Opportunity Zones
Background

• Passed as part of Tax Cuts and Jobs Act (2017)

• First round of proposed regulations – October 2018

• Second round of proposed regulations – April 2019

• Hearing on second round of proposed guidance – July 9

• No consensus on next steps by Treasury
Taxpayers can get capital gains tax deferral (& more)

Qualified Opportunity Funds (QOFs)

for making timely investments in

which invest in

Qualified Opportunity Zone Property
THE ZONES

• Selections made! Will not change without legislative action.

• Over 74,000 census tracts in US
  • About 8,700 are Opportunity Zones
  • Demonstrates disparity and also breadth of opportunities for investment

• 120 OZs in the state of Wisconsin
Online Mapping Tools for Confirming OZs

- www.cdfifund.gov/Pages/mapping-system.aspx
- www.eig.org
THE INVESTOR BENEFIT
Partial Forgiveness and Forgiveness of Additional Gains

- **SALE INVESTMENT**
  - **HELD FOR 5 YEARS**
    - Basis increased by 10% of the deferred gain
    - Up to 90% taxed
  - **HELD FOR 7 YEARS**
    - Basis increased by 5% of the deferred gain
    - Up to 85% taxed
  - **HELD FOR 10 YEARS**
    - Basis is equal to Fair Market Value
    - Forgiveness of gains on appreciation of investment
    - Requires an election

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THE FUND

• Statutory definition of Qualified Opportunity Funds:
  • An investment vehicle organized as a corporation or a partnership for the purpose of investing in Qualified Opportunity Zone Property (QOZP)
• Opportunity Funds self certify
• Noncompliance Penalty
  • 90% asset test
  • Ignore contributions within past 6 months
  • Per month penalty equal to % of shortfall x underpayment rate
  • No penalty for reasonable cause
TYPES OF QOF INVESTMENTS

Qualified Opportunity Zone Property (QOZP)

Qualified Opportunity Zone Partnership Interest (Qualified Opportunity Zone Business)

Qualified Opportunity Zone Business Property

Qualified Opportunity Zone Stock (Qualified Opportunity Zone Business)
5 QOZB Tests

- Organized as a partnership or corporation for tax purposes
- 70% of tangible assets are QOZ Business Property
  - Acquired after 12/31/17
  - Used in an Opportunity Zone
  - Original Use or Substantial Improvement
- 50% of active gross income from OZ
- <5% NQFP
- Ineligible businesses
Readily Identifiable Investment Types in Opportunity Zones

- Commercial Real Estate Development and Renovation in Opportunity Zones
- Opening New Businesses in Opportunity Zones
- Expansion of Existing Businesses into Opportunity Zones
- Large Expansions of Businesses already within Opportunity Zones
Updates from April Guidance

For Investors and QOF Managers

- Six-month safe harbor for new cash contributed to a QOF.
- Rolling investment strategy by QOF permitted if funds are invested in another OZ project within 12 months.
- Interim gains are recognized by QOF investors.
- Carried interests not eligible for OZ benefits.
- No depreciation recapture.
- Strategy for exit from multi-asset funds.
Updates from April Guidance

For Real Estate Development

- Leased property can be qualified property
  - Tenant improvements qualify as original use
  - Leases must be market rate
  - Certain requirements if a lease is with an affiliate
- Property vacant for 5 years or more qualifies for original use
- Substantial improvement on an asset by asset basis rather than an aggregate basis
- In some cases, time requirements can be extended for government delay
- Mere triple net leases are not “active conduct”
Updates from April Guidance

For Business

• Four different ways for a QOZB to satisfy the 50% income test. The methods are based on either hours of employees and independent contractors, amounts paid for these services, tangible property and management functions, or a facts and circumstances analysis.

• 31-month working capital safe harbor applies to the development of a trade or business, in addition to the acquisition, construction, and improvement of tangible property.
What about Reporting?

- Currently there are no reporting requirements other than an asset test every 180 days.
- The service has indicated that reporting requirements may be issued.
- Groups are pushing Treasury to track:
  - job creation
  - poverty reduction,
  - changes in availability of affordable housing in OZs,
  - the extent to which investors consult with local residents in developing their projects,
  - data on how many people from disadvantaged groups are hired,
  - the number of minority owned businesses benefitted
Who is raising capital and how much?

- The Erie Downtown Development Corporation (EDDC) - Fund size: $250 million
  - Downtown revitalization group in Erie, PA. Wants to restore the downtown Erie community by stabilizing rent, create an appealing infrastructure, and improving the competitive retail market.

- SoLa Impact Fund - Fund size: $100 million
  - Renovations to create appealing affordable housing; businesses such as those growing food in vertical warehouses are looking to relocate to these struggling locations.

- LISC - Fund size: Varies
Who is raising capital and how much?

- Harvest Returns, Fort Worth, TX
  - Focused on supporting farmers by investing in sustainable agricultural businesses in Opportunity Zones.

- Catalyst- Fund size: $150 million
  - Impact fund focused on market rate returns and social good. Non-coastal focus.

- Bridge Investment Group – over $500 Million raised
  - National fund with markets to include Sacramento, Salt Lake City and Queens.
What is the Federal Government Doing?

- **Environmental Protection Agency (EPA):** directing funds to communities, 72% of which are Ozs

- **Federal Housing Administration (FHA):** reducing application fees paid by property owners for certain multifamily mortgage insurance programs

- **Department of Housing and Urban Development (HUD):** requesting information from the public on how to maximize the beneficial impact of public and private investments in Ozs
Federal Government – Continued

- **HUD and Treasury Department:** In talks for allowing Puerto Rico to put federal aid into OZs

- **SEC** recently released a summary of the ways in which securities laws are implicated in the OZ program

- **HUD and U.S. Census Bureau:** Issued an OZ challenge program to engage the private sector to create technology that facilitates investments in OZs

- **Whitehouse Opportunity Zone and Revitalization Council:** published an implementation plan on reforms and initiatives to optimize federal resources in OZs
What are States doing?

- **West Virginia:** looking at creating income tax exemption for OZ investments
- **Florida:** trying to align OZs with preexisting enterprise zones to give benefits of both programs to investors
- **Connecticut:** want to exempt historic preservation requirements for OZ buildings vacant longer than 5 years
- **Maryland:** tax credits for OZ businesses that hire former inmates and historic preservation tax credits to businesses
State Government - Continued

- **Missouri**: proposing an increased cap for state historic credits for projects in OZs

- **California**: introducing a bill to exempt projects in OZs from the CA Environmental Quality Act

- **Ohio**: proposing a 10 percent nonrefundable state tax credit for investments of at least $25,000 in an OZ

- **Maryland**: tax credits for OZ businesses that hire former inmates and historic preservation tax credits to businesses
What are local governments doing?

• Educating themselves and their constituents about the incentive
• Examining their pipeline of projects
• Creating prospectuses
• Examining city-owned properties
• Hosting stakeholder meetings
• Layering incentives
• Easing entitlement process
• Considering fund formation
The Missing Middle

- Middle of the County
- Mid to small size projects
- Connection between projects and OZ investors
- Connections between ED and local government bodies who want to create a fund and fund managers who can manage them