New Markets Tax Credits

An opportunity for your community

Valued Advisor Fund

NEW MARKETS
TAX CREDIT COALITION

The Business Valued Advisor Fund, LLC

Agenda

Investment in Opportunity Overview

Legislative and Local/National NMTC Economic Update

NMTC Basics and Lender/Investor Perspective

Brief Case Study

Q & A

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Investment in Opportunity Act

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Investment in Opportunity Act

The Investment in Opportunity Act (IOA) was included in the tax reform passed on December 22, 2017. The IOA is structured in many ways to rely on 45(D)(e) as a guide for investment area, asset type and anticipated reporting requirements. However, other aspects vary significantly.

Three Incentives Provided For:

- **Deferral**: Temporary Deferral of Capital gains for re-investments made into Qualified Opportunity Zone Funds (OZF's) made within 180 days of the sale of the of the subject asset. The taxpayer does not recognize its Capital gains until the earlier of 12/31/2026 or the time the Investment in the OZF is sold.
- **Reduction of Capital Gain**: If taxpayer holds investment in OZF for 5 years, 10% of the original gain is eliminated (i.e. basis in OZF investment will go from zero to 10% of capital gain), if held for 7 years in additional 5% is eliminated. It is not clear how these rules apply if the holding period straddles December 31, 2026, but it appears that recognition is still required on December 31, 2026 (unless Congress decides to extend such date).
- **Appreciation on Investment Excluded**: Appreciation on the OZF investment that is held for at least 10 years are not recognized. Specifically sale or exchange OZF held for 10 or more years, at the election of the taxpayer shall be at fair market value

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Example

Example

Assume a taxpayer owns stock with a basis of $50,000 and sells the stock in 2018 for $150,000. Ordinarily, the taxpayer would recognize $100,000 of capital gain in 2018. However, under the new program, the taxpayer may defer this gain and eliminate tax on future appreciation by investing the $100,000 capital gain in a Qualified Opportunity Fund within 180 days of the sale Unlike a like kind exchange you can reinvest funds from any asset class into an OZF and receive the tax benefits

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Example

Holding Period	Gain from Original Capital Asset	Gain from Fund Appreciation
2 Years	$100,000	$100,000
5 Years	$90,000	$100,000
7 Years	$85,000	$100,000
10 Years	$85,000	$0

OZF's

Qualified Opportunity Zone Funds must be corporations or partnerships formed to invest in Qualified Opportunity Zone census tract (QOZ). An OZF must maintain 90% of its assets invested in QOZ's throughout the investment period – subject to meeting reasonable cause testing – it will be required to pay a monthly penalty based on a calculation of the under-investment multiplied by the underpayment rate in the Code. If structured as a partnership the penalty is passed down proportionately to members. OFZ property will include stock, partnership interest and business property.

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Location of Zones

- The QOZ's are census tracts designated by Governors from each state. The Governors have 90 days from the enactment of the IOA to make these designations or to request an extension to make the designations (March 21, 2018).
- These tracts must meet the definition of "low-income" as defined under the New Market Tax Credit Program in Section 45(D)(e) and the Governor may only select up to 25% of its qualified low-income census tracts as QOZ's, if the State has less than 100 qualified low-income census tracts it may select up to 25 of those as QOZ's.
- The Act does provide the Governor with the ability to designate up to 5% of the QOZ's from tracts that are not "low-income" but are contiguous to low-income areas or naturally occurring opportunity zones may be designated as long as the median incomes of the adjacent areas are not higher than 125% of the adjacent opportunity zones.
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Considerations for Designation

In addition the state is required to consider the following when nominating census tracts as opportunity zones:

- Areas which are currently the focus of mutually reinforcing state, local or private economic development initiatives to attract investment and to foster start-up business activity
- Demonstrated success in specifically targeted areas such as Promise Zones, Renewal Areas, Enterprise Zones and NMTC eligible areas
- Areas which have recently significant job loss due to closure or business migration/relocation

Once designated/certified by Treasury the opportunity zones remain fixed from the date of designation through the close of the 10th calendar year (corresponding with the timeline for the investment period).

Investment Types:

Qualified Opportunity Zone Businesses

- At this time clarity on how the investor pool will be populated, what types of investments will be allowed in the OZF's; what programs will align and close in direct combination with the IOA has not yet been issued.
- It is known that Qualified Opportunity Zone Businesses (QOZB's) must derive at least 50% of their income from Active conduct and less than 5% of the unadjusted properties is nonqualified property.
- It is anticipated by the economic development and housing industries that the IOA will act primarily as a gap filler

Excluded Businesses

- Further certain “sin businesses” do not qualify as QOZB’s. The intent of the program is to invest in businesses that will be active in the QOZs. and not merely a conduit for investment in areas outside of the QOZ’s.
  - A private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack or other facility used for gambling, or any store the principal business of which is the sale of alcoholic beverages for consumption off premises.

Compliance

- Reporting is anticipated to be required annually.
  - is anticipated that the number of OZF's; assets held in OZF's by asset class; the percentage of designated tracts funded and impact and outcomes will be tracked at minimum.
  - Impacts and outcomes may vary from those currently collected under the NMTC program with indications that in addition to job based impacts – it is likely that poverty reduction, new business start-ups and other metrics will be requested as part of the reporting.
  - It is not clear if annual audit/tax for each OZF will be required or how specifically the oversight will be provided.

NMTC Status Report and Legislative Update

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Legislative Report: NMTC Status

- Extended for 5 years at $3.5 billion a year in December, 2015.
- 2017 allocation application was awarded recently in February this year with $3.5 billion in credit being distributed
- Tax Reform retained the 2018 and 2019 Path Act Funded years of the Credit but failed to provide for further extension or to allow the credit to off-set against the Base Erosion Alternative Tax.

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NMTC Awards to Texas CDEs .

Community Development Entity	Location	Service Area	Total Awards
Corp. for Development of Community Health Centers	Austin	Statewide	$ 12,000,000
Dallas Development Fund	Dallas	Local	$ 185,000,000
Lone Star Emerging Business Fund	Houston	Statewide	$ 15,000,000
Lone Start New Markets	Austin	Statewide	$ 25,000,000
Pacesetter	Southlake	Statewide	$ 30,000,000
Pacesetter	Southlake	National	$ 60,000,000
People Fund	Austin	Statewide	$ 75,000,000
Texas Mezzanine Fund	Dallas	Statewide	$ 288,000,000
TransPecos Development Fund	San Antonio	Statewide	$ 115,000,000

In the 2017 round Texas CDEs received 3 awards totaling $105MM; TransPecos at $65 and PF at $30MM and Dallas Development Fund at $55

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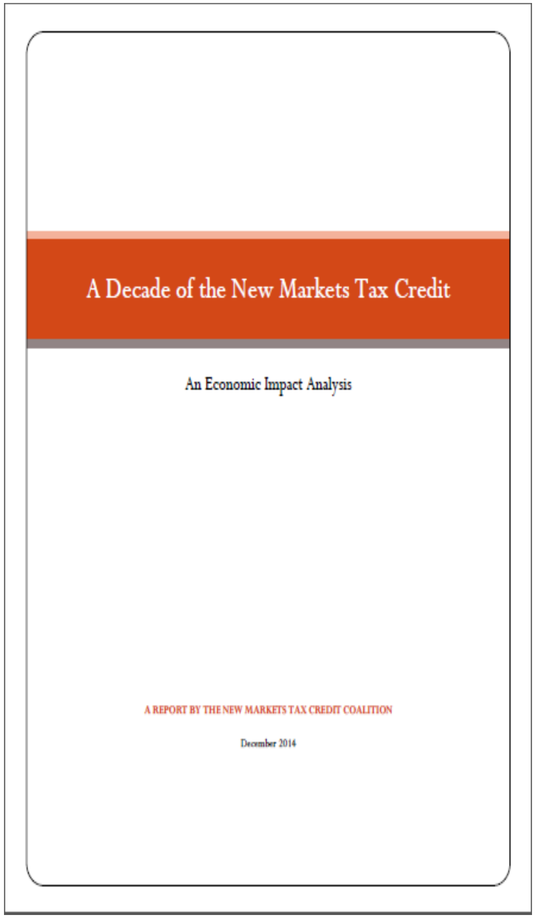
National Economic Impact

$54 billion in NMTC allocation awarded to date (including the recent $3.5 billion in awards)

National Economic Impact (2003-2015)

NMTC Coalition’s December 2017 Economic Impact Report

- $41.9 billion in NMTC financing to 4,980 projects totaling $81.7 billion in project costs
- 1,0113,837 jobs (459,254 construction jobs and 554,545 full-time equivalent jobs)
- 17MM patients served & 250,000 served in educational institutions
- 72% in severely distressed tracts
- $6.7 BB in State and Local Taxes
- $156BB in Economic Activity


A Decade of the New Markets Tax Credit

An Economic Impact Analysis

A REPORT BY THE NEW MARKETS TAX CREDIT COALITION

December 2014

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Texas

The ECONOMIC IMPACT OF THE NEW MARKETS TAX CREDIT

INVESTMENT, 2003-2015

$1.4 billion in NMTC allocation leveraged an additional $871.4 million from other sources for a total of $2.3 billion in project investments.

A total of 152 businesses and economic revitalization projects in Texas received NMTC financing.

JOB CREATION, 2003-2015

34,721 jobs

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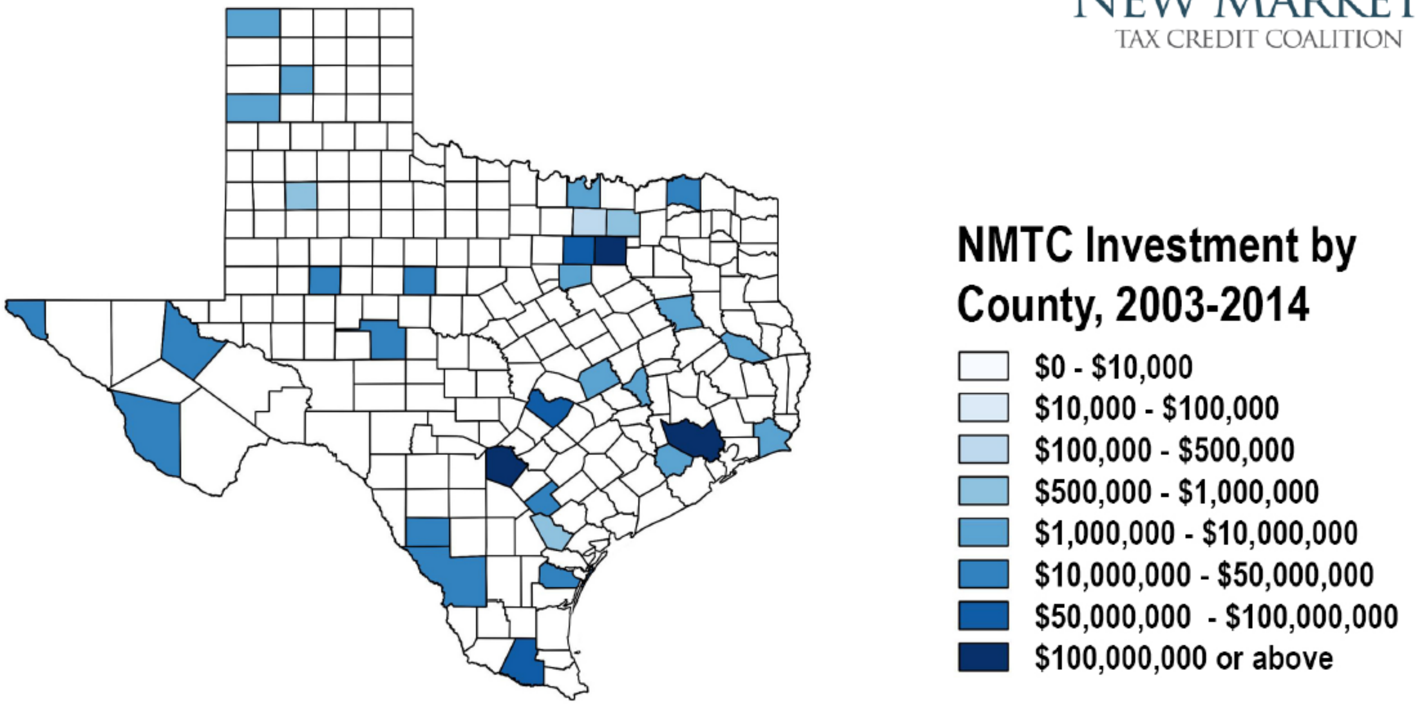
Investment in Texas by County 2003-2014



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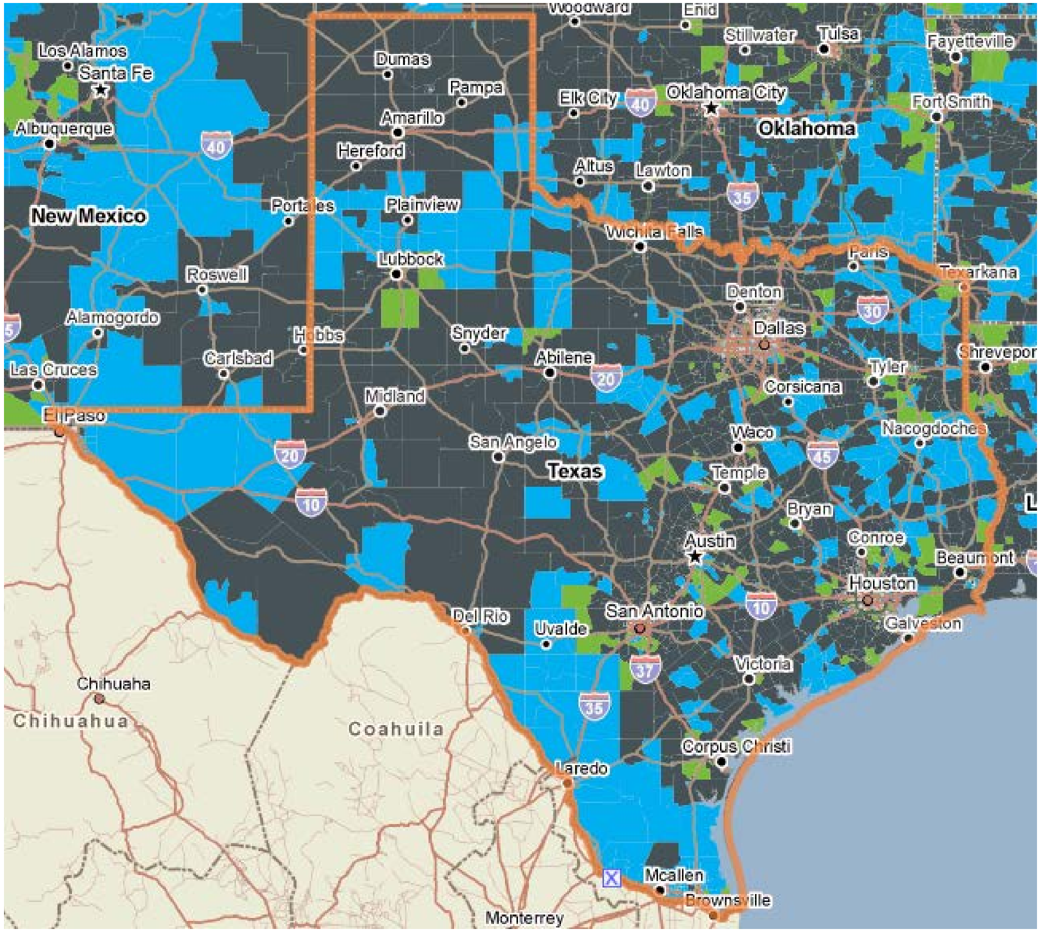
Texas



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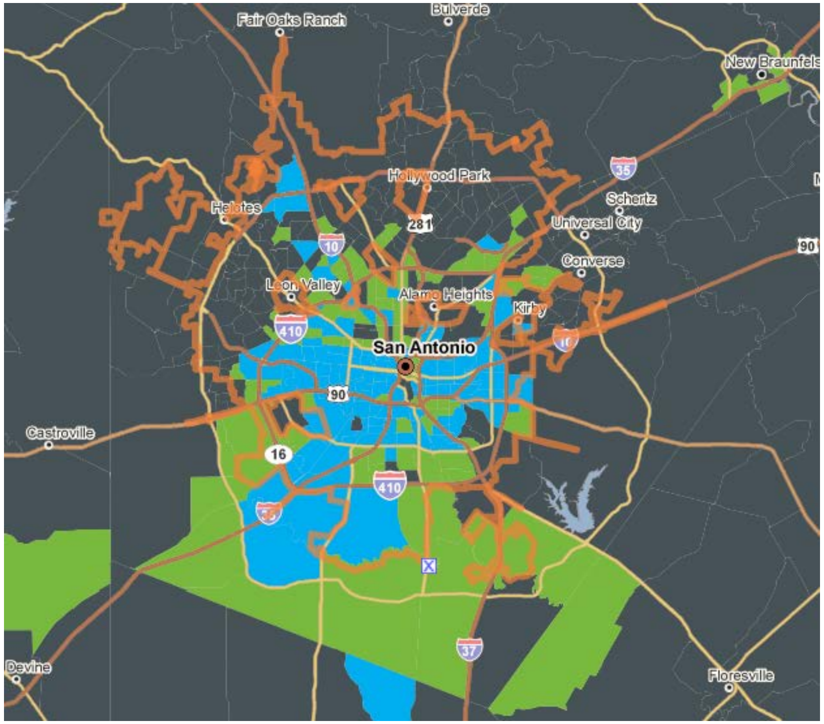
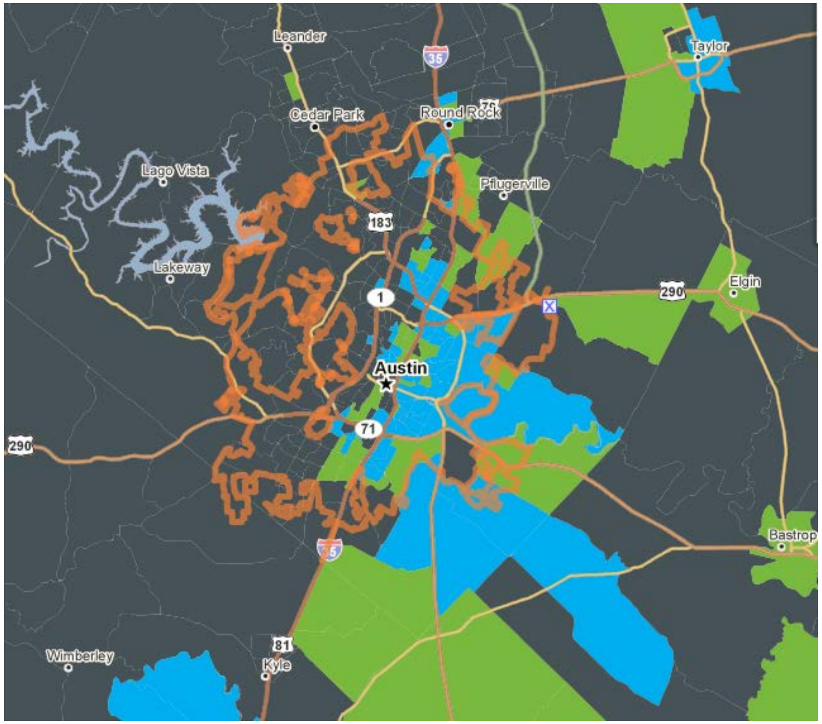
San Antonio and Austin





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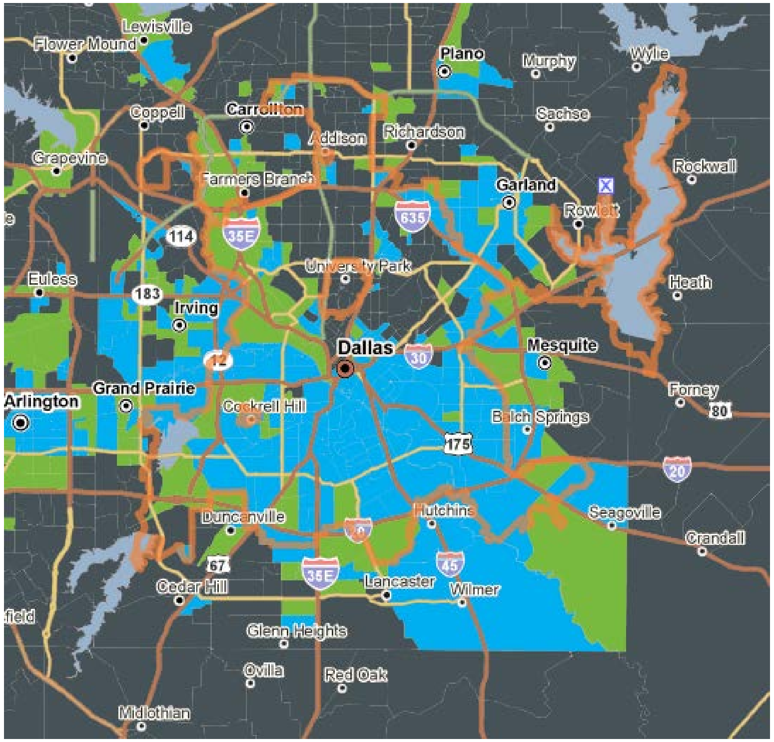
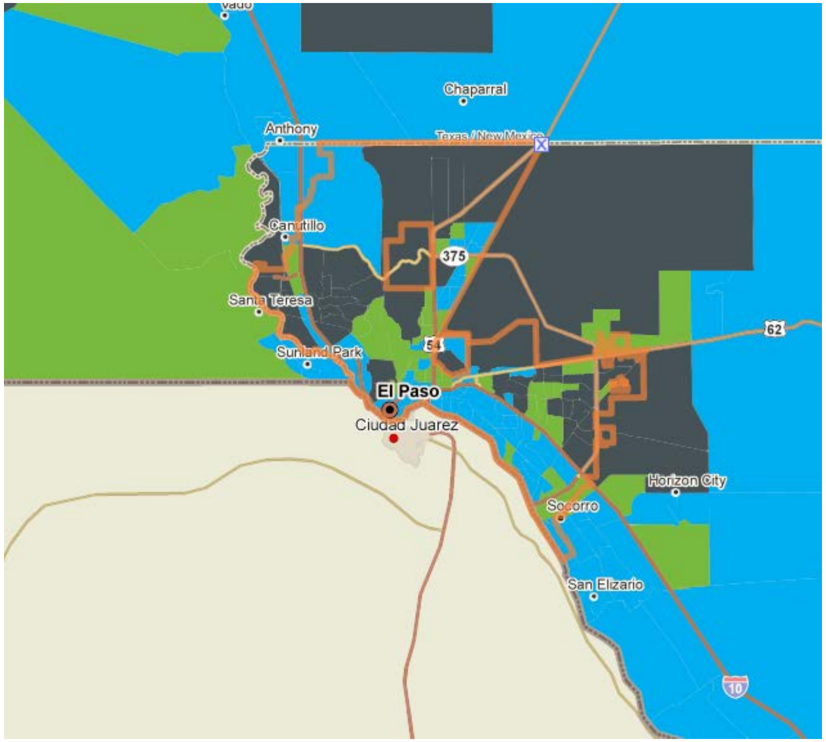
Dallas and El Paso





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More Information

- Fact Sheets, target lists, co-sponsorship lists on the NMTC Coalition website:
- nmtccoalition.org

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NMTC Basics and Investor Perspective

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- Has as its controlling entity, Baker Tilly Capital, an affiliate of Baker Tilly Virchow Krause - One of the top 12 accounting and advisory firms in the United States according to Accounting Today's 2014 list of "Top 100 Firms"
- In aggregate we are one of nation's foremost experts in NMTCs
  - We operate our own CDEs (The Valued Advisor Fund and the Business Valued Advisor Fund), which have received combined allocations totaling $288.4 million in NMTCs
  - Assisted in closing 300+ NMTC transactions to date, bringing investment value of over $15 billion to distressed communities nationwide through the deployment of over $10 billion of NMTC allocation
  - Worked with more than 90 CDEs on successfully structuring and closing transactions
  - Authored over 70 award winning allocation applications totaling roughly $5.5 billion in NMTC awards
  - Provide back office operations to roughly 14 CDEs managing over $3.0 billion in deployed NMTC
- Contact:
  - Terri Preston at tpreston@valuedadvisorfund.com or 312-307-9550

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The Valued Advisor Fund

- The Valued Advisor Fund has a principle vision of providing investments and services that provide for long-term sustainable growth opportunities in our nation’s disadvantaged communities
  - Through investment in community prioritized transactions
  - In coordination with partner CDFIs and CDEs
  - Focusing on high quality job creation and placement with low income persons and low income community residents
    - Access to fresh and affordable healthy foods
    - Access to vital community services that expand sustainable qualities of the community served

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- Utilizing
  - Direct leverage funding to the QALICB
  - Partner funding with CDFI/CDE partners
  - Loan Pool structures for fresh food and small businesses
- Impacts to date:
  - 32 QALICBs funded supporting 1,678 permanent and 2,880 construction jobs
  - 62,696 Low-income Low Access residents of food deserts served
  - 68,000 low-income persons served with education/medical access

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Overview

- What are New Markets Tax Credits?
  - Tax credit program designed to stimulate commercial investment in “low-income communities”
  - The program is administered by the US Treasury Department through a division called the CDFI Fund, in a unique “public/private partnership” with Community Development Entities (CDEs)

Overview

- What is a “low-income community”?
  - Based on census tract data – median income and/or poverty rate
  - Qualifying vs. “Higher Distress”
    - Includes unemployment, Brownfield areas, State Enterprise and other State and Local designated distress areas medically underserved areas, food deserts, Colonias and HUB Zones, among others
  - Qualifying census tracts in non-metropolitan counties automatically qualify as “higher distress”
  - Qualifying census tracts can be located using the mapping program provided on the CDFI Fund website at www.cdfifund.gov or at the following link:

http://www.bakertilly.com/insights/new-markets-tax-credit-and-low-income-housing-tax-credit-mapping-tool/

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Overview

- What is a "Community Development Entity"?
  - CDEs come in a variety of forms:
    - An affiliate of a municipality to promote economic development
    - An affiliate of a bank to help meet the bank's community reinvestment goal
    - Non-profit and for-profit entities with a mission to serve low income communities
  - CDEs have defined geographic service areas and are charged with evaluating each potential NMTC transaction for community impact
  - CDEs can be found using a search engine on the CDFI Fund website at www.cdfifund.gov

Overview

- How does the program work?
  - Through a competitive process, CDEs are delegated authority from the CDFI Fund to attract federal third party investors through utilization of the tax incentive to invest in economic development projects. The investors acquire the rights to the tax credit incentive and these proceeds are typically structured as low interest rate, convertible loans to fund into qualifying businesses or commercial real estate developments through what is most commonly referred to as a leverage structure .
  - CDEs will search for qualifying businesses and real estate developments to provide NMTC-subsidized financing, which is also a competitive process.

Overview

- How does the program work?
  - The NMTC proceeds typically fund about 20-25% of a project and is paired (or “leveraged”) with owner equity, borrowed funds, or other grant/public funds, which in total must equal or exceed the amount of NMTC allocated to a deal.

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NMTC Program Benefits - Borrower

- Economic benefit to recipient
  - Capital to fund projects, business expansion or debt refinancing
    - Tax credits are monetized to bring additional capital to the capital structure
  - Low cost of capital
  - Flexible loan terms including longer amortization and higher LTV ratios
  - Debt Conversion
    - At the end of the 7-year compliance period a significant portion of the NMTC benefit may be converted to equity or carried as debt by an affiliate of the borrower or the borrower itself, depending on the circumstances of the transaction.

NMTC Program Benefits - Community

- Community benefit
  - Create additional economic development for the local community
  - Attract and retain skilled workforce
  - Bring new goods or services to underserved communities
  - Capital investment to underserved, qualified Low-Income Communities (LIC)

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Critical distinctions

Unlike other tax credit programs, the NMTC does not "belong to" the qualified borrower. It was awarded to the CDE, to be monetized, with the proceeds invested in (or loaned to) a business that qualifies for the subsidy.

An Allocation ≠ CASH

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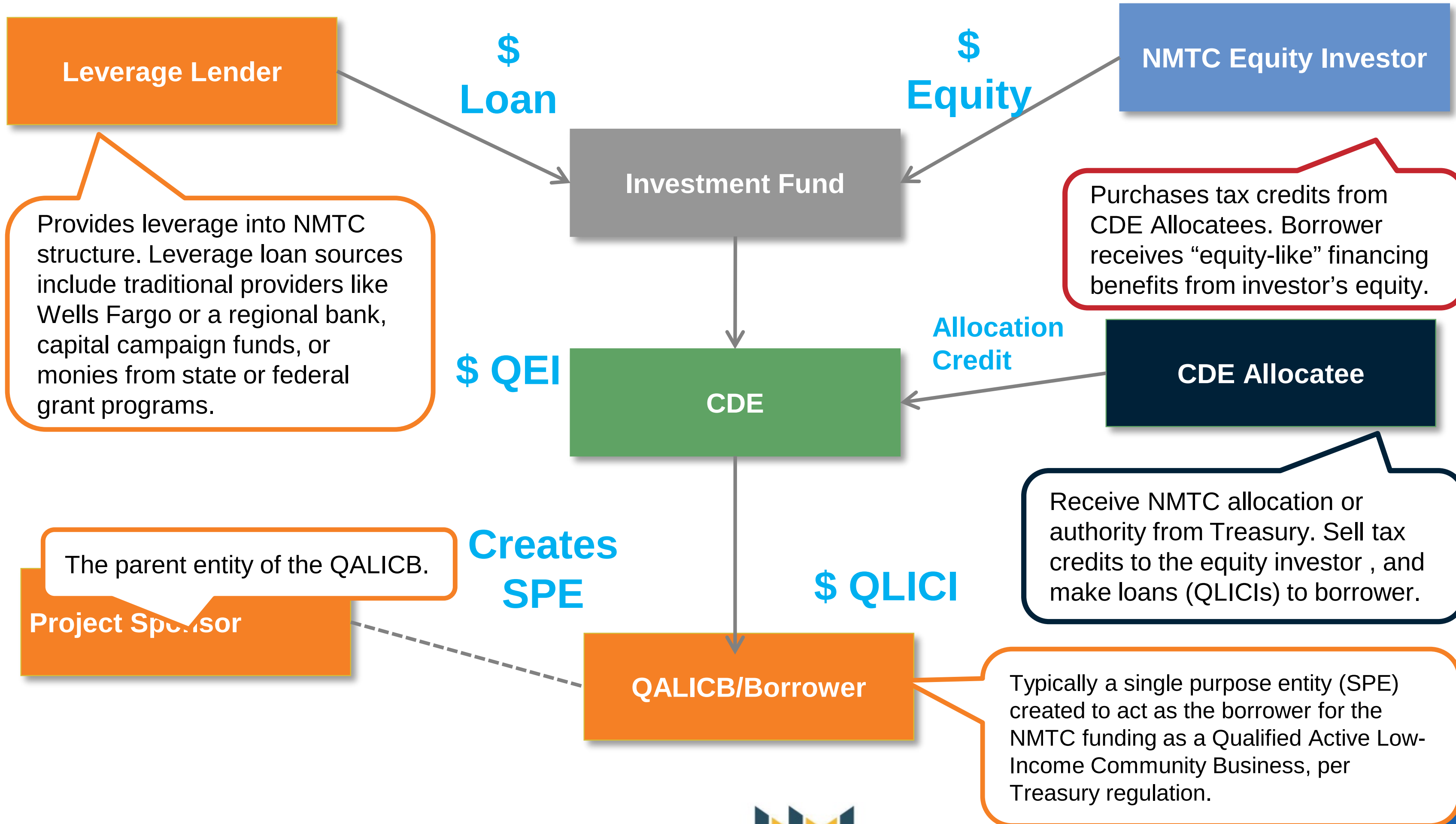
Players in a leverage model

WORKING WITH 3RD PARTY ALLOCATEES - LEVERAGE MODEL STRUCTURE



NMTC Program Benefits - CDE

- The CDE benefits primarily through meeting mission
  - CDEs have a primary mission of providing investment capital for low-income communities and are accountable to the residents of that community through a governing or advisory board
- CDEs also earn fees from obtaining and deploying the allocation and those affiliated with banks earn Community Reinvestment Act (CRA) credit
  - Repayment of spent funds to achieve the allocation
  - Overhead expense for underwriting and closing activities
  - Overhead expense for ongoing outreach activities
  - Overhead expense for loan servicing, compliance and asset management expense of the transaction and Sub-CDE requirements
  - Unwind costs

The Math

The Math (estimated)	
NMTC allocation	$10,000,000
NMTC rate	39%
Tax credits	$3,900,000
Investor monetization ($0.82 per credit example)	$3,198,000
Less estimated closing costs & fees	$800,000
Net NMTC cash to the project:	$2,398,000

NMTC Investor

- Tax credit buyer, typically a financial institution, receives the benefit of the NMTCs and community reinvestment act credit
- Credits purchased from a CDE and realized over a 7 year period
  - Years 1-3: 5%
  - Years 4-7: 6%
  - Total benefit of 39%
- Investor currently pays about $0.80-0.84 in this market for NMTCs
- May act as leverage lender
- No economic interest in the QALICB
- Main concern is to avoid recapture

Qualifying Business or Development—the "QALICB"

- Geographic restrictions
  - Business located in a Low-Income Community
  - Determined by census tract
    - Google: Baker Tilly NMTC Mapping Tool
    - Or: www.cdfifund.gov
- Technical requirements
  - Over 50% of gross income is derived from the business activity located within a Low-Income Community
  - Over 40% of the tangible property of the business is located in a Low-Income Community
  - Over 40% of the services are performed by the employees are in a Low-Income Community
  - Must not have more than 5% in either collectibles or non-qualified financial assets

Qualifying Business or Development

- Ineligible activities
  - Residential rental property
    - Mixed use is permitted so long as over 20% of the rental income is derived from commercial tenants
  - Straight acquisition or refinance of rental property – must have “substantial rehab” (25% of acquisition basis) or be owner occupied
  - Certain businesses:
    - Race tracks & gambling facilities
    - Golf courses & country clubs
    - Liquor Stores
    - Farming
    - Massage & tanning businesses
    - Undeveloped land holding

What makes a good QALICB candidate?

- Located in a "highly distressed" census tract – any one of the following:
  - Poverty > 30%
  - Median Income < 60% of statewide
  - Unemployment > 1.5 times national average
  - Non-metropolitan county
  - Two of any secondary criteria
- Community impact
  - Tangible community benefit – measured by quality job creation, providing unmet goods & services to low income communities (grocery stores), environmentally sustainable construction, etc.
  - Part of an existing plan for economic revitalization
  - "But for" test – NMTC fills a real funding gap that would otherwise not happen
- Ready to go
  - Other sources of funding are committed
  - Approvals all in place

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Valued Advisor Fund – Santana

The project includes the construction of a 212,725 square foot art denim manufacturing facility in Edinburg, Texas (“the Project”). The Project is expected to produce (cotton to yarn) at the rate of 15 million linear meters of denim per year. The Project is the first phase of a four phase plan to produce over 54 million linear meters of denim at the Edinburg site.

Total Project Costs = $27,933,334

Total VAF Allocation = $XXXX

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VAF – Santana

Distress Criteria

- Poverty Rate: 42.2%
- Median Family Income: 46.8%
- 1.48 times the national unemployment rate
- Designated Colonia and Local Development Zone

Community Alignment

The project brings jobs to the poorest county in the nation and has demonstrated support from the community based on county tax abatement; a guaranty from as a part of the financial structure; and grant dollars from the state. In addition the project is in direct alignment with the Hidalgo County economic development strategy which had a two-pronged focus on creating skilled jobs and growing cross-border trade.

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VAF – Santana

Impacts:

- **Direct, Permanent Job Creation (FTE):** 305
- **LIP Accessible Job Creation:** 259
- **Construction Job Creation (FTE):** 84
- **Economic Output Construction :** $24,260,000
- **Economic Output Operations :** $72,560,000
- **Catalytic Impact (direct/indirect future jobs):** 2,900

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Valued Advisor Fund in Rural Texas

- Hotel Saint George
  - Commercial Real Estate: Hospitality, Office, Healthcare, Retail
  - Community Alignment
    - Located in rural Southwest Texas the project supports the communities need for new quality jobs; provided infrastructure funding in the downtown to extend opportunities for business attraction; provided a commitment by the developer to participate in strategic planning to add to the affordable housing base in the community

  - 165 Construction jobs
  - 137 permanent jobs
  - Designed to LEED specifications with an emphasis on water saving features

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Thank you for your interest in serving our nation's distressed communities

Please feel free to contact:

- **tpreston@valuedadvisorfund.com**
- **paul@rapoza.org**

To distress your project, please use the following link:

http://www.bakertilly.com/insights/new-markets-tax-credit-and-low-income-housing-tax-credit-mapping-tool/

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