seven County*, this article provides a one-year retrospective, highlighting key trends and practical takeaways for entities navigating NEPA review. The emerging case law reflects a strong and consistent trend demonstrating that lower courts are embracing the Supreme Court's directive to defer to agency judgments across nearly every dimension of the NEPA process.

At the same time, a handful of cases signal that there are limits to the deference that agencies enjoy post-*Seven County*. Agencies continue to face litigation risk as a court may find that they failed to satisfy specific regulatory requirements or reasonably explain their approach in the administrative record.

BACKGROUND

Seven County reoriented NEPA review by both narrowing the scope of analysis required under NEPA and requiring greater judicial deference to agency determinations in implement-

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ing NEPA. Specifically, the Supreme Court held that courts must afford "substantial deference" to agency judgments in NEPA analysis and decline to "micromanage" fact-dependent decisions so long as they fall within a "broad zone of reasonableness."[3] The Court emphasized that NEPA is "a procedural cross-check, not a substantive roadblock," and that the ultimate question is whether the agency's decision was "reasonable and reasonably explained," not whether the analysis was perfect.[4]

Further, the Court clarified the scope of NEPA analysis in two ways. First, NEPA requires agencies to focus on the effects of the "proposed action" (i.e., the "project at hand"), not separate projects that are geographically or temporally distinct, even if those projects are foreseeable.[5] *Seven County* makes clear that agencies must have broad latitude to draw a "manageable line" between such projects.[6] Second, agencies are not required to analyze the environmental impacts of projects over which they have no authority.[7] The decision did not specifically address how agencies should treat cumulative effects of a proposed action and acknowledged that agencies will need to make judgments in close cases where it is not clear whether one project is separate from another, leaving agencies and lower courts to confront these issues case by case in the highly deferential landscape.[8]

ONE YEAR LATER: HOW LOWER COURTS ARE APPLYING *SEVEN COUNTY*

An analysis of 44[9] post-*Seven County* district and circuit court decisions that substantively applied *Seven County* identifies several trends and issues to watch.

Trends

1. *Deference permeates all aspects of NEPA review*. Courts repeatedly cite *Seven County's* admonition that deference is the "bedrock" of judicial review of NEPA claims, and they consistently broadly defer to agencies on methodological choices,[10] range-of-alternatives determinations,[11] sufficiency of detail[12] and scope-of-analysis determinations.[13] Taken together, these decisions confirm that *Seven County* operates as a cross-cutting constraint on judicial second-guessing of agency determinations regarding the scope of reviews under NEPA. Agencies prevailed in over 80% of the cases we examined, with losses largely confined to narrow, case-specific issues. Generally, if an agency's analytical choices fall within a "broad zone of reasonableness," the agency's review will be found to have satisfied NEPA. For agencies and project proponents, these cases suggest a favorable environment for defending NEPA documents.

2. *Agencies have wide latitude to draw a "manageable line" when defining the scope of NEPA analysis*. Prior to *Seven County*, a limited set of cases used the "manageable line" concept to exclude from NEPA review only those activities outside an agency's jurisdiction.[14] Under *Seven County*, courts are now especially deferential to agency decisions to exclude impacts from actions that fall outside the reviewing agency's jurisdiction.[15] Moreover, post-*Seven County* cases extend the "manageable line" concept to other NEPA scope determinations[16] and

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consistently uphold agency decisions to exclude geographically or temporally distinct projects and future, contingent actions from the scope of analysis, even if their effects are foreseeable.[17] Courts have not necessarily required agencies to explain the lines drawn on what to exclude—in some cases, courts have simply inferred the lines and then deferred to agencies' apparent choices.[18] Nonetheless, despite agencies' broad discretion, project sponsors should work with agencies early to define the proposed action description and scope of analysis, and ensure that the written record reflects a clear rationale for excluding activities as separate in time, place or regulatory authority.

3. *Cumulative impacts remain a potential vulnerability (for now)*. Courts generally defer to agency assessments of cumulative impacts.[19] Nevertheless, agencies may fall short if they exclude obviously adjacent projects or skip the analysis altogether.[20] That said, new NEPA procedures have omitted express requirements to conduct cumulative impact analysis. As time passes, therefore, courts will apply those new procedures, and litigation risk related to cumulative impact analysis likely will decline. For now, the key takeaway is that cumulative impacts remain a potential vulnerability, especially for decisions made under prior procedures, but future risk will depend on how courts interpret and apply the new, more flexible NEPA procedures.

4. *There are bounds on the "broad zone of reasonableness."* Even after *Seven County*, agencies cannot gloss over regulatory requirements or basic administrative law principles.[21] For example, the District of Washington vacated a Forest Service NEPA analysis because project maps and a "condition-based management" plan were too vague to comply with NEPA's requirement to ensure a "hard look" at impacts and enable the public to provide meaningful comment.[22] In another case, the District of Alaska held that the Forest Service violated NEPA by defining the project's purpose and need so narrowly—by baking in projected growth assumptions—that it effectively predetermined the outcome and foreclosed consideration of reasonable alternatives.[23] These post-*Seven County* agency losses generally suggest that project proponents and agencies should remain attentive to the fundamental tenets of NEPA review and ensure the analysis is reasonable and explained in the record.

5. *Even when courts find that agencies have fallen short, they have gravitated toward remand without vacatur*. *Seven County* underscored that a NEPA deficiency does not necessarily require vacating an agency decision. The central question is whether the agency had sufficient information to make an informed decision.[24] Post-*Seven County*, courts have elected to remand deficient NEPA analyses without vacating the agency decision in cases where the NEPA error was discrete and not structural and where vacatur would have severe on-the-ground consequences.[25] For project sponsors, this trend provides some reassurance that NEPA deficiencies are less

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likely to unravel approvals of projects, particularly where the administrative record demonstrates a substantively informed decision and the equities weigh against project disruption. That said, advancing projects to key milestones (e.g., receiving a Notice to Proceed and initiating construction) can strengthen arguments against vacatur, and project sponsors should ensure that the underlying substantive approvals are well-supported in the record. In a post-*Seven County* landscape where plaintiffs may shift focus to non-NEPA claims, as discussed below, a defensible record across all governing statutes is increasingly critical both on the merits and in avoiding remedies that lead to extremely costly and disruptive delays.

Issues to Watch

1. *Application of Seven County deference beyond NEPA*. Some courts have begun applying *Seven County*'s principles of agency discretion and deference in regulatory matters across other statutes. For example, the Western District of North Carolina deferred to the definition of the "action area" delineated in a Biological Opinion considering effects to protected wildlife and plant species under Section 7 of the Endangered Species Act (ESA), finding that it fell within the "broad zone of reasonableness."[26] The Ninth Circuit similarly invoked *Seven County* to grant heightened deference to the National Marine Fisheries Service's critical habitat designations under the ESA.[27] To date, courts have not explicitly applied *Seven County* principles to reviews of historic properties under Section 106 of the National Historic Preservation Act (NHPA), but the procedural similarities between Section 106 and NEPA suggest that there are arguments supporting increased deference in those areas as well.

2. *Shifting plaintiff focus to other statutes*. Given the increased difficulty of prevailing on NEPA claims, plaintiffs will likely shift their focus to other statutes, including the ESA, the NHPA, and substantive authorizing and land management statutes. Ensuring that the record demonstrates compliance with these other statutes and supports a substantive decision will be critical for the long-term durability of federal approvals.

3. *Interpretation of new NEPA procedures*. The court decisions since *Seven County* generally relate to agency actions developed under prior NEPA frameworks, including the now-removed Council on Environmental Quality regulations.[28] As courts begin reviewing agency actions under the current frameworks—which generally afford agencies greater discretion and impose fewer prescriptive analytical requirements (including, in many cases, eliminating a stand-alone cumulative effects analysis)—we expect the basis for further judicial deference on outstanding issues such as cumulative effects to be stronger, a point on which agencies have lost even post-*Seven County*.[29]

IN SUMMARY

- Courts are consistently applying *Seven*

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County to afford substantial deference to federal agencies across all aspects of NEPA review—including methodology, alternatives, and scope—so long as decisions fall within a "broad zone of reasonableness."

- Legal challenges seeking to require analysis of upstream or downstream effects or separate projects have largely failed, with courts finding that agencies have broad latitude to draw a "manageable line" around the project at issue.
- Agencies are prevailing in the vast majority of post-*Seven County* cases, but litigation risk remains where challengers can identify concrete regulatory or record-based deficiencies.
- Courts are increasingly willing to remand without vacatur for limited NEPA defects, reducing the risk that discrete issues will unravel approvals for entire projects.
- Litigation risk may shift away from NEPA and toward other environmental statutes, such as the Endangered Species Act and the National Historic Preservation Act.

CONCLUSION

One year after *Seven County*, the emerging case law confirms that the decision has meaningfully reshaped the NEPA landscape in ways that favor agencies and project proponents. Courts are consistently applying a highly deferential standard of review, giving agencies broad latitude to define the scope of analysis and to make methodological judgments, while limiting successful challenges to narrow, record-specific deficiencies. At the same time, *Seven County* has not eliminated litigation risk: Agencies—and applicants working with them—must continue to ensure that NEPA analyses and the agencies' subsequent substantive decisions are grounded in the governing regulations and procedures, clearly explained in the administrative record and coordinated with compliance under all applicable environmental statutes. While project proponents will likely experience greater certainty afforded by *Seven County*, continued evolution in the case law is anticipated in the coming months.

NOTES:

[1]Seven County Infrastructure Coalition v. Eagle County, Colorado, 605 U.S. 168, 145 S. Ct. 1497, 221 L. Ed. 2d 820 (2025).

[2]605 U.S. at 184.

[3]605 U.S. at 169, 192.

[4]605 U.S. at 173, 185.

[5]605 U.S. at 190.

[6]The "manageable line" concept was emphasized in Seven County but originated in pre-Seven County case law. See Metropolitan Edison Co. v. People Against Nuclear Energy, 460 U.S. 766, 774 n.7, 103 S. Ct. 1556, 75 L. Ed. 2d 534, 18 Env't. Rep. Cas. (BNA) 1985, 52 Pub. Util. Rep. 4th (PUR) 189, 13 Envtl. L. Rep. 20515 (1983); Department of Transp. v. Public Citizen, 541 U.S. 752, 767, 124 S. Ct. 2204, 159 L. Ed. 2d 60, 58 Env't. Rep. Cas. (BNA) 1545, 26 Int'l Trade Rep. (BNA) 1097, 34 Envtl. L. Rep. 20033 (2004).

[7]605 U.S. at 188.

[8]605 U.S. at 190 ("[t]here may be a gray area" but "a court should defer to an agency so long as the agency drew a reasonable and 'manageable line' " (quoting Pub. Citizen, 541 U.S. at 767)).

[9]As of June 5, 2026.

[10]See, e.g., Standing Trees, Inc. v. United States Forest Service, 2025 DNH 99, 2025 WL 2411206, *11 (D.N.H. 2025) (finding agency's decision to rely on state water quality data rather than producing baseline water quality data fell "within a broad zone of reasonableness" (quoting Seven Cnty., 605 U.S. at 183)).

[11]See, e.g., Center for Biological Diversity v. United States Bureau of Land Management, 141 F.4th 976, 998 (9th Cir. 2025) (finding agency's use of a full field development standard to select alternatives fell within a "broad zone of reasonableness" (quoting Seven Cnty., 605 U.S. at 183)).

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[12]See, e.g., Gas Transmission Northwest, L.L.C. v. Federal Energy Regulatory Commission, 157 F.4th 674, 713 (5th Cir. 2025) (holding that agency determinations regarding EIS depth and breadth must merely "fall within a broad zone of reasonableness" (quoting Seven Cnty., 605 U.S. at 183)).

[13]See, e.g., Alliance for the Wild Rockies v. Matt Anderson, 2026 WL 892326, *7 (D. Mont. 2026) (extending "substantial deference" to agency's determinations of how to limit its NEPA analysis (quoting Seven Cnty., 605 U.S. at 183)).

[14]See New Jersey Dept. of Environmental Protection v. U.S. Nuclear Regulatory Com'n, 561 F.3d 132, 139 (3d Cir. 2009) (noting that in cases citing to the test, "this [manageable] line appears to approximate the limits of an agency's area of control.").

[15]See, e.g., Sierra Club v. Federal Energy Regulatory Commission, 153 F.4th 1295, 1308 (D.C. Cir. 2025) (holding that an agency could no longer be compelled to "speculate about the effects of a separate project that is outside its regulatory jurisdiction" (quoting Seven Cnty., 605 U.S. at 189)); Lopez v. United States, 2025 WL 2380475, *22 (D. Ariz. 2025) (finding that the Forest Service was not required to consider alternative mining techniques for operations that may occur on private lands that the Forest Service lacks authority to regulate).

[16]See, e.g., National Council of Negro Women v. Duffy, 2026 WL 754991, *14 (S.D. Miss. 2026) (upholding a "manageable line" that "exclud[ed] the effects of speculative projects that are separate in time and place."); Alliance for the Wild Rockies v. Matt Anderson, 2026 WL 892326 (D. Mont. 2026) (holding that the US Forest Service "drew a 'manageable line' in determining how much depth of analysis to afford and how much detail to include" with regards to cumulative effects (quoting Seven Cnty., 605 U.S. at 191)).

[17]See, e.g., American Wild Horse Campaign v. Raby, 144 F.4th 1178, 1192 (10th Cir. 2025) (holding that the agency has no obligation to analyze even foreseeable effects of future actions when they arise from separate projects).

[18]See, e.g., Alliance for the Wild Rockies, Native Ecosystems Council, Council on Wildlife and Fish, and Yellowstone To Uintas Connection v. Mulholland, 2026 WL 892385, *22 (D. Mont. 2026) (upholding agency's "apparent" scoping decisions where agency decisions "show[ed] evidence of a faint but 'manageable' line"); Alliance for the Wild Rockies v. U.S. Forest Service, 2025 WL 2655984, *10 (E.D. Wash. 2025) (upholding an "apparent" line drawn to exclude other projects as separate based on general references that did not contain details of any specific projects excluded).

[19]See, e.g., Chattooga Conservancy v. United States Department of Agriculture, 2026 WL 865760, *10 (D.D.C. 2026) (deferring to agency's cumulative impact analysis because agencies are "better equipped to assess what facts are relevant to the agency's own decision than a court is" (quoting Seven Cnty., 605 U.S. at 181)); Alliance for the Wild Rockies v. Matt Anderson, 2026 WL 892326, *8 (D. Mont. 2026) (holding that the US Forest Service "drew a 'manageable line' in determining how much depth of analysis to afford and how much detail to include" with regards to cumulative effects (quoting Seven Cnty., 605 U.S. at 191)).

[20]See, e.g., Alliance for the Wild Rockies, Native Ecosystems Council, Council on Wildlife and Fish, and Yellowstone To Uintas Connection v. Mulholland, 2026 WL 892385, *19–21 (D. Mont. 2026) (holding that the Forest Service improperly omitted from its cumulative effects analysis a reasonably foreseeable project adjacent in time and space to the proposed action); Alliance for Wild Rockies v. James, 2026 WL 686492 (D. Mont. 2026) (finding that plaintiffs were likely to succeed on claim that the Bureau of Land Management's actions were arbitrary and capricious based on the failure to conduct and publish a cumulative impacts analysis on spring grazing's effect on sage grouse).

[21]See, e.g., Alliance for the Wild Rockies, Native Ecosystems Council, Council on Wildlife and Fish, and Yellowstone To Uintas Connection v. Mulholland, 2026 WL 892385, *21 (D. Mont. 2026) ("[D]eference to the agency cannot overcome the plain language of the relevant NEPA regulation."); Ctr. for Biological Diversity, 141 F.4th at 999 (holding that longstanding administrative law precedents requiring agencies to acknowledge and explain changes in agency position still applied, despite the heightened deference conferred by Seven County).

[22]Alliance for the Wild Rockies v. U.S. Forest Service, 2025 WL 2655984, *12 (E.D. Wash. 2025).

[23]Miller v. U.S. Forest Service, 2025 WL 2802244, *8 (D. Alaska 2025).

[24]Seven Cnty., 605 U.S. at 185.

[25]Orutsararmuit Native Council v. United States Army Corps of Engineers, 2025 WL 1654878, *7 (D. Alaska 2025); Ctr. for Biological Diversity, 141 F.4th at 1015–16 (citing Idaho Farm Bureau Federation v. Babbitt, 58 F.3d 1392, 1405, 41 Env't. Rep. Cas. (BNA) 1207, 32 Fed. R. Serv. 3d 774, 25 Envtl. L. Rep. 21265 (9th Cir. 1995)).

[26]Defenders of Wildlife v. U.S. Forest Service, 2026 WL 914620, *6 (W.D. N.C. 2026) (finding that, although "not a model of clarity or thoroughness," the Biological Opinion's definition of the action area falls within the "broad zone of reasonableness" (citing Seven Cnty., 605 U.S. at 182–83)).

[27]Alaska v. National Marine Fisheries Service, 171 F.4th 1145, 1156–57 (9th Cir. 2026) ("But 'when an agency exercises discretion granted by a statute,' we ask only 'whether the agency action was reasonable and reasonably explained.' " (quoting Seven Cnty., 605 U.S. at 179–80)).

[28]Removal of National Environmental Policy Act Implementing Regulations, 91 Fed. Reg 618 (Jan. 8, 2026) (codified at 40 C.F.R. pts. 1500 to 1508).

[29]See supra note 21.

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U.S. Department of Housing and Urban Development Pulls the Plug on Emotional Support Animal Guidance: 5 Steps for Education Housing Administrators

*Joshua D. Nadreau and Shiloh Theberge**

In this article, the authors discuss the decision by the U.S. Department of Housing and Urban Development permanently rescinding prior guidance on emotional support animals in housing, effectively ending nearly two decades of federal protection for those who rely on emotional support animals.

Federal housing officials have formally stripped emotional support animals (ESAs) of their protected status in housing, a sweeping policy change that will directly affect how college and university housing offices process accommodation requests from students with disabilities. The U.S. Department of Housing and Urban Development has issued an enforcement memo permanently rescinding prior guidance on ESAs in housing, effectively ending nearly two decades of federal protection for those who rely on ESAs. The memo eliminates the presumption that landlords and housing providers must accommodate untrained ESAs, replaces it with the much stricter ADA standard for trained service animals, and takes effect immediately. This article explains what happened, what it means for college and university housing, and what campus housing operators should do now.

WHAT HUD DID

Fair Housing and Equal Opportunity (FHEO) Assistant Secretary Craig Trainor signed the memo on May 22,[1] effective immediately. It permanently cancels both of HUD's prior guidance documents on assistance animals in housing: one issued in 2013, FHEO-2013-01, and the updated version from 2020, FHEO-2020-01. Together, those documents told housing providers they had to treat ESAs as assistance animals rather than pets, could not charge pet fees, and could only request limited documentation.

Going forward, FHEO will find reasonable cause for failure to provide a reasonable ac-

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commodation involving the waiver of a pet policy only where the animal has been individually trained to perform work or tasks directly related to the complainant's disability. That is the ADA's definition of a service animal, which is a much higher bar than an untrained ESA has historically needed to clear.

HUD said it was making this change because the 2020 guidance failed to provide greater clarity on the supposed distinction between pets and emotional support animals, which had caused problems at the agency. Over 20% of FHEO's fair housing complaints had come to revolve around untrained ESAs, a caseload HUD characterized as unsustainable.

WHAT HASN'T CHANGED

Higher education administrators should tread carefully before changing any policies, as several critical elements of the law have not changed.

- First, the Fair Housing Act itself has not been amended. This memo withdraws prior HUD guidance, but it does not by itself rewrite the Fair Housing Act or state laws. It simply alters how HUD will treat complaints and guidance going forward.
- Second, the memo is explicitly limited to animal accommodation complaints under the Fair Housing Act. Complaints filed under Section 504 of the Rehabilitation Act and the ADA are not affected. State laws and complaints filed under state laws are also not affected. For campus housing offices, this is particularly significant. Campus housing at public universities is subject to Section 504, and many states have their own fair housing laws that go beyond federal protections. Your obligations under those frameworks remain unchanged.
- Third, nothing in the enforcement guidance affects the rights of parties to seek redress through a private action in court. Students whose ESA requests are denied can still sue, and private litigation does not require a prior HUD finding. The removal of HUD enforcement does not eliminate legal exposure for housing providers who deny legitimate accommodation requests.

WHAT CAMPUS HOUSING OPERATIONS SHOULD DO

Here are five practical steps that higher education housing administrators can take in light of this memo:

1. *Maintain vigilance with ESA requests*

   Do not treat this memo as a green light to categorically deny ESA requests. As noted above, the Fair Housing Act remains the law. Automatically denying all ESA requests is still off limits, and disability discrimination is still illegal. Any student with a genuine disability and a legitimate need for an animal is still entitled to an individualized interactive process, regardless of whether the animal is trained.

2. *Train your staff on what "trained" actually means under the new standard*

   There is no requirement that training be done by a professional organization or certified trainer. Owner training can be sufficient under the new policy, as it is under the ADA. A student claiming their

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dog is individually trained to interrupt a panic attack or perform a specific psychiatric task may well meet the standard even without formal credentials. Your reviewers need to understand this distinction to avoid denying requests that are actually valid under the new framework.

3. *Make sure you understand the documentation process*

   Now that HUD's 2020 guidance is rescinded, you have more flexibility on what documentation you can and cannot request. Requiring documentation from a licensed healthcare provider who has an actual treatment relationship with the student (not an online letter mill) is now a defensible standard. You can also feel more confident rejecting obvious fraud, including online certificates and generic letters from providers with no therapeutic relationship.

4. *Review existing approved accommodations*

   If a student's ESA has already been approved as a reasonable accommodation, that approval stands. Your institution would have to take affirmative steps to revoke it, which could raise its own legal issues. The bigger concern is new requests, transfers to different campus housing, or students returning next year who need to renew an accommodation.

5. *Watch your state law*

   Many states (like California, New York, Illinois, and others) have their own fair housing statutes that independently protect ESAs. Those laws are unaffected by this memo. If your institution operates in a state with stronger protections, the federal rollback provides no cover.

WHAT'S NEXT?

HUD has indicated it intends to engage in notice and comment rulemaking regarding animal-related reasonable accommodations, with the aim of harmonizing its regulations with those of the ADA. That process will take time and will likely produce a clearer and more restrictive permanent standard. You will want to monitor the situation closely, as it will eventually replace the current guidance vacuum.

NOTES:

[1] https://dredf.org/wp-content/uploads/2026/05/ESA-Enforcement-Memorandum-w-Appendix-05.22.2026-SIGNED-Incomplete-Access-Pass.pdf.

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