



# CDFA Texas Webinar: The Latest on Opportunity Zones

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The broadcast will begin at 10:00 AM (Central)

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# CDFA Texas Webinar: The Latest on Opportunity Zones

## Now Speaking



### **Tim Fisher**

Manager, Government Affairs  
Council of Development Finance Agencies  
Columbus, OH

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*See all of CDFA's resources on Opportunity Zones online at [www.cdfa.net](http://www.cdfa.net)*



# CDFA Texas Webinar: The Latest on Opportunity Zones

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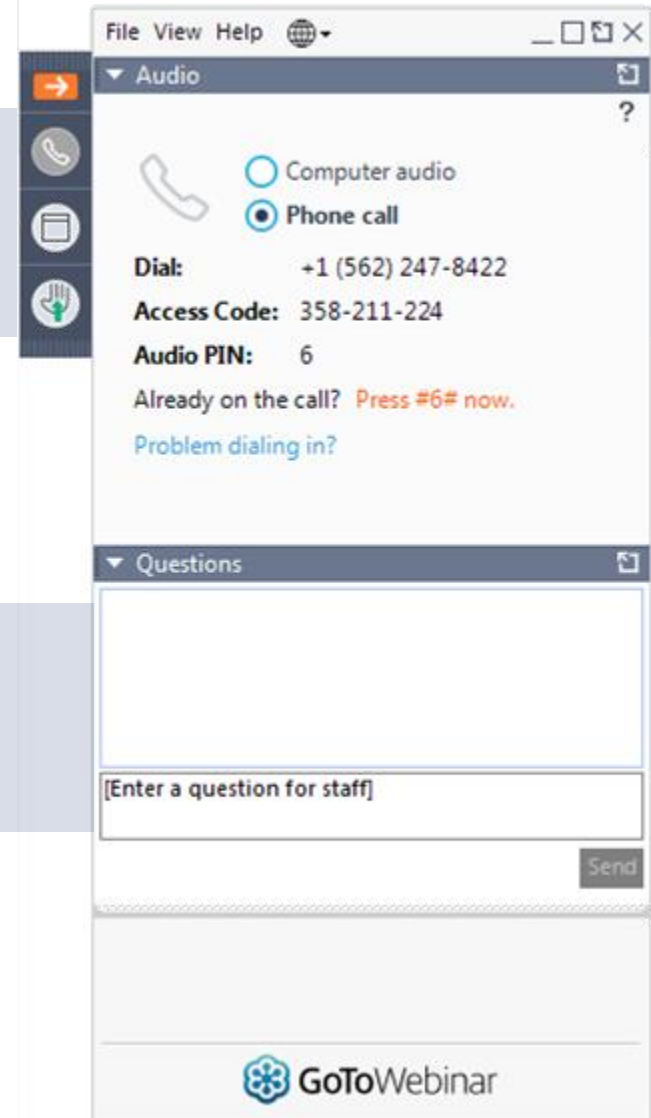
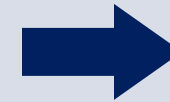
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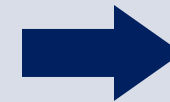


# CDFA Texas Webinar: The Latest on Opportunity Zones

Using your telephone will give you better audio quality.



Submit your questions to the panelists here.





# CDFA Texas Webinar: The Latest on Opportunity Zones

## Panelists

### **Byron Sarhangian**

Partner  
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Phoenix, AZ

### **Michael Perrine**

Managing Director  
Baker Tilly Capital, LLC.  
Austin, TX

### **Robin Bentley**

Assistant Director, Economic Development  
City of Dallas  
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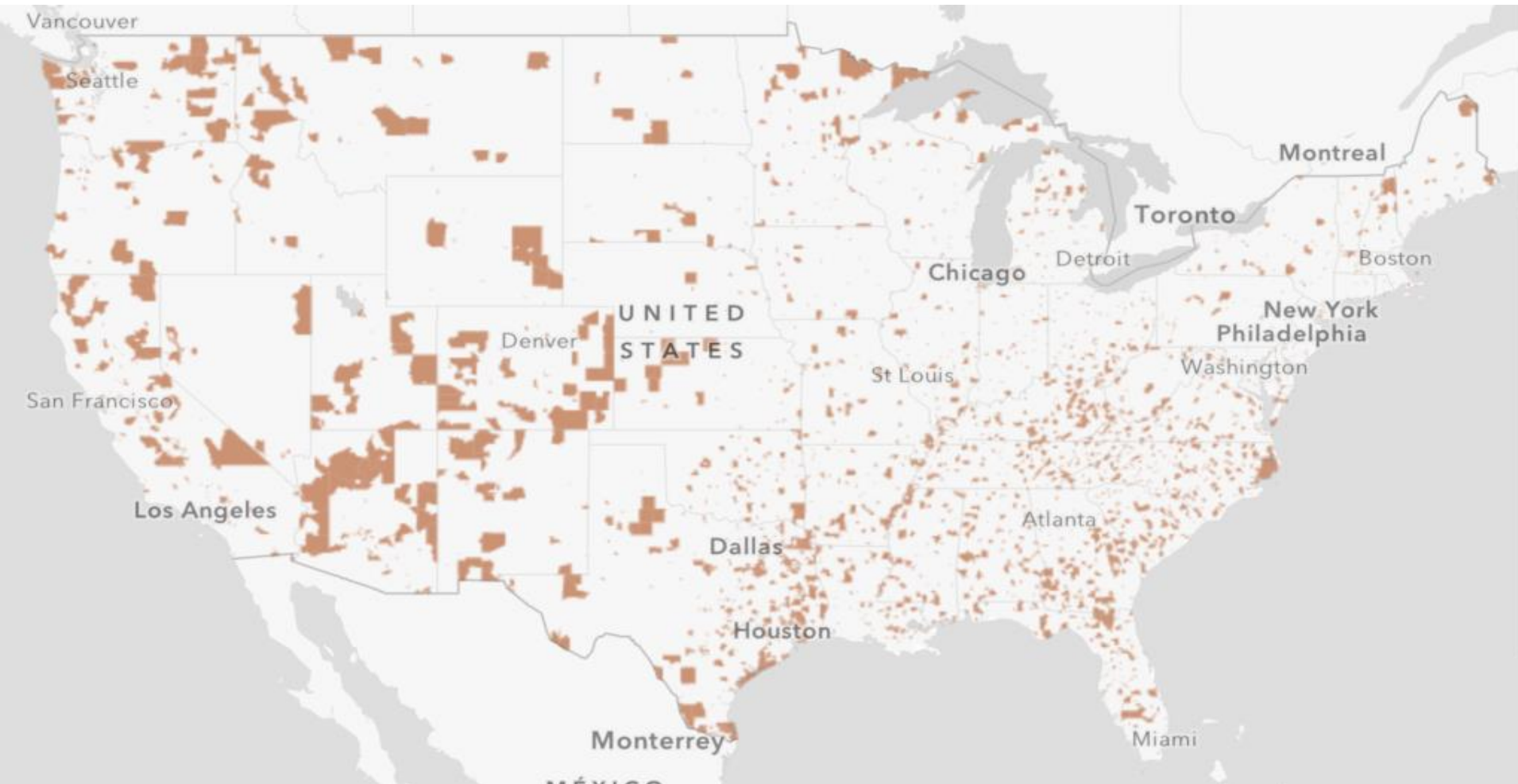
# Opportunity Zones

- 8,700 Opportunity Zones across the United States
- Texas has 628 Opportunity Zones in 145 counties
- Nominated by Governors in early 2018. All Opportunity Zones designated by the U.S. Department of the Treasury as of June 2018.
- Opportunity Zones are low-income census tracts eligible for investment from Opportunity Funds.

# Opportunity Zones

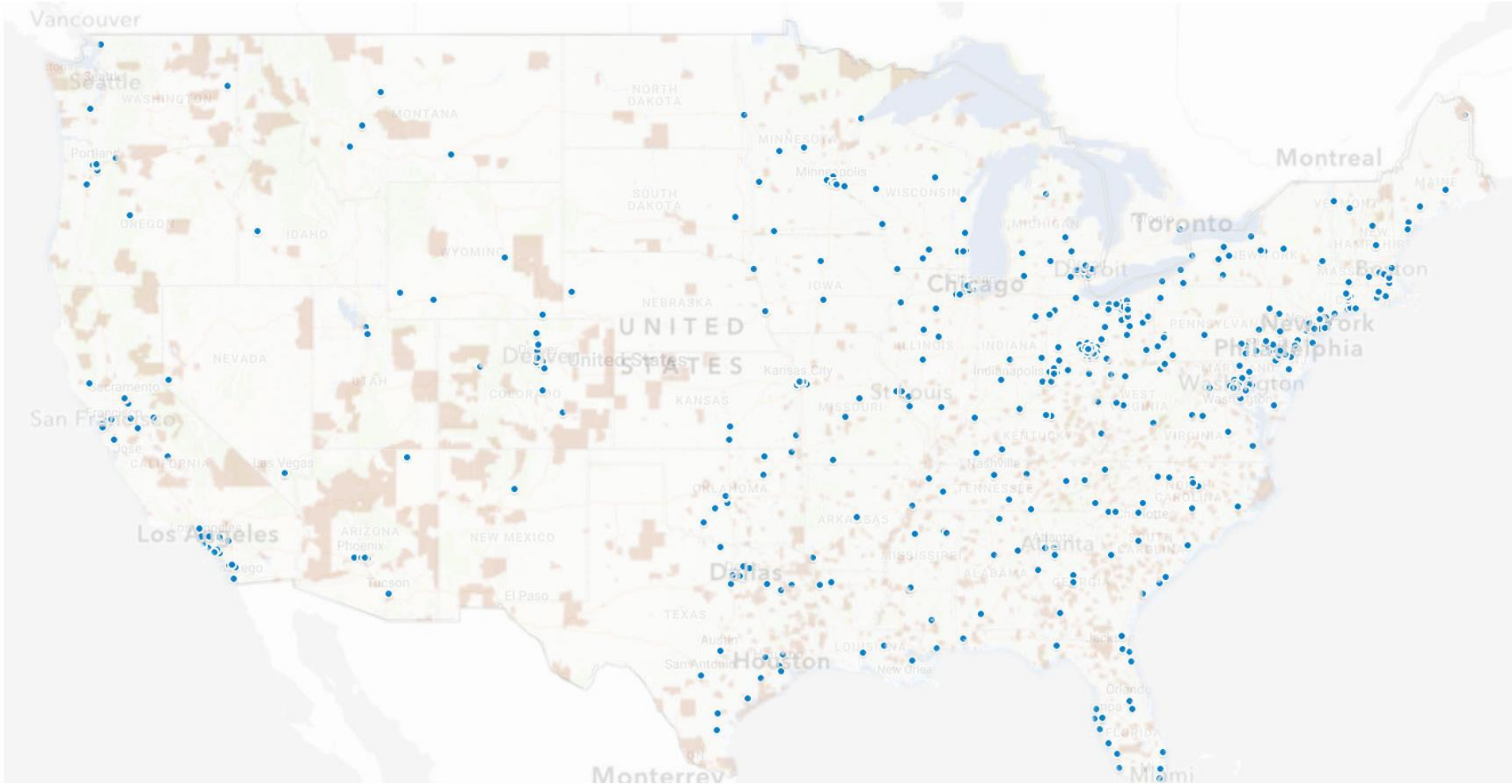
- Approximately 35 million people live in Opportunity Zones
- 56% of those residents are minorities
- 294 Zones are tribal lands
- 76% are in metropolitan areas

# Opportunity Zones

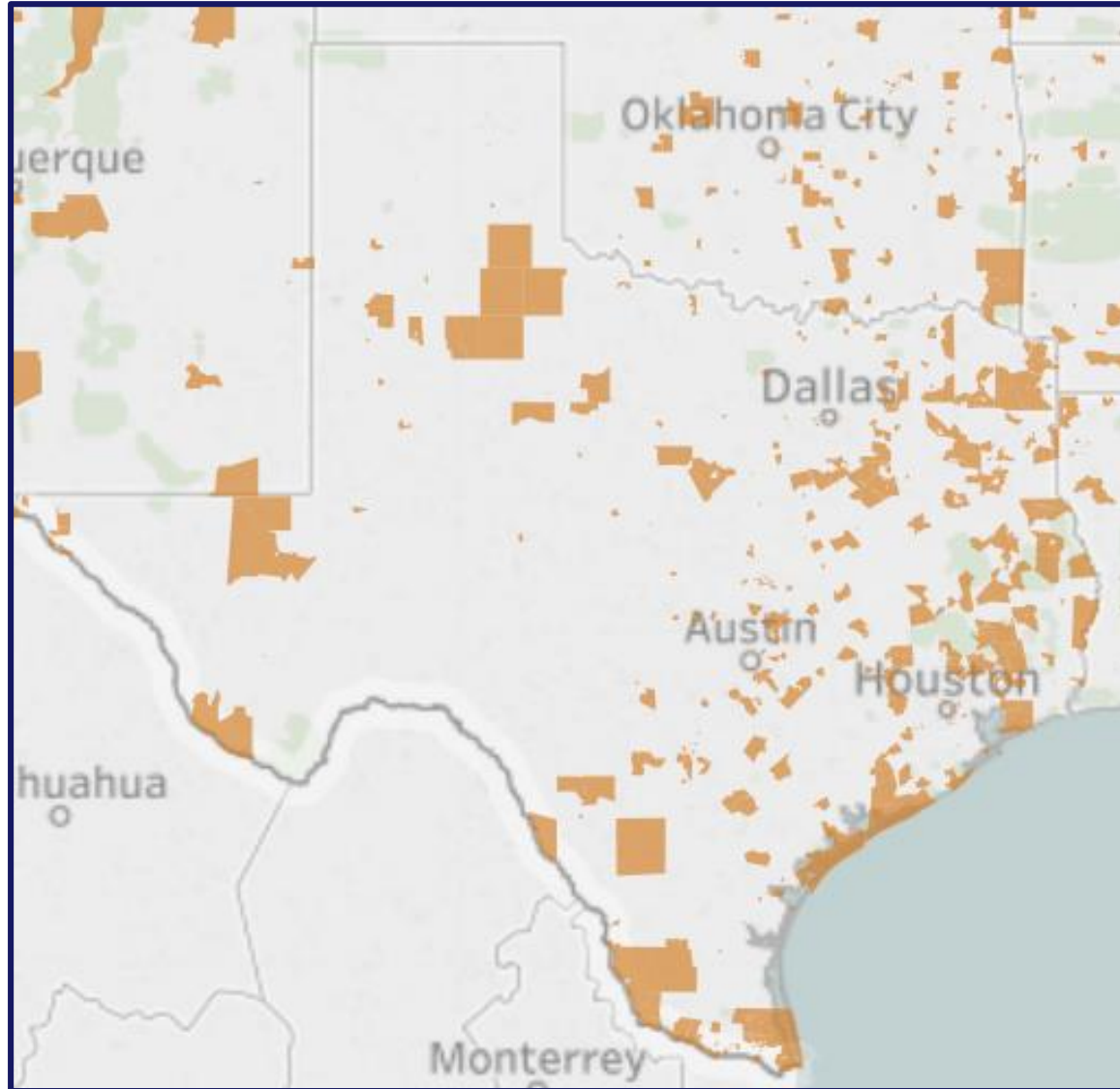




# CDFA Members + Opportunity Zones



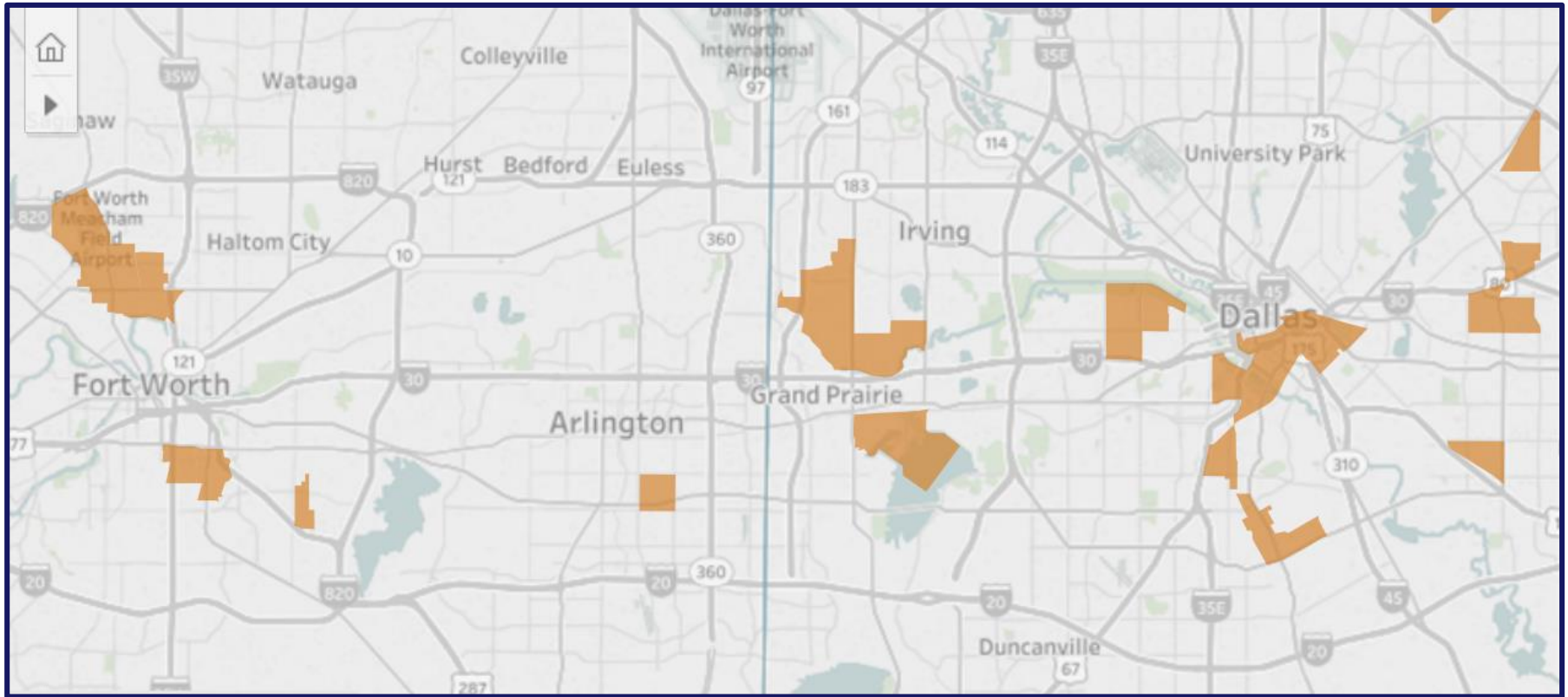
# Texas Opportunity Zones



Source: Ohio Development Services Agency



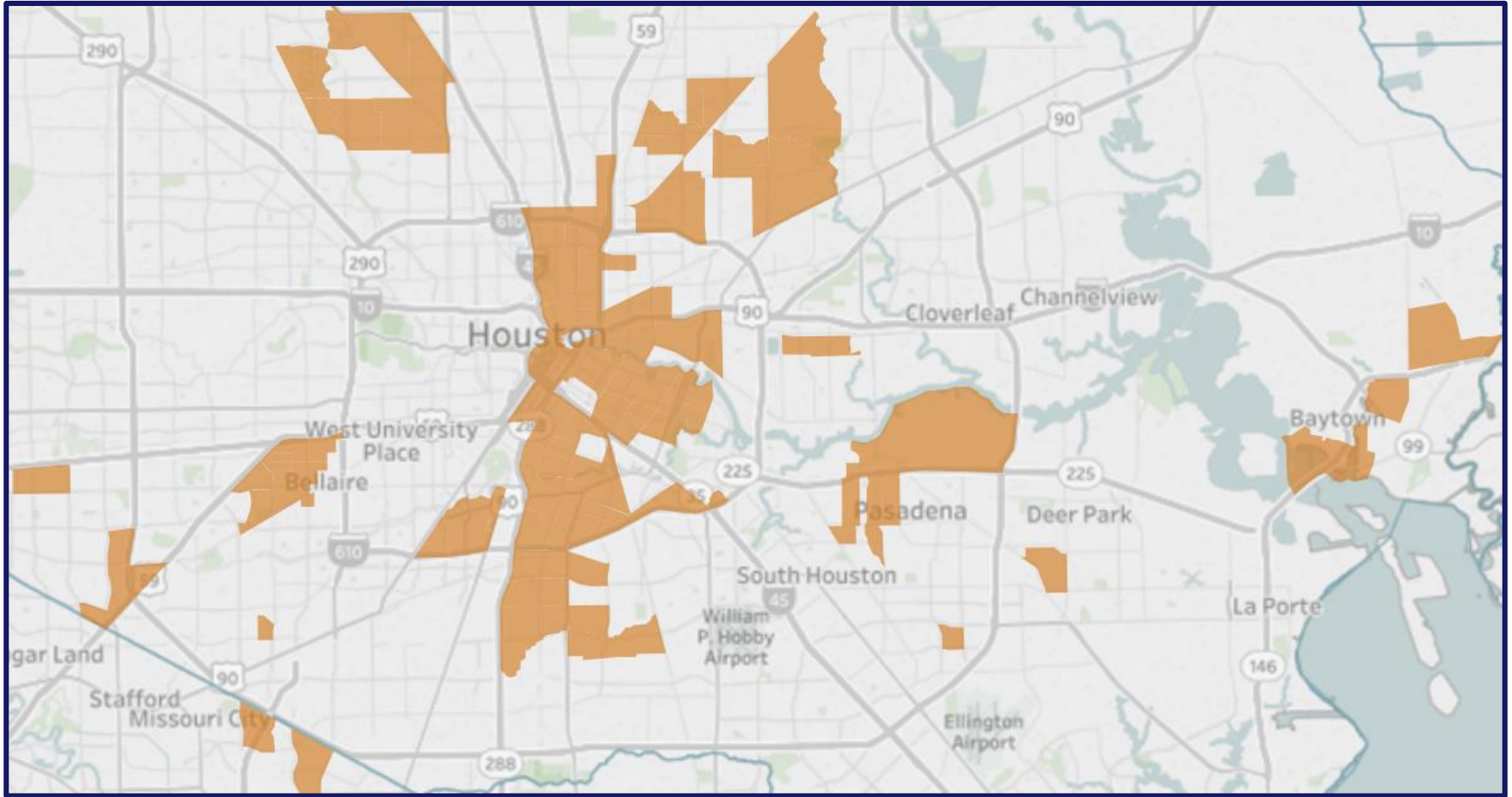
# Dallas/Ft. Worth Opportunity Zones



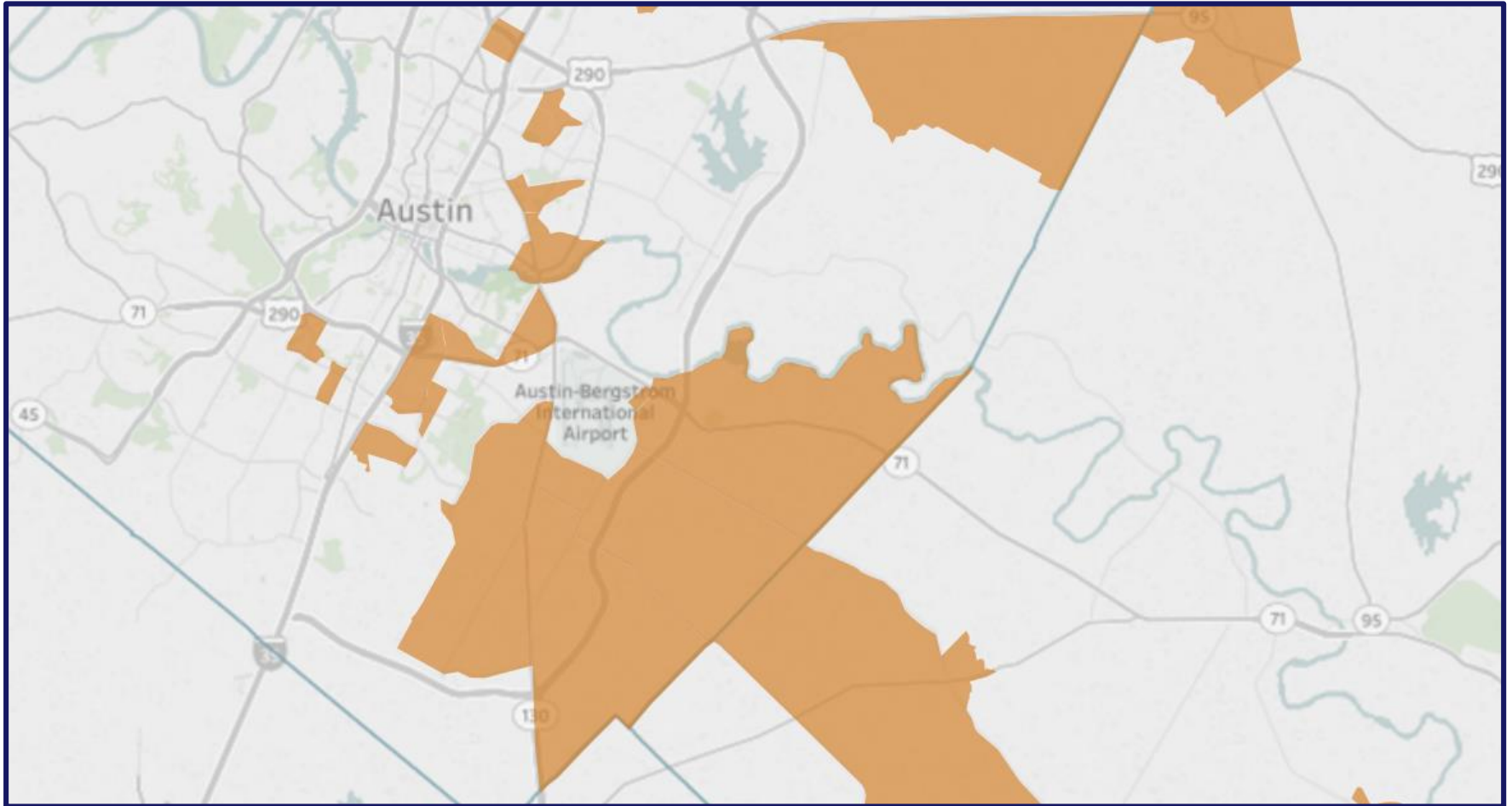
Source: Ohio Development Services Agency



# Houston Region Opportunity Zones



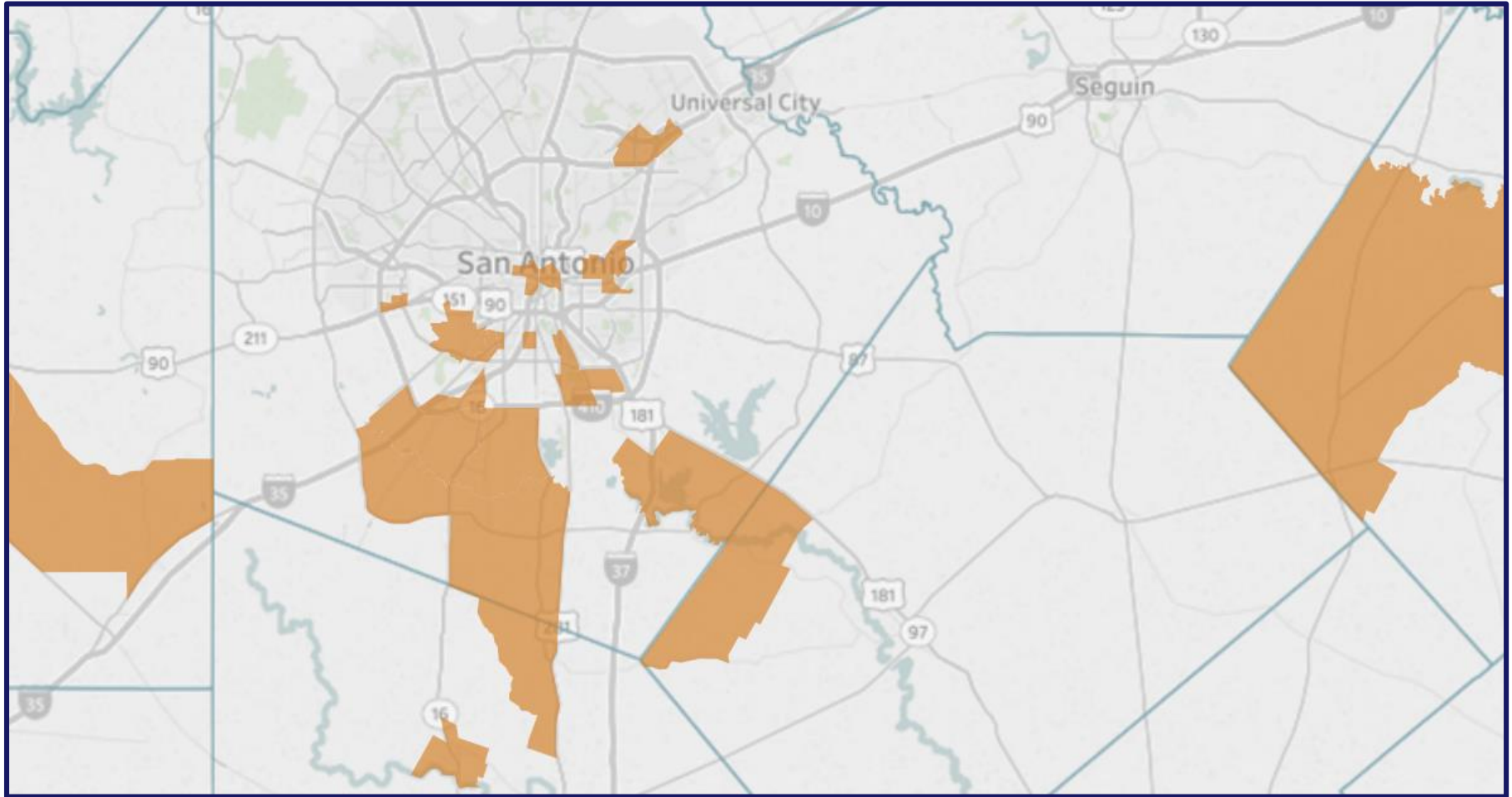
# Austin Region Opportunity Zones



Source: Ohio Development Services Agency



# San Antonio Region Opportunity Zones



# Opportunity Funds

**Opportunity Funds can help tap into the estimated \$6 trillion market for unrealized capital gains.**

What are the benefits to investing in Opportunity Funds?

- Defer taxes owed on federal capital gains taxes by moving them into an Opportunity Fund. If invested for 5 years, receive a 10% reduction in the tax. If invested for 7 years or more, receive a 15% reduction in the tax.
- Investors can defer the tax on their capital gains until the earlier of the date the Opportunity Fund investment was sold or December 31, 2026.
- For investments held at least 10 years, any earnings realized by an Opportunity Fund are not subject to federal capital gains taxes.

# Opportunity Funds

## **Opportunity Funds must make equity investments.**

- Investors can capitalize Opportunity Funds using gains realized within 180 days of a sale. No limit on size of funds, number of funds, or how many Opportunity Zones the fund invests in.
- Opportunity Funds must invest at least 90% of their assets in qualified investments located in Opportunity Zones.
- Opportunity Funds can make equity investments in qualified businesses or real estate projects.
- Opportunity Fund investors are seeking responsible exit solutions in order to realize the tax free earnings after the 10 year period.



# Opportunity Funds

## Where can Opportunity Funds invest?

Opportunity Fund assets can be invested in the following:

- Opportunity Zones stock
- Opportunity Zones partnership interests
- Opportunity Zones business property

**Note:** IRS Proposed Guidance for Opportunity Funds released October 19.

Visit [www.cdfa.net](http://www.cdfa.net) to read the publication.





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## Now Speaking



### **Byron Sarhangian**

Partner

Snell & Wilmer

Phoenix, AZ

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# Opportunity Zone Program Tax Cuts and Jobs Act

Byron Sarhangian

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Snell & Wilmer  
LAW OFFICES

## 3 Tax Incentive Benefits

### 1. Temporary Deferral of Eligible Gain

- *Applies to any capital gain from the sale or exchange of any property to an unrelated person*
- *\$6 trillion of potential eligible capital*

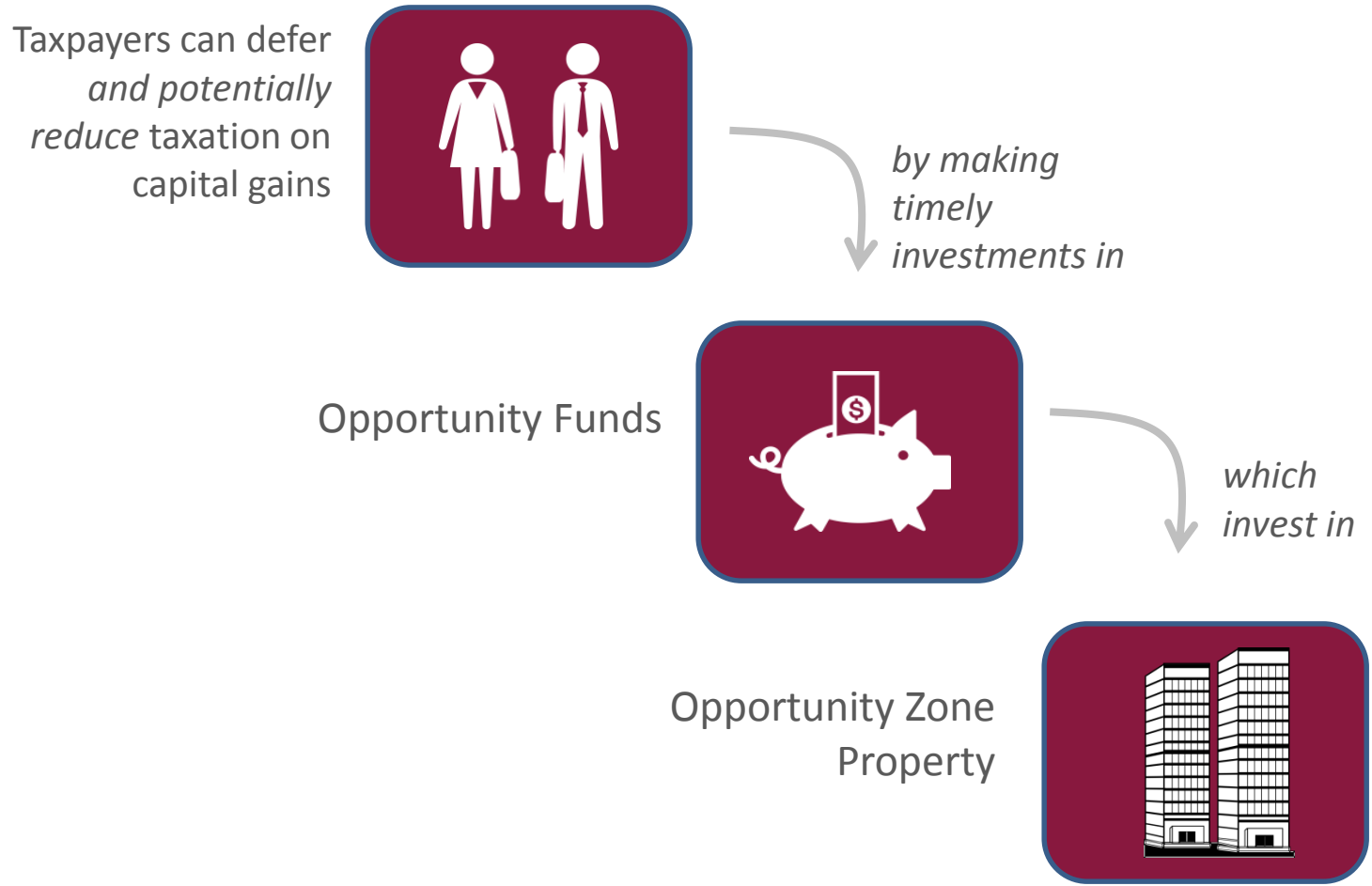
### 2. Partial reduction of Deferred Gain

- *Income Tax is still paid on a large portion of the Deferred Gain*

### 3. Forgiveness of Additional Gain

- *Applies to the Appreciation in the Investment*

# How do Taxpayers Benefit?



Source: Novogradac & Company LLP

# Eligible Gains

- Eligible Gains
  - Capital Gains
    - Long-term
    - Short-term
  - Section 1231 Gains
  - Section 1250 Unrecaptured Gain
- Not Eligible
  - Depreciation recapture (Ordinary Income)
  - Inventory
- Tax Attributes are Retained

## 180-Day Period

- Must invest in an Eligible Interest in an Opportunity Fund within 180 days from the Sale or Exchange of the Property
- Multiple Elections are Possible within a Single Gain:
  - Invest in different funds
  - Must use same 180-day period
- Special rule for Pass-through Entities

# Temporary Deferral of Gain

- Applies to any Eligible Taxpayer
- Sale or Exchange of Property to an Unrelated Person
- On or before December 31, 2026
- Election is made by the Taxpayer
- Deferred Gain: The Aggregate Amount Invested That Does Not Exceed the Amount of Gain Generated
  - In an Opportunity Fund (O-Fund) as an Eligible Interest
  - Within 180 days of the sale/exchange



## Deferred Gain: When & How Much

**When:** Includable in taxable income for the taxable year which includes the earlier of:

- Investor's sale of its interest in the O-Fund; or
- December 31, 2026

**How Much:** Subject to income tax is based on the lesser of:

- Amount of the Deferred Gain
- or*
- The fair market value of investment in the O-Fund

*Less*

The Taxpayer's basis in the O-Fund

- **Ability to Invest Previously Deferred Gain in new O-Fund**

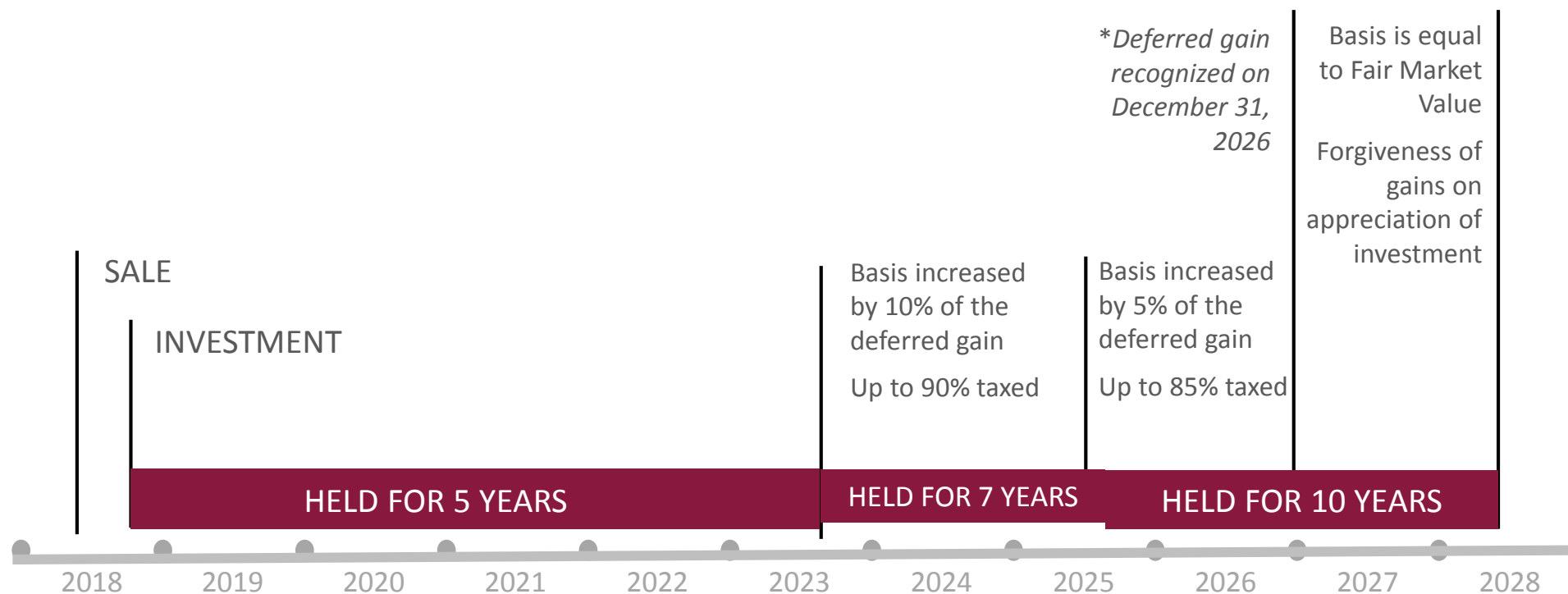
## Partial Reduction of Deferred Gain (Tax Basis)

- **Taxpayer has an Initial Basis in the O-Fund of Zero**
- **Hold for 5 Years**
  - Investor's tax basis in the O-Fund is increased by 10% of the amount of the Deferred Gain
- **Hold for 7 Years**
  - Investor's tax basis in the O-Fund is increased by an additional 5% of the amount of the Deferred Gain

## Full Forgiveness

- Where Investor holds its interest in the O-Fund for at least 10 years:
  - Elections to step-up the Tax Basis to FMV of Investor's interest in the O-Fund on the date of the sale or exchange
    - *Significant benefit but must hold long term*
  - The result is no gain on the appreciation above Investor's original investment in the O-Fund.
    - *Perhaps no income tax on depreciation recapture?*
  - **Sale or Exchange must be on or before December 31, 2047 in order to make the election**
- Phantom income issue arising on December 31, 2026

# Deferral, Partial Reduction, and Forgiveness of Additional Gains



Source: Novogradac & Company LLP

## Example\*

- Investor sells stock for \$30M (\$20M of long term capital gain) on July 1, 2018
- Investor invests \$20M in an interest in an O-Fund on November 1, 2018.
  - Does not need to invest the entire \$30M
- December 31, 2026:
  - Investor's tax basis in the O-Fund was increased by \$3M (15% of \$20M)
    - \$2M on November 1, 2023, and \$1M on November 1, 2025.
  - Investor has to pay tax on \$17M long-term capital gain
- November 2, 2028:
  - Investment in the O-Fund has appreciated from \$20M to \$60M (\$40M in potential gain)
  - If the investment in the O-Fund is sold, then there is no taxable gain on the \$40M of appreciation.

\* Results/outcomes may vary

## Opportunity Fund Certification

- Self-Certification using Form 8996
  - Attached to the taxpayer's federal income tax return for the taxable year, taking into account extensions.
- Identify the “first taxable year” and “first month” entity wants to be an O-Fund
- Investments made before the first month not eligible
- Where less than 6 months remaining in taxable year from first month then 90% Requirement is measured on last day of year



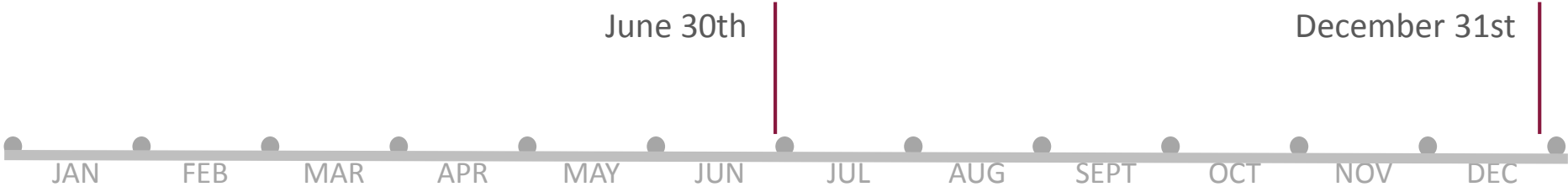
# Opportunity Fund – 90% Requirement

Must hold at least 90% of assets in Opportunity Zone Property, determined by the average of the percentage of Opportunity Zone Property held on:

The last day of the first six month period of the fund's taxable year

*And*

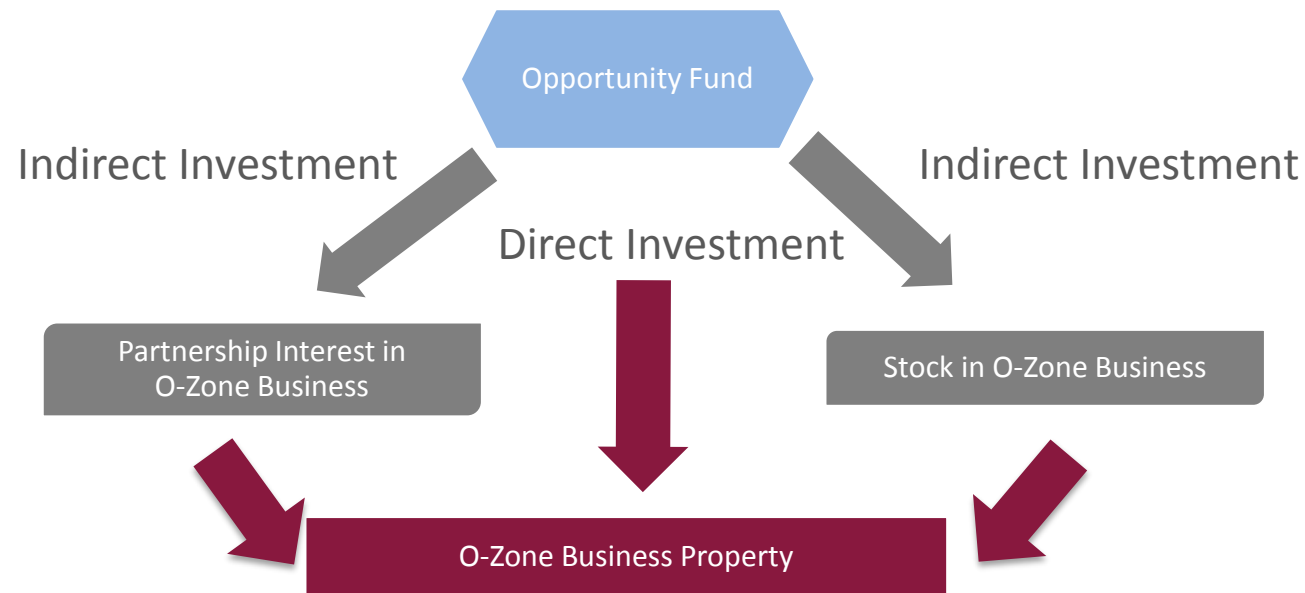
The last day of the fund's taxable year



Source: Novogradac & Company LLP

# Opportunity Zone Property

- Broad Definition - However, no debt.
- Investments that constitute O-Zone Property are:
  - Indirect Approach: Equity investment in an Opportunity Zone Business (an O-Zone Business).
  - Direct Approach: Direct purchase of Opportunity Zone Business Property (O-Zone Business Property).



Source: Novogradac & Company LLP



# Opportunity Zone Businesses - Regulations

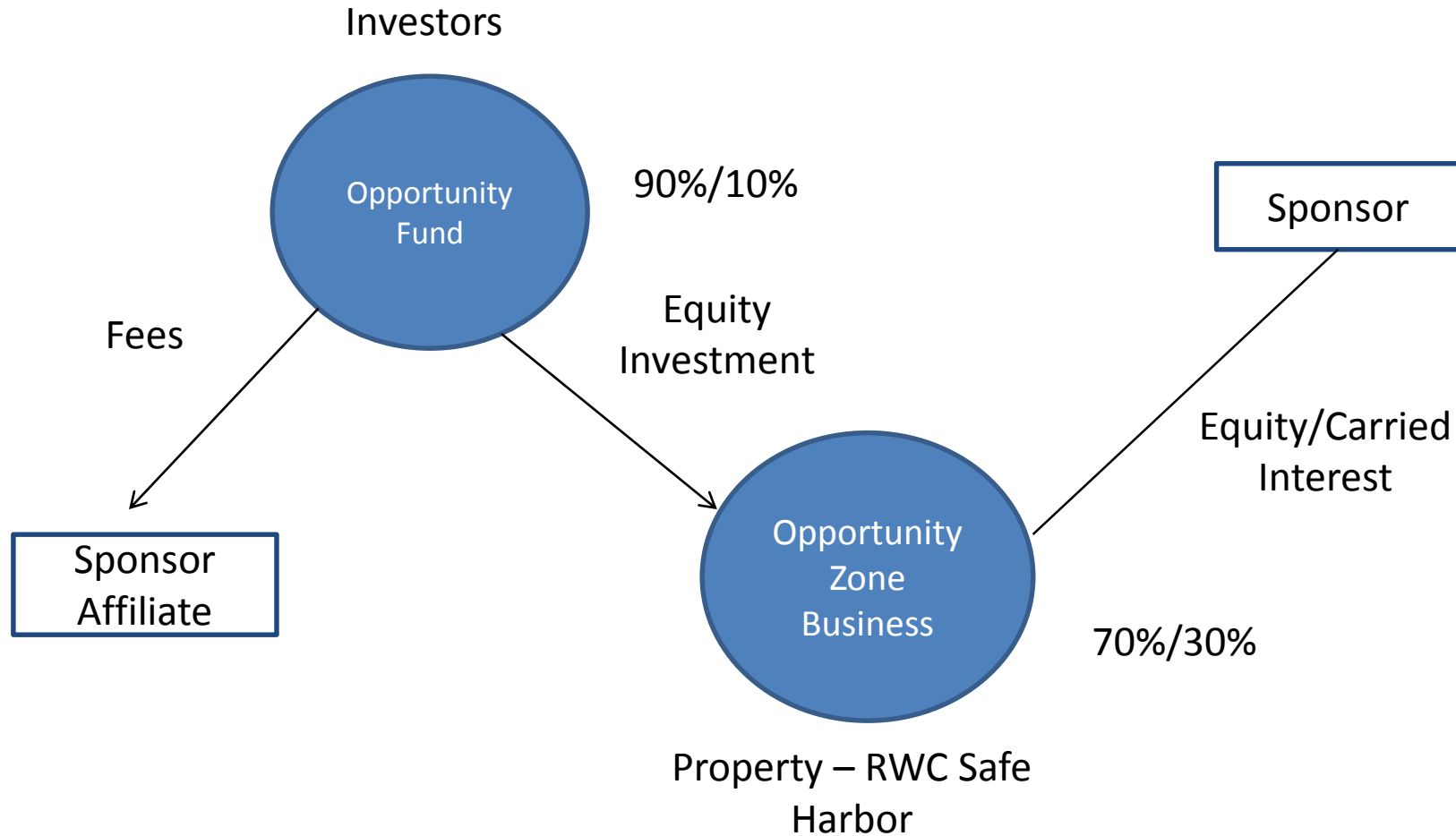
- Non-Qualified Financial Property
  - Less 5% of average of its assets can be cash or “cash type” assets
    - Does not include Accounts/Notes Receivable
    - Exception to NQFP for **reasonable amounts of working capital** (RWC) in cash, cash equivalents, or short term debt instruments (Working Capital Assets)
- **RWC– Safe Harbor-** Working Capital Assets are treated as RWC (Written Plan):
  - **Amounts designated in writing** for acquisition, construction, and/or substantial improvement of tangible property in an Opportunity Zone;
  - **Written schedule** consistent with ordinary start-up of a business for expending the Working Capital Assets within 31 months of receipt; and
  - Working Capital Assets are **actually used** in a manner that is **substantially consistent** with the previous provisions.

## Excluded Businesses

*Can't be a "Sin Business"*

- Golf Course
- Country Club
- Massage Parlor
- Hot Tub Facility
- Suntan Facility
- Racetrack (or other gambling facilities)
- Any store the principal business of which is the sale of alcoholic beverages for consumption off premises

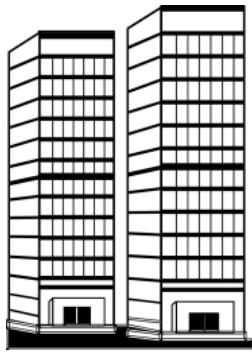
# Indirect Approach Structure



## Special Rule – Acquisition of a Building

- Acquiring a Building an Underlying Land
  - Substantial improvement requirement met by improving the building
  - Revenue Ruling 2018-29
    - 60%/40% (Land/Building)
    - Re-purposing of the building
    - Adding to the basis of the building (125%)
    - Cannot have original use with respect to land
  - What does this mean for vacant land?

# Possible Investments in Opportunity Zones



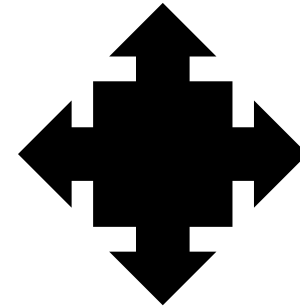
**Real Estate  
Development and  
Significant  
Rehabilitations in  
Opportunity Zones**



**Opening New  
Businesses in  
Opportunity  
Zones**



Acquiring an  
Existing  
Business and  
Relocating it  
(with  
Expansion) in  
an Opportunity  
Zone



Large Expansions  
of Businesses  
already within  
Opportunity  
Zones

*Source: Novogradac & Company LLP*

# Opportunity Zones – Status

- Guidance is needed to address many important issues:
  - *Residential Rental Property – Is it a problem for an O-Zone Business*
  - *Refinancing distributions*
  - *Interim gains issue (Reinvestment)*
    - *Avoiding the Penalty while holding cash*
    - *Not having an allocation of taxable gain to Investors*
    - *How long would the O-Fund have for reinvestment*
  - *Vacant Land – Substantial Improvement?*
  - *Multi-Asset Funds – Exit Mechanics*
  - *Meaning of the term “active” (to determine implication on triple net leases)*
- Second tranche will be released in late 2018/early 2019

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## Now Speaking



### **Michael Perrine**

Managing Director  
Baker Tilly Capital, LLC.  
Austin, TX

*In Partnership  
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## Opportunity Zones

Powerful new incentives for community investment and growth.

# About Baker Tilly

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# Benefits of the Opportunity Zone



- > **Deferral:** The original gain invested is taxable only when the investment in the Opportunity Fund is sold or Dec. 31, 2026, whichever occurs first.
- > **Partial forgiveness:** If the OZ investment is held five years, the original gain is discounted 10 percent (15 percent if held more than seven years). Investment must be made by Dec. 31, 2019, in order to qualify for 15 percent discount since tax on original gain is due Dec. 31, 2026.
- > **Tax-free appreciation:** If the Opportunity Fund investment is held for more than 10 years, the tax basis of the OZ investment steps up to its fair market value upon sale.

# How might this incentive benefit a Project or Company?



Some ways location within an OZone may help -

- \* Reduce cost of capital
- \* Fulfill/close gaps in capital stack
- \* Quicker project realization and stabilization
- \* Available to combine with existing tax credit programs and other tax incentives such as governmental grants or subsidized lending

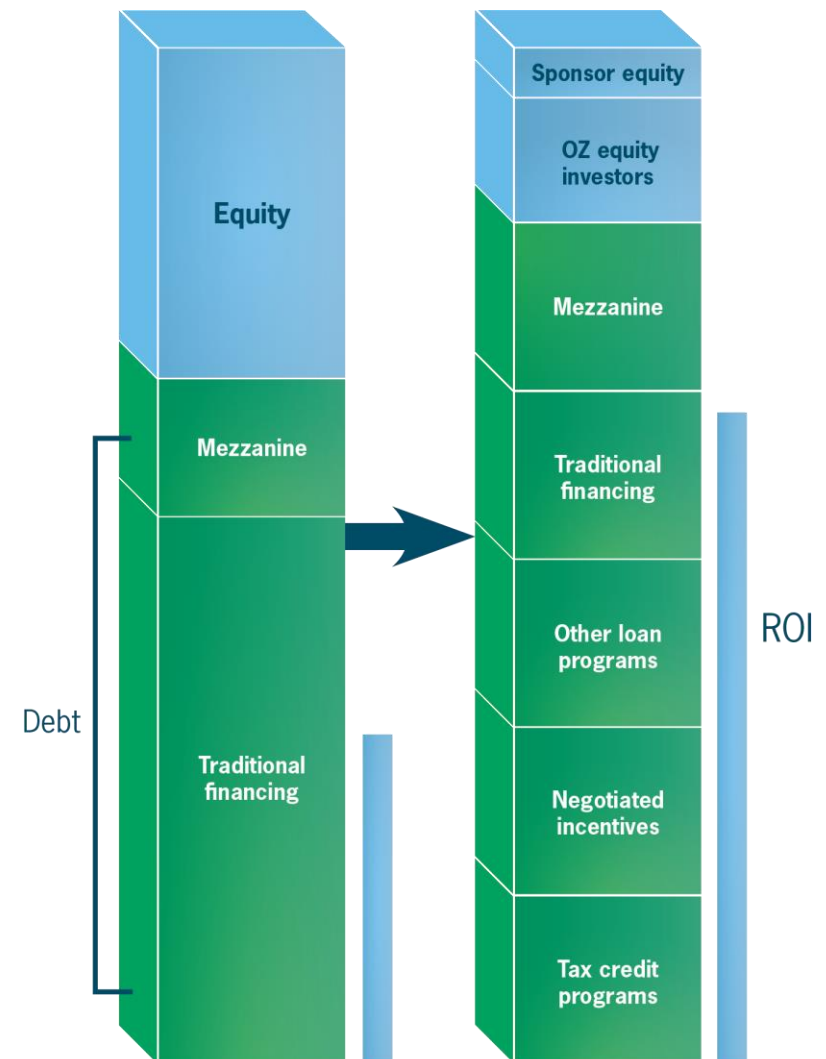
Benefits apply to varied asset classes, project types and operating ventures. Updates to guidance expected.

# Layering of incentives illustration



## Benefits

- > Makes projects economically feasible
- > Higher return on investment
- > Lower cost of capital
- > Lower owner's investment
- > Higher probability of successful project
- > Opportunity to expand the project without expending additional funds
- > Potential shifting of tax attributes to sponsor



# Opportunity Zone eligible areas



Eligible areas based on low-income census tracts and tracts contiguous to these low-income census tracts

- > 8,000 Opportunity Zones in the U.S.
- > 11 percent of country is designated as an Opportunity Zone
- > We expect more guidance on Opportunity Zone Funds, Opportunity Zone Businesses and Opportunity Zone Properties soon
- > An interactive map of Opportunity Zones is available at [\*\*bakertilly.com/opportunityzones\*\*](https://bakertilly.com/opportunityzones)



# New Markets Tax Credits (NMTC)



## Program overview

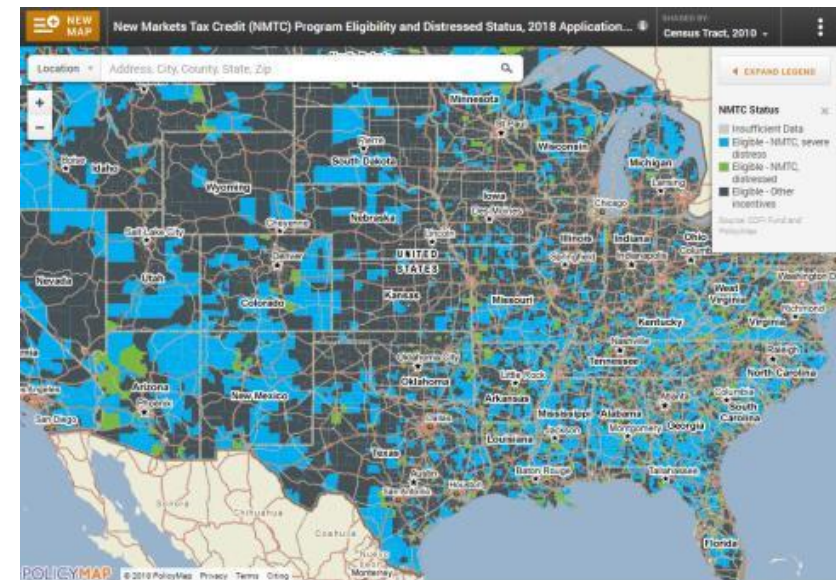
- > Created in 2000 to encourage investment in eligible low-income communities
- > Investors (receiving benefit of federal tax credit) provide low-interest loans to businesses

## Eligibility

- > Location
- > Community benefit through job creation or retention, community services, environmental sustainability, etc.

## Funding

- > Based on a competitive application model



[bakertilly.com/nmtc-lihtc-tax-credit-mapping-tool](http://bakertilly.com/nmtc-lihtc-tax-credit-mapping-tool)

# How long is the designation?



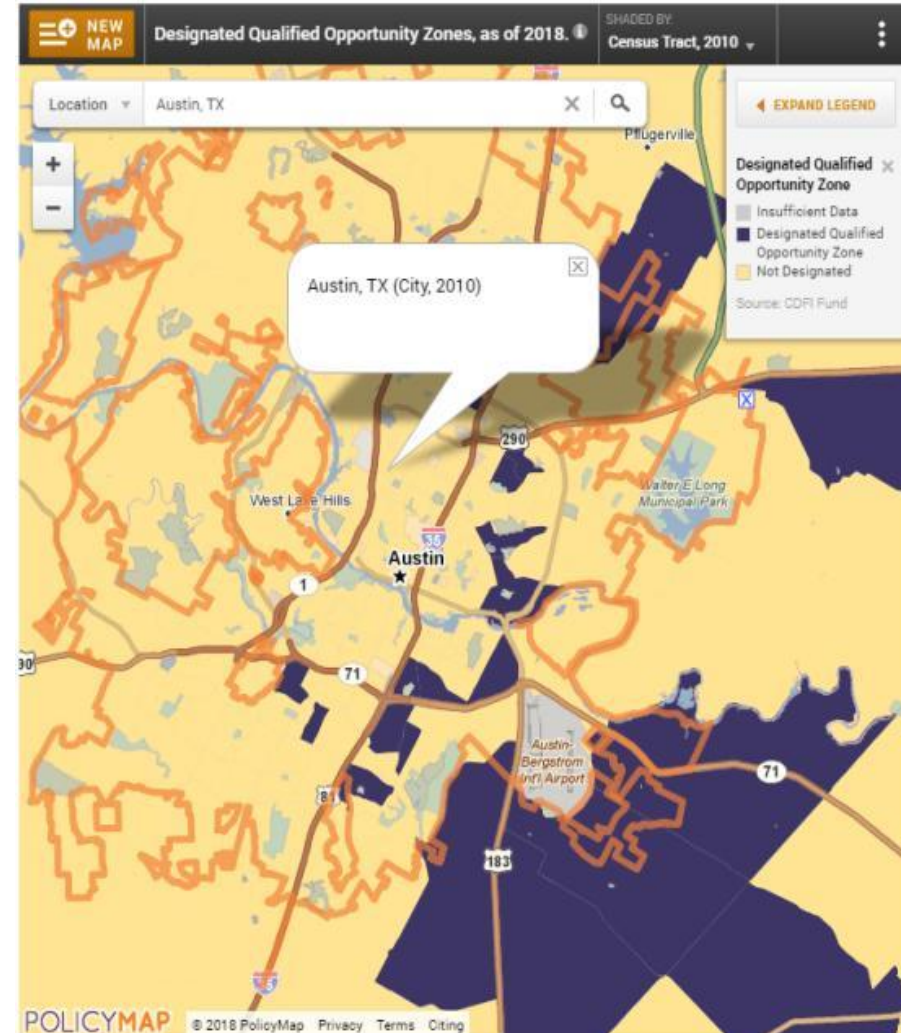
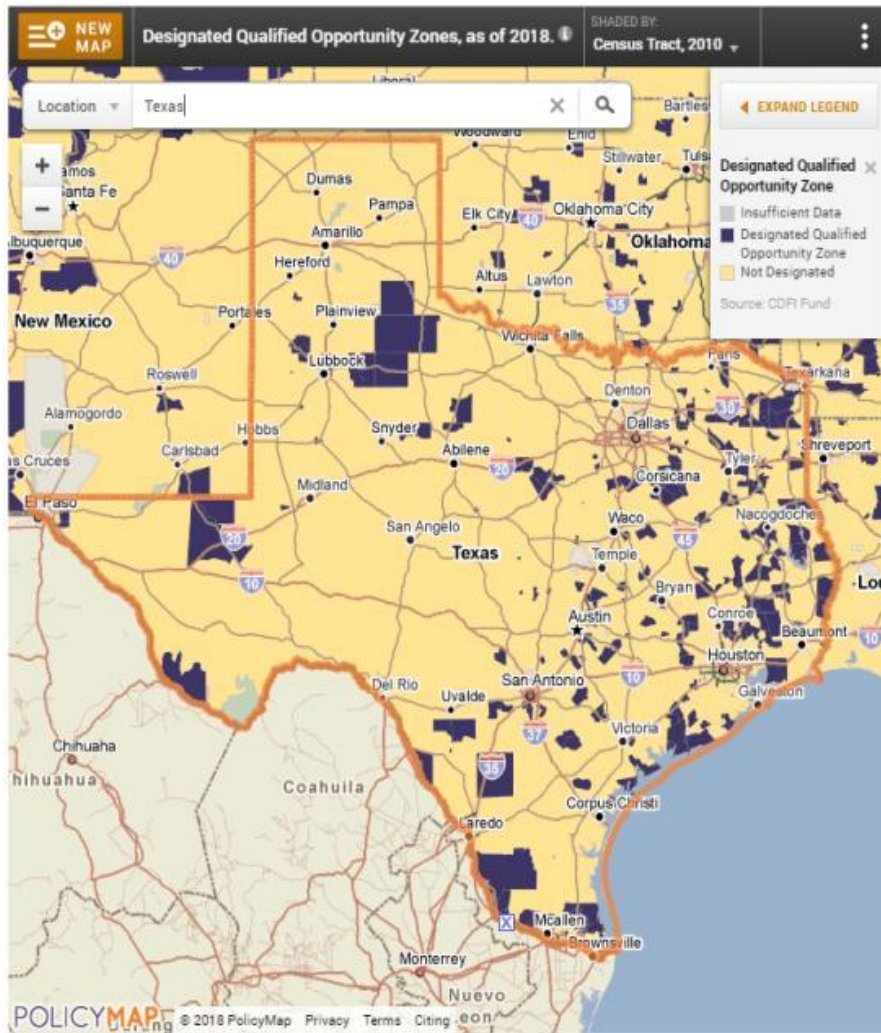
- > The designation of a census tract as a QOZ remains in effect until December 31, 2028
- > This means that the benefits of this program are available for qualified investments until June 29, 2029 – 180 days after 12/31/28 (date QOZ designation expires)
- > The regulations clarified that if an investment is made, and during the holding period of the investment the QOZ designation expires, the investor can still obtain the tax benefit of tax-free appreciation on a sale of their investment until a hard date of 2047



# Baker Tilly's OZ mapping tool



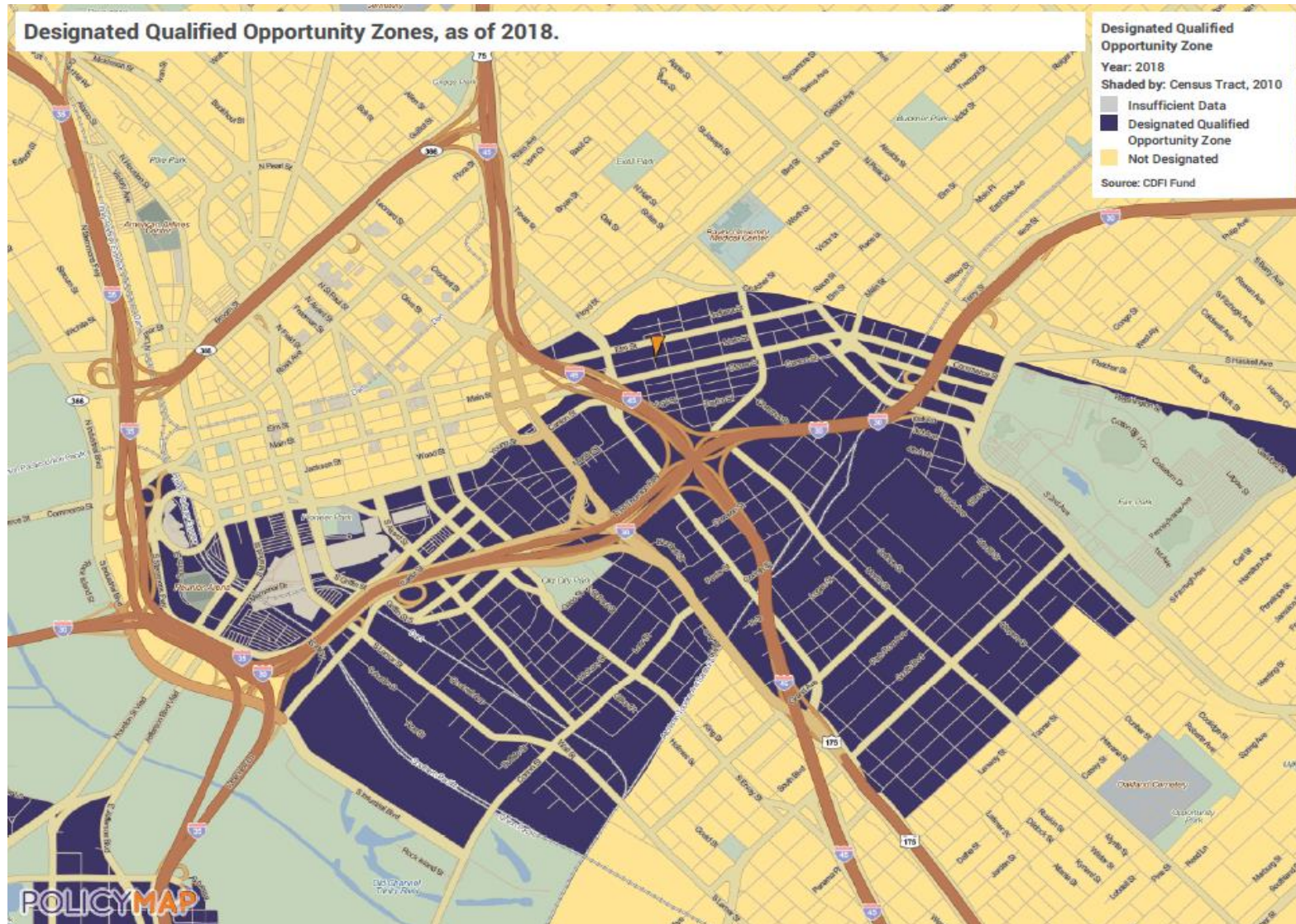
Find eligible areas at [bakertilly.com/opportunityzones](https://bakertilly.com/opportunityzones)



# Downtown Dallas – Deep Ellum to Fair Park



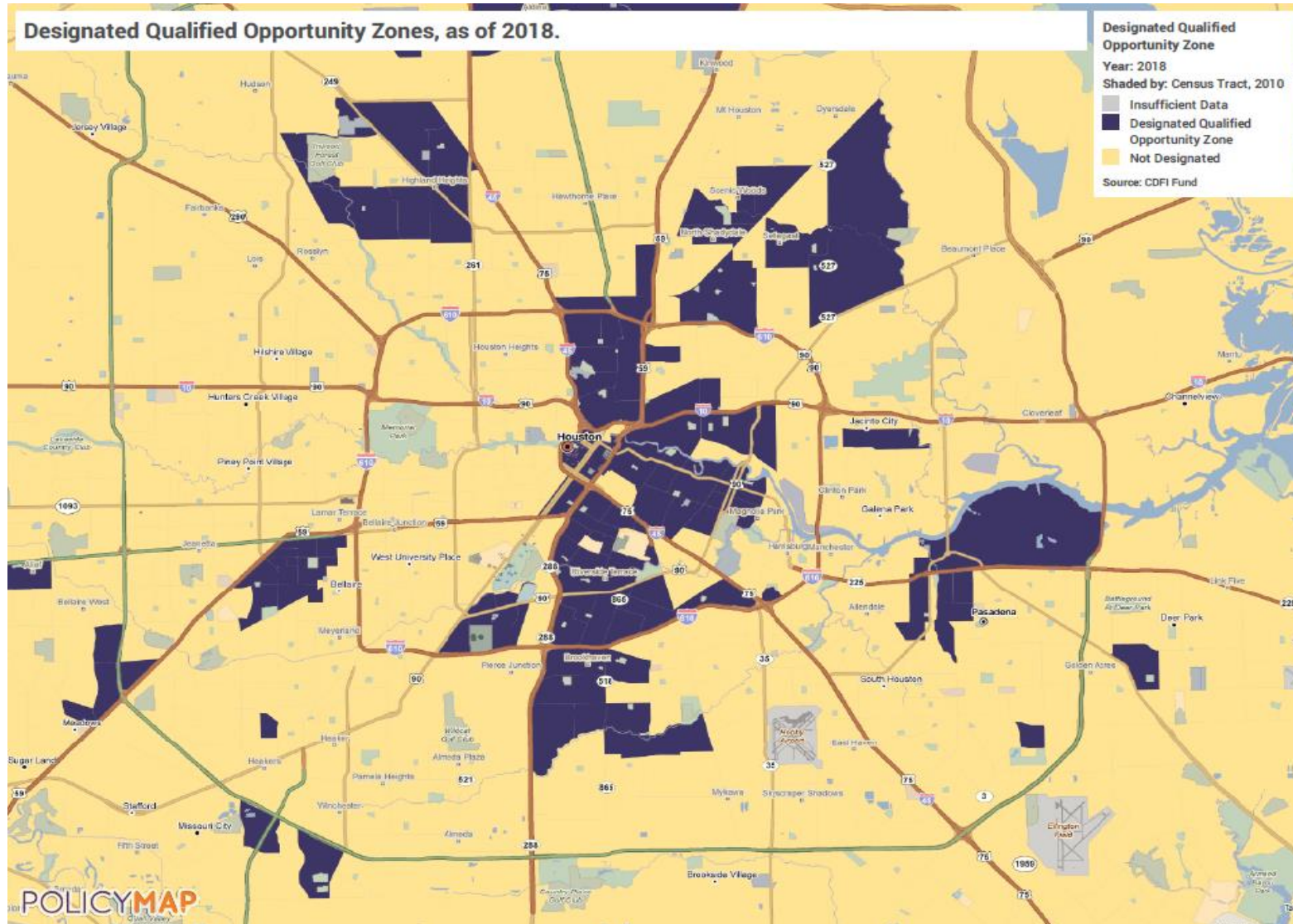
Find eligible areas at [bakertilly.com/opportunityzones](https://bakertilly.com/opportunityzones)



# Houston and vicinity



Find eligible areas at [bakertilly.com/opportunityzones](https://bakertilly.com/opportunityzones)



# What investment types does the OZ program favor?



## Commercial real estate

- > Works well since the program is focused on long-term investment and real estate is not going to grow out of compliance like an operating business potentially could

## New business startup in an OZ after Dec. 31, 2017

- > Also works well since it meets the requirements of the qualified Opportunity Zone Business Property

## Expanding an existing business into an OZ

- > Works well, but if the business outside of the OZ is a substantial part of your business, may have to set up a regarded entity to run operations inside the OZ; new 70/30 rule for qualified Opportunity Zone business affords some leeway

## Small business already in an OZ with large expansion

- > If already in an OZ at Dec. 31, none of the assets would be Qualified Opportunity Zone Business Property; would have to meet “substantial improvement” requirement

# Original use or substantial improvement



The original use of the Opportunity Zone property must commence with the fund or there must be “substantial improvement” to the property.

- > The Opportunity Fund has a 30-month window to improve the property, such that the basis of the property increases by an amount that exceeds the amount of the adjusted basis at the beginning of the 30-month period.
- > The basis of the land is excluded from the underlying calculation.
- > For example, an Opportunity Fund acquires a building for \$10 million, \$4 million attributable to the land and \$6 million attributable to the improvement; at the end of 30-month period, improvements of \$6 million +\$1 must be made.

# What type of investment qualifies?

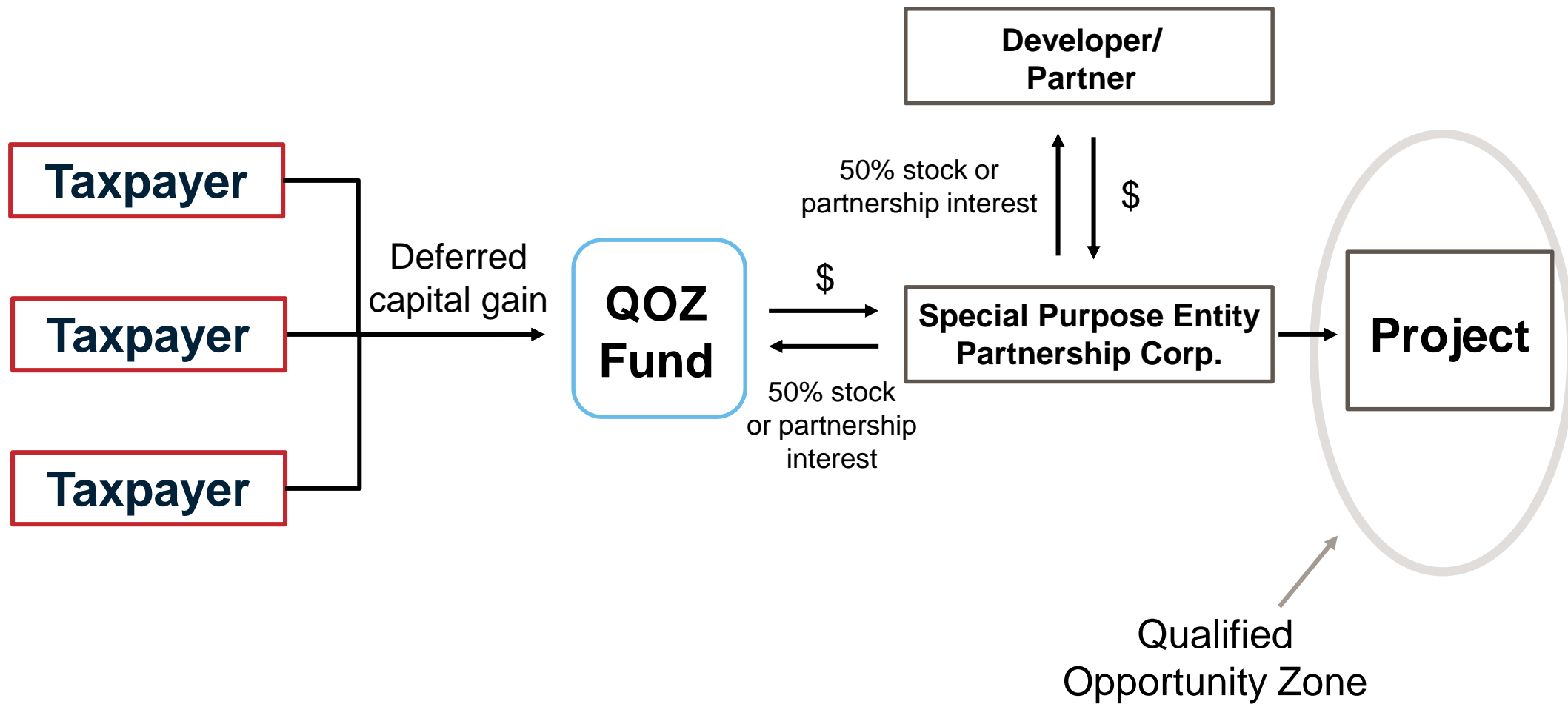


## Qualified Opportunity Zone business property means:

- > Tangible property used in a trade or business
  - We assume rental real estate qualifies as a trade or business since it is used in an example in the newly released guidance— Revenue Ruling 2018-29
- > Property acquired by purchase after Dec. 31, 2017
  - What about land already owned in an OZ? Does it qualify?
- > The original use of such property **in the qualified OZ** commences with the qualified Opportunity Fund or the Opportunity Fund substantially improves the property
  - Can you relocate an existing business into an OZ and qualify?
- > Where the Opportunity Fund owns the property directly, substantially all of the use of such property occurs within a qualified OZ
  - What happens if a business expands outside an OZ? What does “substantially all” mean for this purpose?



# Investment structure: indirect investment



# Open issues exist – among others



- > **How does the “substantial improvement” requirement apply to a direct business requirement versus a real estate investment?**
  - We are waiting for further clarification on the application of the OZ legislation to an operating business
- > **Is public infrastructure an allowable investment for an Opportunity Fund?**
  - The law does not prohibit investment in public infrastructure, but infrastructure alone is probably not a permissible investment since a government cannot accept equity investments
- > **Will states follow suit and exempt state taxes for OZ investors?**
  - Some states have adopted the federal OZ legislation, including Wisconsin, as well as adding their own layered benefits



*Data herein dated December 3, 2018*

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## Now Speaking



**City of Dallas**

**Robin Bentley**

Assistant Director, Economic Development  
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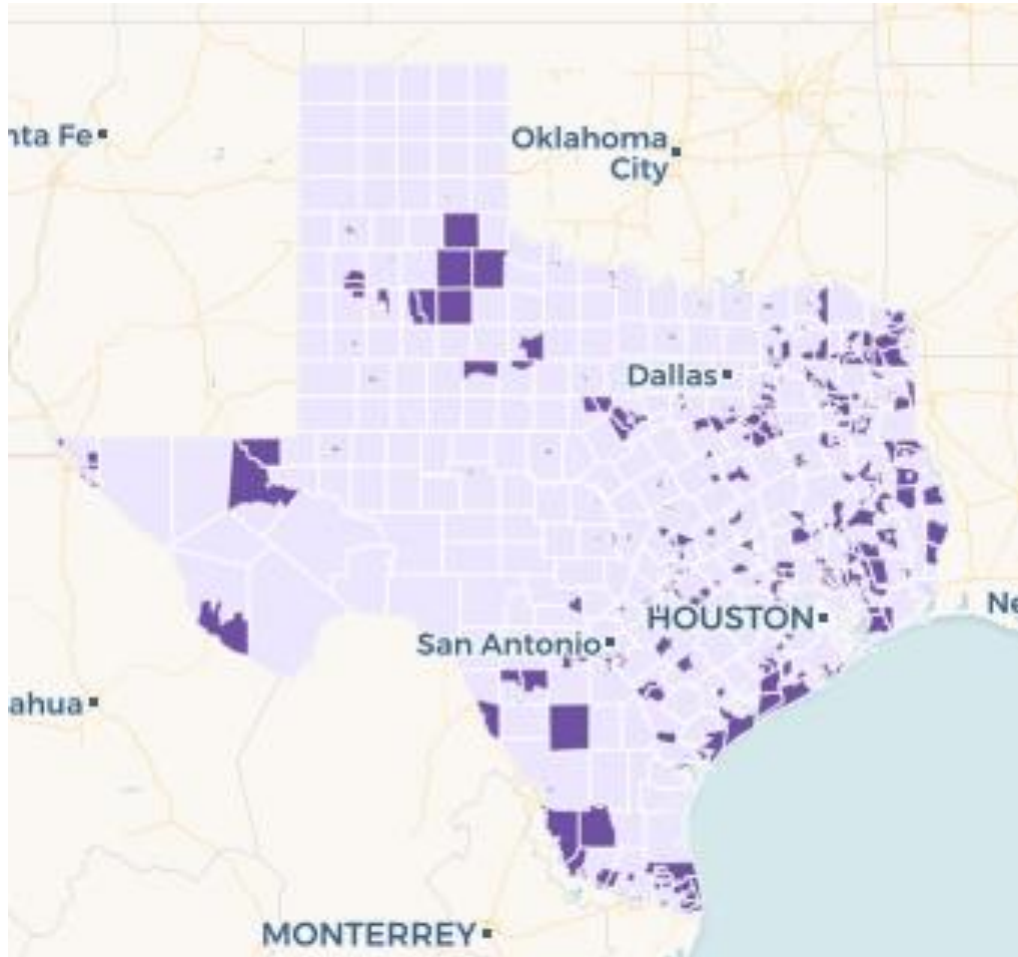


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# Local Strategies for Opportunity Zones

Robin Bentley  
Office of Economic Development  
City of Dallas

# Texas Opportunity Zones



- 628 Total Opportunity Zones
- 60% of Texas's zones are in a partially or fully rural census tract
  - Rural areas are overrepresented in zone selection, as only 38% of all Texas census tracts fall into the partially or fully rural designation
- Counties with the most zones:
  - **Harris** (105, 16.7% of the total zones)
  - **Bexar** (24, 3.8% of the total)
  - **Hidalgo** (23, 3.7% of the total)
  - **Travis** (21, 3.3% of the total)
  - **Dallas** (18, 2.9% of the total)

# Where are you in the process?



Opportunity Zones are a new program, and communities may be anywhere along this continuum in determining how to support and align with the federal legislation.

# BUILDING AWARENESS

## ▶ **First Steps**

- ▶ Determine your local contact
- ▶ Understand the program benefits
- ▶ Keep up to date on regulatory developments

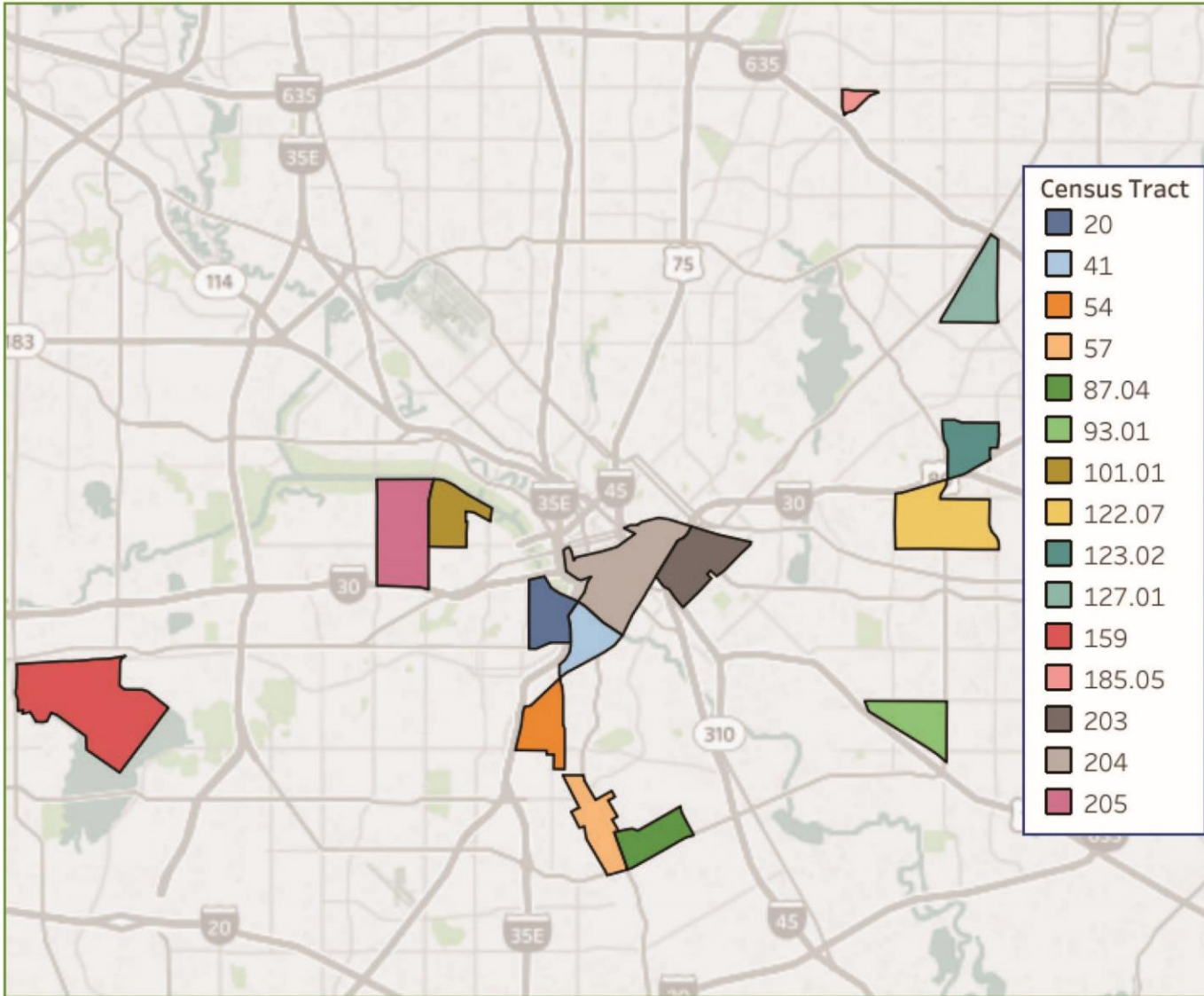
## ▶ **Local Discussions**

- ▶ Make sure your organization's leadership knows about the program and your zones
- ▶ Speak with large landowners in your zones

## ▶ **External Marketing**

- ▶ Create a basic map of your zones
- ▶ External marketing can be as simple as a handout or website update, or as complicated as a full prospectus

## Example Flyer



## CITY OF DALLAS OPPORTUNITY ZONES

The City of Dallas has  
15 federally-designated  
Opportunity Zones

Opportunity Zones can  
drive capital to support  
new businesses and  
investments in the  
targeted census tracts  
by providing Opportunity  
Zone investors with a  
deferral of capital gains  
taxes, among other tax  
benefits

# PENNSYLVANIA'S FLAGSHIP OPPORTUNITY ZONE

LOCATED IN THE HEART OF ERIE, PA



## City of Erie Investment Prospectus

Building Opportunity | Restoring Hope | Transforming Erie





# ALIGNMENT OF POLICIES

## ▶ Other States

- ▶ **MISSOURI:** reserving \$30 million of the state's Historic Preservation Tax Credits allocation for projects in Opportunity Zones.
- ▶ **ARIZONA:** Arizona Commerce Authority released an interactive tool called Arizona Assets which identifies infrastructure, land ownership, educational resources, and more in relation to the location of the state's Opportunity Zones.
- ▶ **KENTUCKY:** The Kentucky Cabinet for Economic Development has launched KYOZ, a website that will act as a central clearinghouse for all information related to Opportunity Zones in Kentucky, including a map of available industrial sites and buildings located in Opportunity Zones.
- ▶ **MICHIGAN:** Michigan State Housing Development Authority will begin adding a point system to their Qualified Allocation Plan for certain Opportunity Zones investments to receive Low Income Housing Tax Credits.

# ALIGNMENT OF POLICIES

## ▶ State of Texas

- ▶ Texas's favorable tax climate is already in general alignment with the program.
- ▶ However, opportunities exist to align OZ policies with the LIHTC QAP, the state historic tax credit program, state economic development incentives, and other state programs and policies.
- ▶ As of December 3, 2018, no Texas bills have been filed related to Opportunity Zones or Opportunity Funds.


# MINDFULNESS OF INCLUSION

Texas Opportunity Zone Data	Not Eligible	Eligible, Not Selected	Opportunity Zone
<b>Race/Ethnicity (%)</b>			
White	60.5	27.2	34.0
Black	8.0	14.8	18.9
Hispanic/Latino	24.1	54.2	44.6
<b>Poverty (%)</b>			
In poverty	8.6	26.5	28.1
<b>Education (%)</b>			
Less than high school	9.7	28.3	28.0
Bachelor's or higher	37.4	16.4	13.4
Percentage point increase in college graduates 2012–2016	7.6	19.2	21.9
<b>Median Home Value</b>			
Median home value 2016 (\$)	211,141	102,343	89,932
Percent increase in home value 2012–2016 (%)	12.5	7.0	9.3

 Indicates significant difference between OZ tract and eligible, not-selected tract

# MINDFULNESS OF INCLUSION

- ▶ Local governments do not have approval rights over Opportunity Fund investments unless the development is also seeking local incentives, zoning changes, etc.
- ▶ However, local governments can partner to mitigate the impacts of investment:
  - ▶ Neighborhood Empowerment Zones
  - ▶ Local Hiring Efforts
  - ▶ Participation in Workforce Development Efforts

The background features abstract, overlapping geometric shapes in various shades of blue, ranging from light sky blue to deep navy blue. These shapes are primarily located on the left and right sides of the page, framing the central white area where the text is placed.

**Robin Bentley**  
**Office of Economic Development**  
**City of Dallas**  
**[robin.bentley@dallascityhall.com](mailto:robin.bentley@dallascityhall.com)**



# CDFA Texas Webinar: The Latest on Opportunity Zones

## Audience Questions

*In Partnership  
with*

The logo for the Texas Economic Development Council (TEDC). It consists of the letters "T", "E", "D", and "C" in a bold, sans-serif font, each inside a colored square (blue, orange, yellow, and blue respectively). Below the letters is the text "TEXAS ECONOMIC DEVELOPMENT COUNCIL" in a smaller, all-caps, sans-serif font.

TEXAS ECONOMIC DEVELOPMENT COUNCIL

The header of the CDFA website. It features the CDFA logo on the left, the tagline "Advancing Development Finance Knowledge, Networks & Innovation" in the center, and a navigation menu on the right. The navigation menu includes links for "About", "Events", "News", "Sponsor", "Subscribe", "Membership", "Education", "Resources", "Advocacy", "States", and "Technical Assistance".

Advancing Development Finance Knowledge, Networks & Innovation

About Events News Sponsor Subscribe

Membership Education Resources Advocacy States Technical Assistance

### Opportunity Zones

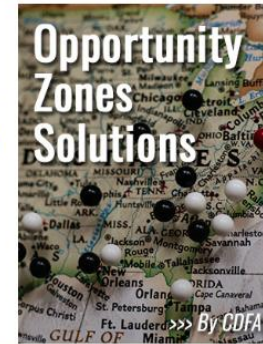
#### Overview

Created as part of the Tax Cuts and Jobs Act, **Opportunity Zones** are a federal economic development tool aiming to improve the outcomes of distressed communities around the country. Opportunity Zones are low-income census tracts that offer tax incentives to groups who invest and hold their capital gains in Zone assets or property. By investing in Opportunity Zones, investors stand to gain a temporary deferral on their capital gains taxes if they hold their investments for at least 5 years, and a permanent exclusion from a tax on capital gains from the Opportunity Zones investments if the investments are held for 10 years.

Support provided by



Want regular updates on Opportunity Zones? Subscribe to CDFA's **Opportunity Zones Update** newsletter.



+ How Opportunity Zones Work

+ Rules and Regulations

+ Official Treasury Designations

+ Opportunity Zones Resources

+ Headlines

*See all of CDFA's resources on Opportunity Zones online at [www.cdfa.net](http://www.cdfa.net)*



# CDFA Texas Webinar: The Latest on Opportunity Zones

## Upcoming Events

### **CDFA EDA Revolving Loan Fund Webinar Series: Developing a Loan Committee and Monitoring their Involvement**

December 11, 2018 | 2:00 PM Eastern

### **Intro Property Assessed Clean Energy (PACE) Finance WebCourse**

December 12-13 2018 | Daily: 12:00-5:00 PM Eastern

### **TEDC 2019 Legislative Conference**

February 20-22, 2019 | Austin, TX

**Register online at [www.cdfa.net](http://www.cdfa.net)**

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# CDFA Texas Webinar: The Latest on Opportunity Zones

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This webcast is designed to provide accurate and authoritative information in regard to the subject matter covered. It is available with the understanding that CDFA and the panelists are not engaged in rendering legal, accounting, or other professional services. If legal advice or other expert assistance is required, the services of a competent professional should be sought.