

THE ORANGE REPORT

YOUR SOURCE FOR KANSAS CITY COMMERCIAL PROPERTY INFORMATION

SECOND QUARTER
2018

Qualified Opportunity Zones

As real estate developers and investors, we are presented with opportunities to explore and utilize incentive programs, tax credits and investment tools which can make otherwise unviable projects a realistic option. Often, the hardest part of taking advantage of these programs is staying informed of new programs as they become available. Recently, a new tool was added to our arsenal, Qualified Opportunity Zones, designed to spur economic development in distressed communities. The following explanation comes from our long-time legal counsel and partner, Polsinelli, and explains the parameters, uses and benefits of this new program.

New Federal Program Provides Tremendous Opportunity, Tax Benefits for Real Estate Investors

Last December, Congress passed a major tax reform bill that, among many other changes, created a new program called "Opportunity Zones" to promote long-term investments in low-income areas by providing the opportunity for taxpayers to re-invest capital gains and defer and/or reduce capital gains taxes. Although we are still awaiting official guidance from Treasury and IRS on the program, early signs point to Opportunity Zones being one of the most important tax changes of the last few decades for investors and businesses. Polsinelli is part of a coalition helping to develop the administrative rules and guidance regarding these investments, and we believe strongly in the future of Opportunity Zone investing. Below is the information you need to know about this program and how it can affect real estate investment for years to come.

What, When, Where, Why, and How: Understanding Opportunity Zones

What Are Opportunity Zones? Opportunity Zones are disadvantaged areas in each state that are designated for special treatment under the new Tax Act. Investors get significant tax advantages for investing in real estate and businesses in the Opportunity Zone, with the goal of the Tax Act being to incentivize economic development in the disadvantaged areas and help create jobs there.

Where Are The Opportunity Zones? All states have designated their Opportunity Zones, and a map of the Opportunity Zones is available [here](#). Many Opportunity Zones are located in major metropolitan areas across the United States, including the Kansas City area.

Who Should Care About Opportunity Zones? In short, everyone who pays taxes. Under the new program, individuals and companies making long-term real estate and business investments in Opportunity Zones can earn capital gains on those investments and never pay taxes on that money. In addition, investors with existing taxable gains from the sale of real estate or another business can reinvest the gains in an Opportunity Zone, never pay taxes on 15% of the existing gain, and defer the remaining 85% of the gain until 2026. Importantly, there is no cap on the amount of tax savings that can be achieved through Opportunity Zones.

How Do Investments In Opportunity Zones Work? Investment in Qualified Opportunity Zones centers on long-term investment of capital gains into Qualified Opportunity Funds (a

Continued on the next page.

Sources: ¹CoStar: Total existing space, for all retail and office types, including direct and sub-lease. Change for Average Vacancy Rate represents the difference between 2017 & 2018- percentages. ²U.S. Census Bureau: Estimated monthly. ³Creighton Economic Forecasting Group. Survey ranges from 0-100 with a score of 50 considered growth neutral. Under 50 indicates a contracting economy for the next three to six months. Mid-America survey states are Kansas, Missouri, Arkansas, Iowa, Minnesota, Nebraska, North Dakota, Oklahoma and South Dakota. ⁴U.S. Bureau of Labor Statistics. Unemployment rates seasonally adjusted. ⁵Kansas City Regional Association of Realtors. Average sales price of new & existing homes. ⁶Home Builders Association of Greater Kansas City. Total units YTD as of March 2018.

Kansas City Sales & Leasing Data

KC MSA Shopping Center Retail ¹			
	Q2 2017	Q2 2018	% Chg
Total GLA (s.f.)	158,857,227	157,986,713	-0.55%
Avg. Lease Rate	\$12.42	\$13.11	5.56%
Avg. Occupancy Rate	94.0	94.4	0.4%

KC's Largest Retail Lease Signings - 2018 YTD ¹		
Submarket	Tenant	Size (sf)
95Metcalf South	Lowe's	165,000
3102 Prospect Avenue	Sunfresh	38,000
Twin Creeks Shopping Center	Ross Stores	25,243

Avg. Total MSA Vacancy and Lease Rate ¹		
Period	Vacancy Rate	Lease Rate
Q2 2018	5.6%	\$12.77
Q2 2017	6%	\$12.39
Q2 2016	5.6%	\$11.84
Q2 2015	6.8%	\$11.64

Qualified Opportunity Fund Model

- **Jan. 2, 2018** - Taxpayer enters into a sale that generates \$1M of capital
- **June 30, 2018** - Within 180 days, Taxpayer contributes entire \$1M to a Qualified Opportunity Fund, which invests in a Qualified Opportunity Fund Property.
- **June 30, 2023** - After 5 years, Taxpayer's basis in investment in Fund increases from \$0 to \$100k (10% reduction in recognizable gain)
- **June 30, 2025** - After 7 years, Taxpayer's basis in investment in QOF increases from \$100k to \$150k (15% reduction in recognizable gain)
- **Dec. 31, 2026** - \$850K of the 1M of deferred capital gains are taxed and the basis in QOF investment increases to \$1M
- **June 30, 2028** - 10 years later, Taxpayer sells investment for \$2.0MM. Basis is deemed to be Fair Market Value (i.e., no capital gains tax on the appreciation of the original investment)

National & Regional Trends

U.S. Food & Retail Sales ³		Business Conditions Index ⁴			
Period	In Millions	2018	April	May	June
Q2 2018	\$ 1,508,903	Missouri	62.4	69.6	62.6
Q2 2017	\$ 1,424,312	Kansas	56.4	68.7	62.5
Q2 2016	\$ 1,369,283	Mid-America	64.5	67.3	61.8
Q2 2015	\$ 1,335,574				

Unemployment Rate ⁵			Consumer Price Index ⁶			
June	'17	'18	2018	April	May	June
Midwest	4.2	4.0	Midwest	233.9	235.1	235.5
U.S.	4.3	4.0	U.S. City Avg	250.5	251.6	252.0

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"Fund"). A Fund is an intermediary that an investor can create and own that buys real estate or other business property in Opportunity Zones, or buys stock or partnership interests in businesses that operate on real estate in an Opportunity Zone.

Specifically, investors that would otherwise be required to recognize capitals gains on their taxes can defer payment of such taxes by investing the capital gains in a Fund within 180 days of the date such capital gain was recognized (i.e., the date of a sale or exchange). If the capital gain investment is held within a Fund for at least 5 years, the investor would reduce their tax burden by 10 percent; if the investment is held for 7 years, the burden would be reduced another 5 percent. Finally, if the investment is held within a Fund for at least 10 years, the investor would not be required to pay capital gains tax on any gain generated by its investment in a Qualified Opportunity Zone (i.e., the taxpayer would only be required to pay tax on the initial capital gains invested with the 15 percent stepped-up basis).

Can I Create An Opportunity Zone Fund? Yes. Even with the lack of existing guidance from the Treasury, there are some applications that are likely to be reasonably safe in achieving tax savings now. For example, if you are a developer about to acquire and develop real estate in an area that has just been designated as an Opportunity Zone, you should consider creating a fund now and structuring the deal through your fund in order to preserve the option of tax forgiveness. If you are a business looking to acquire and improve property, you should consider property in an Opportunity Zone, creating a Fund, and structuring the deal through the Fund. Individuals or business investors with large gains should consider investing in an Opportunity Zone Fund.

What Can I Do With Opportunity Zones While We're Awaiting Guidance? You can do a lot. You can begin identifying properties and businesses in Opportunity Zones that are good potential targets for investment. You may be able to execute options or contracts for their purchase, while you await further guidance on the Zones. If you are a developer about to develop property in a Zone, or a business about to purchase property in a Zone, you may want to create a Fund now and even raise additional capital. If you are an investor with a large capital gain in 2018, you may also want to create a Fund to preserve your deferral options. If you want to create and manage a Fund, while it is not advisable in advance of guidance to raise money and begin investing (and it is not clear yet whether funds will need to be closed or can be open-ended), you may begin talking to your investors informally to generate interest in the pending new Fund, and you may begin to prepare materials and business plans around a new proposed Fund.

For more information on Opportunity Zone investments, contact the Polsinelli QOZ team:

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About LANE4 Property Group

LANE4 provides its clients the best position from which to succeed. The firm offers an advantage in tenant representation, project leasing, property management, investment sales, receivership, project management, and development. These comprehensive services allow our clients to streamline their time and optimize their investments. From the initial market analysis through the grand opening and operation, the team at LANE4 executes each step of the process with skill and professionalism.

Our team has forged strong relationships with our constituents: tenants, investors, municipalities, architects, engineers, attorneys, contractors, and developers. This experience, dedication, and focus – combined with creativity and passion – is the LANE4 formula that maximizes our partners' results.

Kansas City Housing

Average Home Price ⁶			
County	June '17	June '18	% Chg
Cass County, MO	\$231,719	\$253,594	9%
Clay County, MO	\$212,891	\$224,199	5%
Jackson County, MO	\$193,810	\$202,199	4%
Platte County, MO	\$274,508	\$283,086	3%
Johnson County, KS	\$336,483	\$345,840	3%
Leavenworth County, KS	\$214,297	\$217,235	1%
Miami County, KS	\$205,610	\$253,807	23%
Wyandotte County, KS	\$139,267	\$153,269	10%
Kansas City Region	\$238,388	\$246,867	4%

Residential Building Permits - June YTD ⁷			
County	2017	2018	% Chg
Cass County	320	276	-14%
Clay County	664	508	-23%
Jackson County	1,140	1,477	30%
Platte County	274	289	5%
Johnson County	1,390	1,281	-8%
Leavenworth County	124	142	15%
Miami County	58	62	7%
Wyandotte County	242	107	-56%
Kansas City Region*	4,212	4,142	-2%

For. Your. Information.

Community Involvement Spotlight

KCADC :: Gwen Locher

Gwen Locher has served on the Board of Directors for the Kansas City Area Development Council since early 2015. The Kansas City Area Development Council aims to attract new companies and talents to the KC region, enhancing awareness of our metro's assets and creating positive perceptions of the bi-state community.

Giving Back

After developing a soft spot for the nearby Frank Rushton Elementary School, LANE4 decided to help the students enjoy their back to school experience by donating brand new supplies including backpacks, notebooks, pencils, crayons, scissors, glue sticks and more to the nearby school. As put by one LANE4 colleague, "Nothing beats the smell of fresh pencils on the first day of school."

While our team originally thought that we could make a small difference in the lives of some less fortunate students, we had no idea how big a difference in our own lives supporting this school would make. The gratitude and appreciation shown by the families and faculty of Frank Rushton has humbled and touched us beyond our expectations. We have come to value the school and everything they do for the community, and are proud to do what little we can to show our support.

All information furnished is from sources deemed to be reliable, but no warranty or representation is made as to the accuracy thereof and the same is subject to errors, omissions, changes, or other conditions.



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