K&L GATES

2018 INVESTMENT MANAGEMENT CONFERENCE

New York, October 30, 2018

Private Fund Opportunities: Opportunity Zone Funds, Sustainability & Impact Investment Management

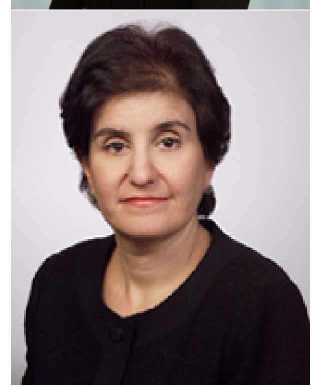
© Copyright 2018 by K&L Gates LLP. All rights reserved.

PANELISTS

Abdul-Rahman Lediju
Investment Advisor
UN Capital Development Fund
New York
+1.212.684.7400
abdul-rahman.lediju@uncdf.org

Jolyne Caruso
Chief Executive Officer
The Alberleen Group
New York
+1.212.993.7401
jolyne@alberleen.com

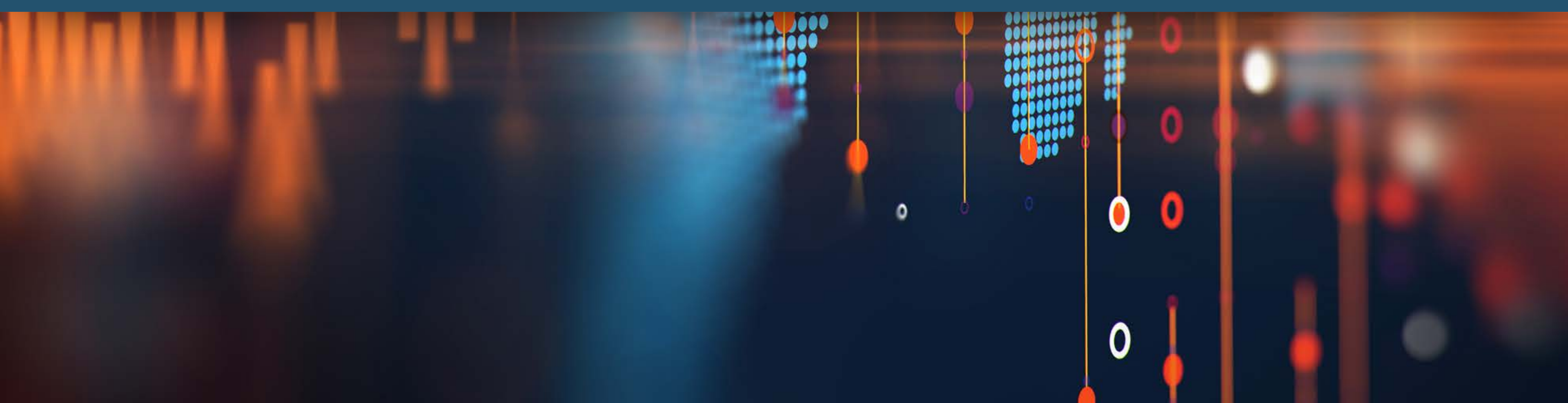
Edward Dartley
Partner
Investment Management
New York
+1.212.536.4874
ed.dartley@klgates.com



Cary J. Meer
Partner
Investment Management
New York, Washington, D.C.
+1.202.778.9107
cary.meer@klgates.com

Adam J. Tejeda
Partner
Tax
New York
+1.212.536.4888
adam.tejeda@klgates.com

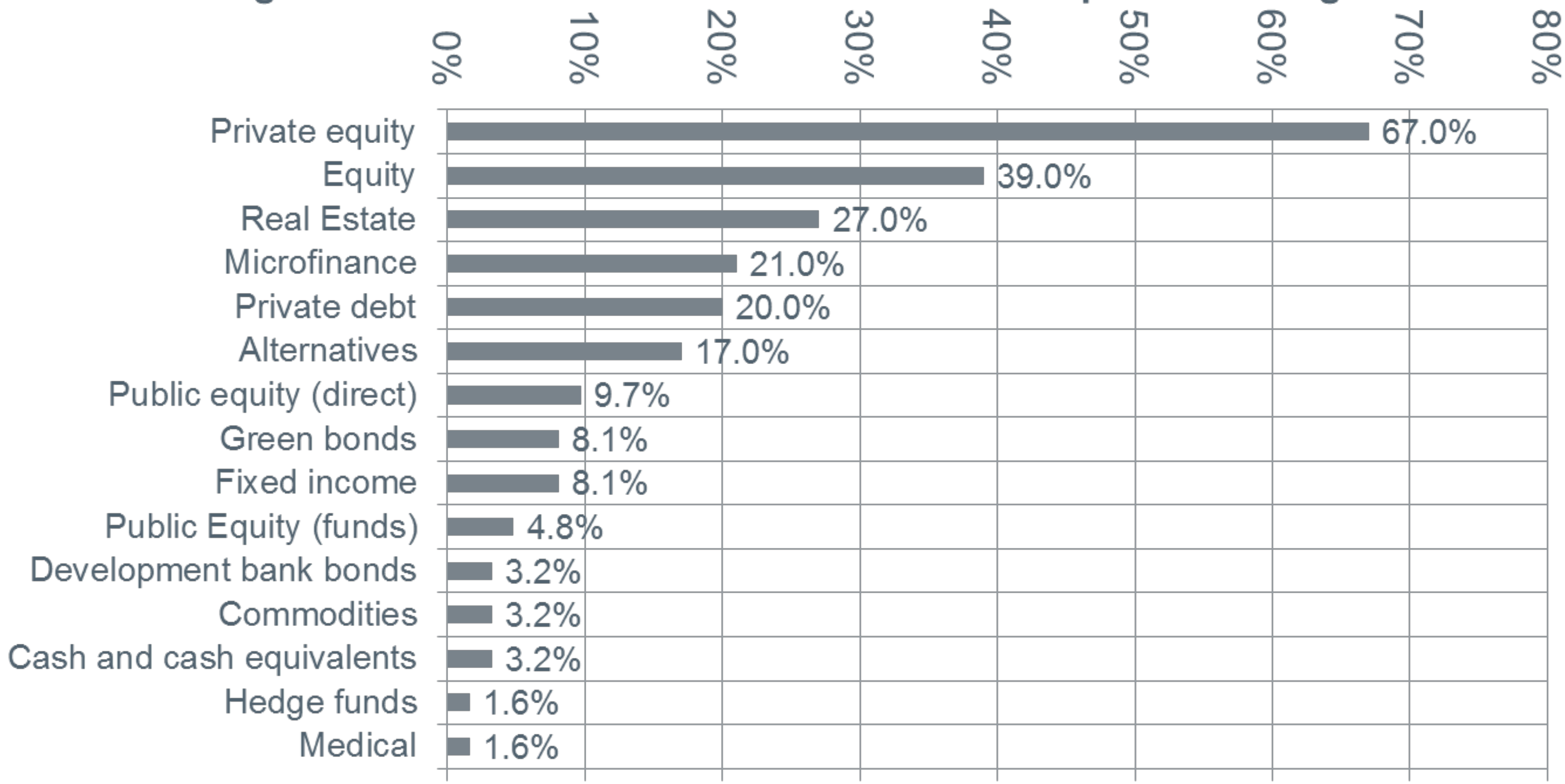
IMPACT INVESTING



"OUR DUTY IS TO LEAVE SOMETHING GOOD BEHIND"

- Impact investing is arguably one of the fastest growing areas in the average family office investment portfolio
- Global Sustainable Investing Alliance reports that $23 trillion in assets around the world have been committed to socially responsible investing strategies
- The 2018 GIIN Annual Impact Investor Survey estimates that 229 of the world's leading impact investor organizations collectively manage over USD $228 billion in impact assets across the globe

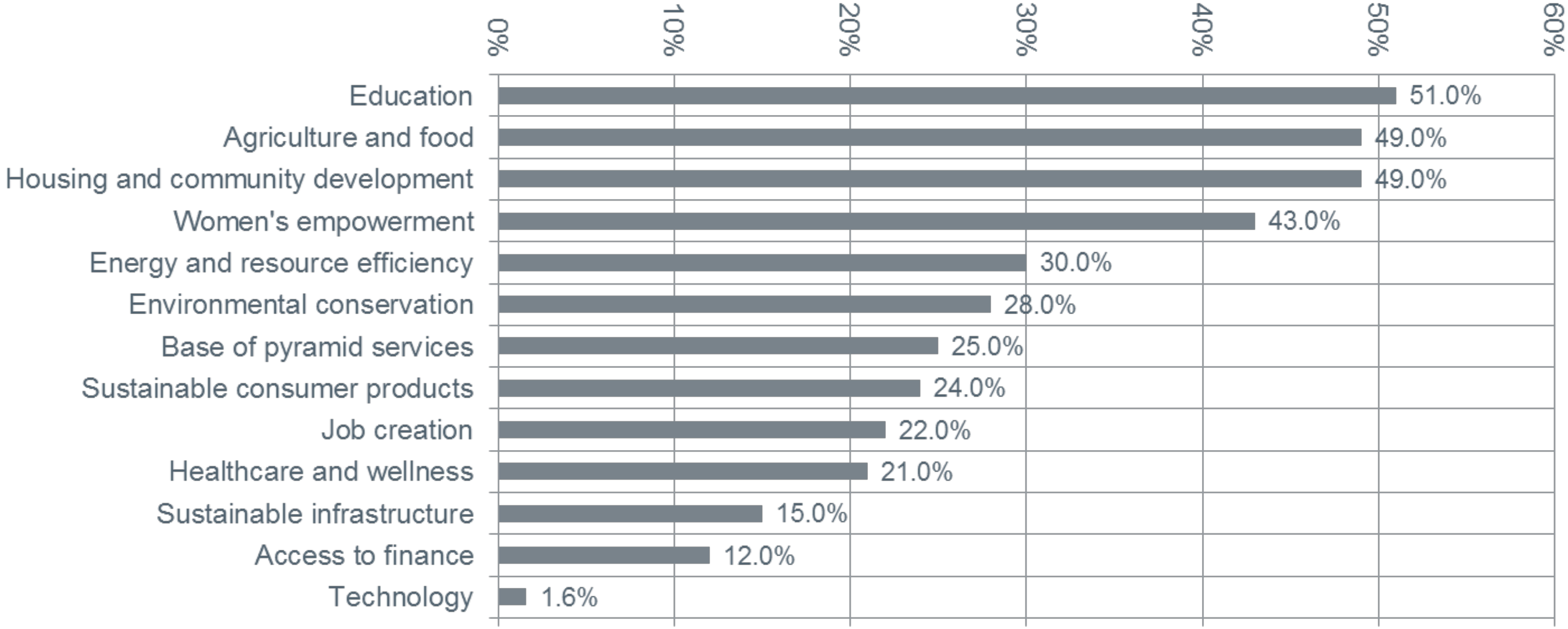
Figure 1.28 Most common asset classes for impact investing



Source: The UBS / Campden Wealth Global Family Office Report 2018
Note: Respondents were able to select multiple options

Once again this year, education remains the number one area to invest in, with over half (51%) of impact investors targeting this cause. Housing and community development became a greater focal point, as it shifted from ranking in ninth place last year to second place this year, with 49% of investors now concentrating on this area. Women's empowerment also garnered greater attention this year, moving from seventh place to fourth (or to 43%) (figure 1.29).

Figure 1.29 Most common areas of impact investments



Source: The UBS / Campden Wealth Global Family Office Report 2018
Note: Respondents were able to select multiple options

Measurement is the most common challenge

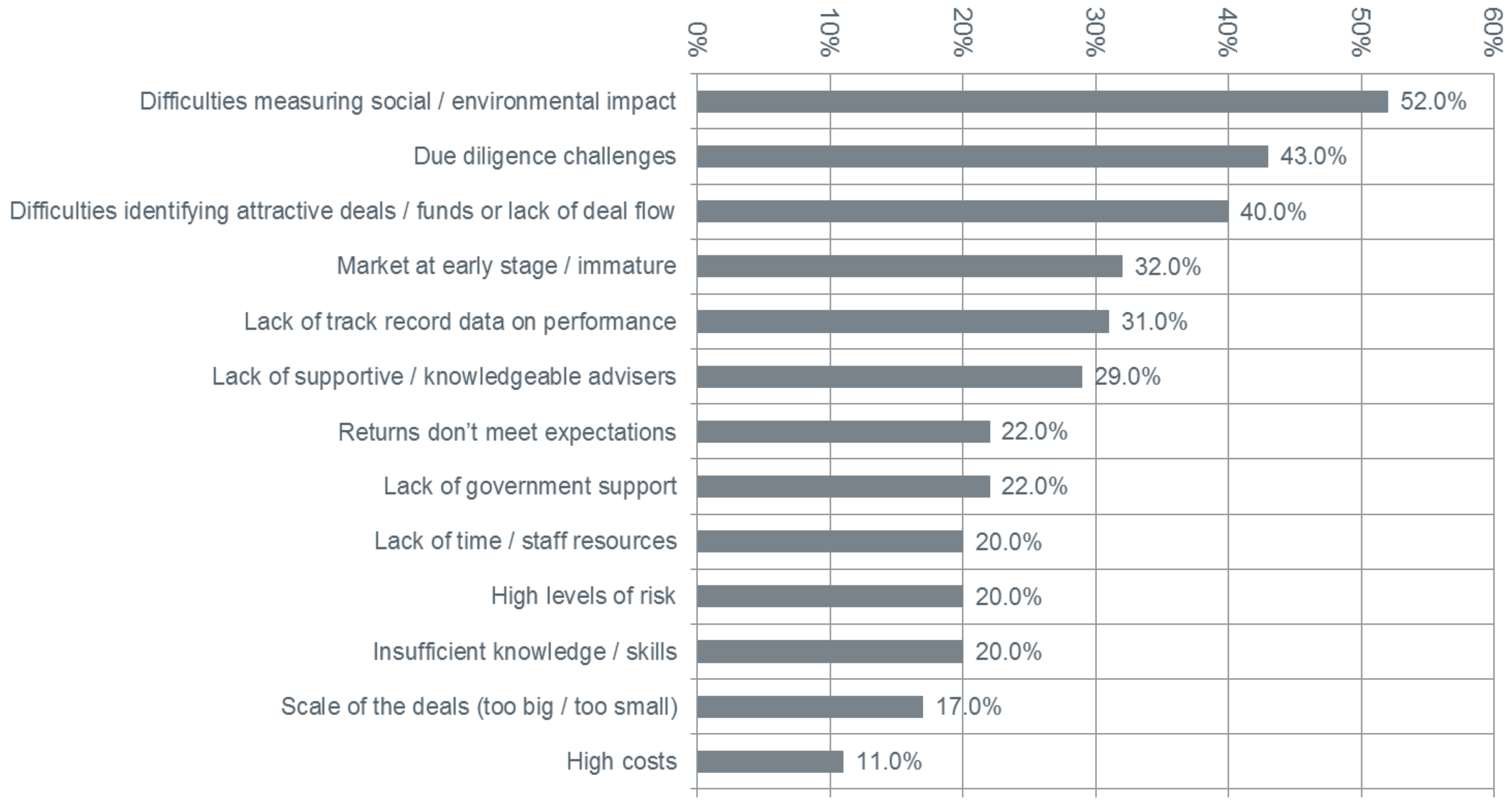
The greatest challenges for impact investing include difficulties in measuring the level of impact, as reported by over half of respondents (52%), due diligence (43%), difficulties identifying attractive deals / funds or lack of deal flow (40%) and market immaturity (32%) (figure 1.30).

In relation to supporting the measurement of impact investments, whilst it is relatively straight forward to ascertain profit margins on investment returns, calculating the extent of social or environmental impact can however be trickier.

To aid investors, the Stanford Social Innovation Review (2016) broadly outlines four measurements which are often used – ‘expected return’, ‘theory of change’, ‘mission alignment’, and ‘experimental and quasi-experimental’ methods*. While it is noted that these processes all carry their advantages and disadvantages, each reportedly accomplishes their objective to aid in the calculation of social investment returns. It may therefore be fruitful for those involved in impact investing to explore these and other such methods used, such as the Bridges Impact Management Framework, to ensure that they have a robust process for measuring success.

*McCreless, Michael. ’Toward the Efficient Impact Frontier’, Stanford Social Innovation Review. Winter 2017, Volume 15, Number 1.

Figure 1.30 Most common challenges faced in impact investing

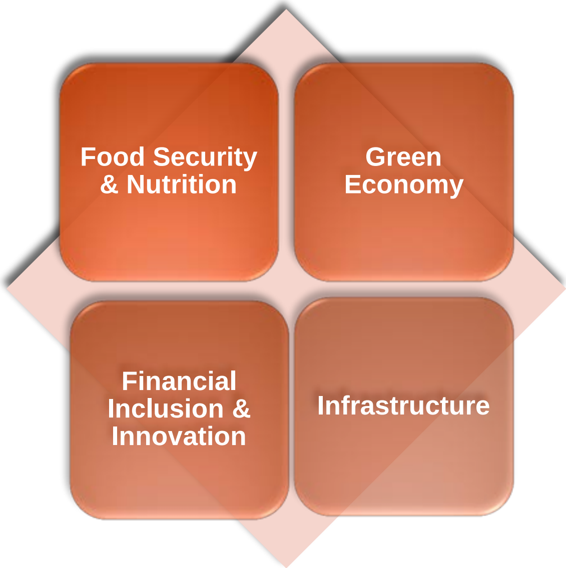


Source: The UBS / Campden Wealth Global Family Office Report 2018
Note: Respondents were able to select multiple options

UNITED NATIONS CAPITAL DEVELOPMENT FUND

UNCDF: DEVELOPMENT-FOCUSED INVESTMENTS AND TECHNICAL ADVISORY VIA MULTI-SECTOR APPROACH

- **What is UNCDF?** UNCDF is the United Nations’ capital investment organization primarily serving the world’s poorest 47 countries. With its capital mandate, it designs and implements various financial instruments to reduce poverty and support local economic development.
- UNCDF investments and TA have primarily centered around supporting financial service providers (FSPs), small and medium enterprises (SMEs) and project developers across four thematic areas:



Why these sectors? (1) Private Donor and Member State Priorities; (2) Sectors that can potentially achieve most market creation and development gains in LDCs

UNCDF GEOGRAPHIC PRESENCE

UNCDF Global Presence in 2017 | Active programs (boots on the ground)

NEW INITIATIVE: PRIVATE INVESTMENT FUND

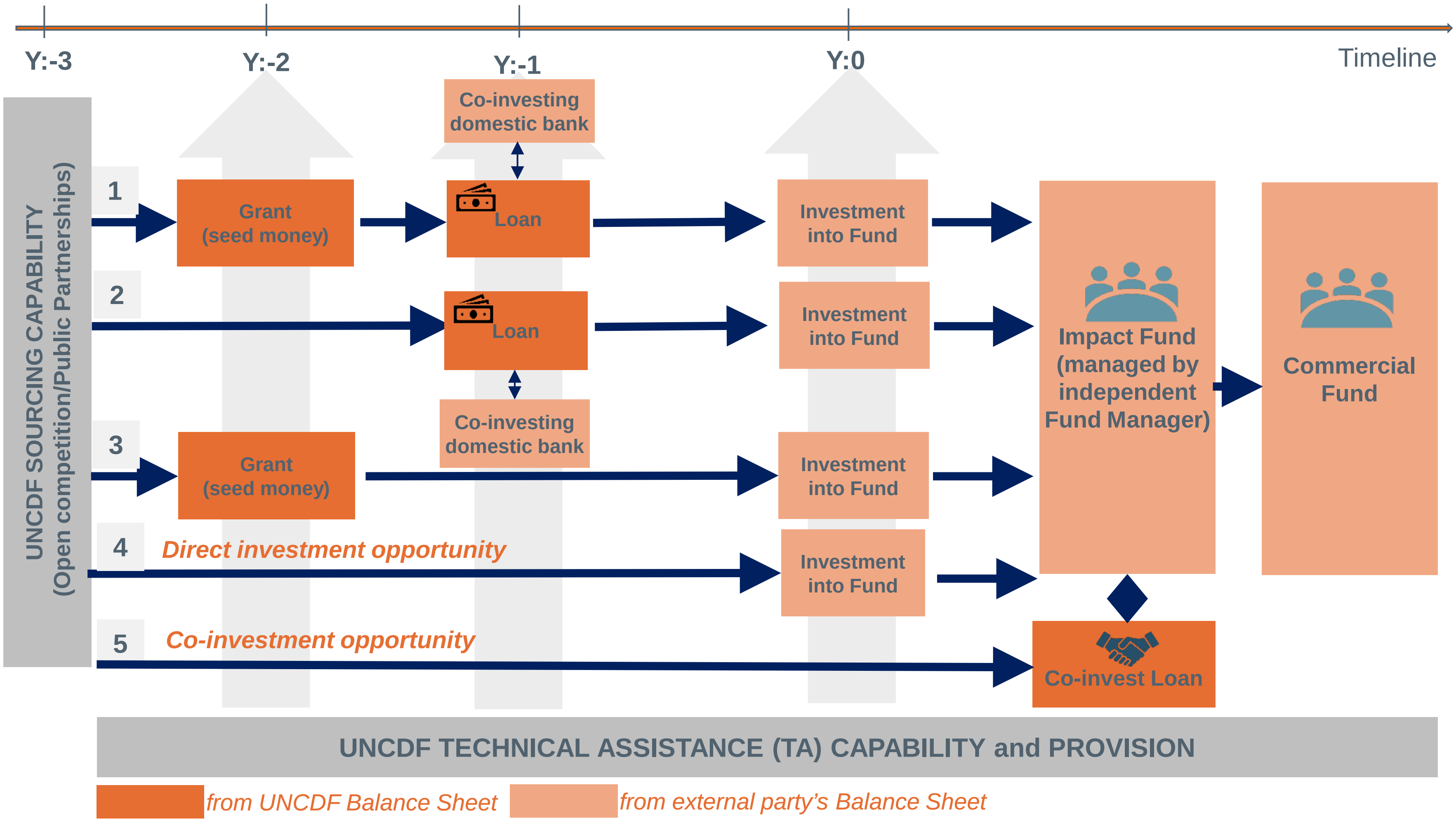
Reasons

- Increase the support to the implementation of the SDG objectives
- To better support UNCDFs pipeline of investment opportunities
- To raise additional funds – reach another set of capital provider
- To be able deploy equity into the companies
- To find a revenue model for UNCDFs sourcing and post investment support
- To be an agent to refer investment opportunities from other UN agencies to the fund

Main sourcing tool of private sector investment opportunities

- Open competitions (RFPs, EOIs, Challenge funds etc) give UNCDF
  - Sector knowledge
  - Map companies
  - Innovative and early stage company knowledge
  - Grants

UNCDF IN THE ECOSYSTEM OF PRIVATE INVESTMENTS



OPPORTUNITY ZONES

THE POLICY

- The Opportunity Zones (OZ) program was created by the Tax Cuts and Jobs Act enacted in December 2017
- The purpose of the OZ program is to help direct economic resources to low-income communities, spurring economic growth and job creation
- A descendant of Empowerment/Enterprise Zones, and New Markets Tax Credit

THE DEFINITIONS

- Opportunity Zone:
  - Low-income census tract nominated by a state's governor and certified by the Treasury Secretary as an OZ eligible to receive private investments through Qualified Opportunity Funds (QOFs)
  - Designations are finalized and expire at the close of the 10th calendar year after the designation (2028).

K&L GATES

THE DEFINITIONS

- Opportunity Fund:
  - Any investment vehicle classified as a corporation, partnership (which can include LLCs) for the purpose of investing in Opportunity Zone property
  - Funds can be a mix of capital gains, non-capital gains and borrowed funds (but only capital gains share qualifies for special tax treatment)
  - Funds self-certify to Treasury that they meet requirements to comply with the OZ program

THE DEFINITIONS

- Opportunity Zone Business:
  - Substantially all the tangible property owned or leased is OZ business property
  - At least 50% of gross income derived from active trade/business
  - Substantial amount of any intangible property is used in the active trade or business
  - Limits on financial property (deter passive investment)
  - No “sin” businesses

QUALIFYING BUSINESSES

- Capital intensive best suited
- Active, not passive
- Real estate
  - Residential
  - Commercial
- Manufacturing
- Distribution/warehouse
- Research
- Energy




THE DEFINITIONS

- Opportunity Zone Property:
  1. OZ stock in an OZ business
  2. OZ partnership interest (capital or profits) in an OZ business (includes LLCs)
  3. OZ business property
     - Tangible property used in a trade or business of the QOF
     - Acquired by purchase (capital lease) after 12/31/2017
     - Original use in the OZ begins with the QOF
     - Substantially improved property (at least match adjusted basis)
     - Substantially all the use is in an OZ

THE PLAYERS

- Investors with capital gains
- Urban and rural economic development authorities, developers, entrepreneurs, innovators, businesses and others
- Fund developers and managers
- "People *with* money, people who *need* money, and people who can *manage* money"

THE MECHANICS

CAPITAL GAINS

↓

OPPORTUNITY FUNDS

↓

OPPORTUNITY ZONE PROPERTY

Individuals and businesses invest unrecognized capital gains in Opportunity Funds

↓

Opportunity Funds hold at least 90% of assets into Opportunity Zone Property

↓

Opportunity Zone property is stock, partnership interest or Opportunity Zone business property

Tax on capital gains deferred as late as 12/31/2026

↓

10% increase in basis after investment held 5 years; 15% total increase in basis if held 7 years

↓

Gains on OF investments held at least 10 years are tax free

OTHER TERMS AND CONDITIONS

- Investors must invest in QOF within 180 days of transaction.
- Stock/partnership interest must be acquired post 12/31/2017
- Related party rules apply
- Failure of OF to meet 90% holding test results in penalties
- Basis in QOF investment increased by gain recognized on deferred capital gains (deferral less increase in basis)
- May be able to “twin” with New Markets Tax Credit

TAX ANALYSIS

- How the 5, 7 and 10 year tax benefits work

No investment in OZ

- $500,000 capital gains
  * 23.8% (20% capital gains + 3.8% NIIT)
  $119,000 tax owed 2018

5 year investment in OZ Fund

$500,000 capital gains tax deferred
* 90% (10% increase in basis)
* 23.8%
$107,100 tax owed year 5

Basis in OF is $450,000 ($500K*90%)

7 year investment in OZ Fund

$500,000 capital gains tax deferred
* 85% (15% increase in basis)
* 23.8%
$101,150 tax owed year 7

Basis in OF is $425,000 ($500K*85%)

10 year investment in OZ Fund

Basis deemed equal to fair market value of investment at time of sale or exchange; disposition is federal income tax free.

HOT OFF THE PRESS – OZ REGULATIONS!

- Substantial improvements do NOT include land costs – more projects will qualify
- 180 day investment period extended in some cases – more time for investors
- More liberal treatment of "dead" cash – will help avoid penalties
- Can hold investments until 2047 – fosters long-term commitment
- LLCs OK

OTHER QUESTIONS ABOUT OZ ANSWERED BY THE PROPOSED REGULATIONS

- Can an existing entity become a QOF?
  - Yes, an otherwise eligible entity may delay QOF status until a later date.
- What is the process for investors to disclose to the IRS that they have invested in the OZ program?
  - Investors will attach Form 8949 to their tax returns for the year in which the gain would have been recognized.
- May pass-through entities invest directly in a QOF?
  - Pass-through entities may invest directly in a QOF. Capital gains invested by a partnership are not included in the partners' distributive shares of taxable income for that taxable year.
- How much time does a QOF have to meet the 90-percent asset test after receiving capital gains from investors?
  - 18 months for cash moved down to an OZ business or 31 months provided that the cash is for the acquisition, construction or substantial improvement of tangible property and the OZ business has a plan in place to deploy the capital and uses it in a manner consistent with the plan.

K&L GATES

PENDING QUESTIONS ABOUT OZ

- Draft regulations state that further regulatory guidance is expected from Treasury in coming weeks.
- What constitutes “original use” of property?
- Do capital gains arising from transactions by the Opportunity Fund or businesses owned by the Opportunity Fund stay at the Opportunity Fund level or do they flow up to the Fund investors?
- Is a trade or business operated by the Opportunity Fund required to be a qualified Opportunity Zone Business?

WHAT YOU SHOULD DO *NOW* TO PREPARE

- Don’t wait to get started
- Understand the mechanics, the math, and the potential of the program and how it can work for you to attract investors/reduce capital costs
- Identify locations of designated OZs
- Identify suitable projects and potential investors
- Consider terms, fund structure, complementary incentives, financing, and other factors - build in resiliency for Q&A results
- Be staged to go!

STAY CONNECTED!


K&L GATES

OPPORTUNITY ZONES

The Tax Cuts and Jobs Act includes a new program called Opportunity Zones (each, an "OZ") that offers potentially significant tax incentives for investors to help to attract funding for projects and businesses in low-income areas.

Under the program, individuals and other entities can delay paying federal income tax on capital gains until as late as December 31, 2026, if those gains are invested in "Opportunity Funds" that invest at least 90% of their assets in businesses or tangible property located in low-income areas designated as OZs. Further, the gains on investments in the funds can be federal income tax-free if the investment is held for at least 10 years. The tax benefits could reduce the cost of capital for these projects, making them more viable, especially when paired with other development incentives like the New Markets Tax Credit. Congress intended that the OZ program operate with minimal restrictions in order to maximize investor participation and thus economic activity and job creation. The K&L Gates OZ team provides a full spectrum of cross-practice services to help fund sponsors, developers, innovators, and investors understand and implement this new program in order to unlock its full investment potential.

Because the OZ program was included in legislation that advanced through Congress quickly, certain details and contours of the program will have to be further defined by the U.S. Department of the Treasury ("Treasury"), the Internal Revenue Service ("IRS"), and other federal regulatory agencies. Those interested in the OZ program have raised a number of important questions that regulators have not yet answered, including whether a qualified Opportunity Fund may be organized as a limited liability company and the applicability of Securities and Exchange Commission registration requirements.

We Have the Team to Help

K&L Gates offers a full suite of practice areas necessary to understand and implement the OZ program. We understand that operating in this space requires a cross-practice, multifaceted approach to navigating the logistical, legal, and regulatory hurdles that may arise. Our multidisciplinary team of tax, tax policy, investment management, real estate, renewable energy, and tax-exempt organizations/nonprofit institutions professionals collaborate to advise and provide full-service guidance to educate clients about the program, evaluate whether the program is consistent with client goals, address legal and regulatory hurdles,

The Nuts and Bolts of the OZ Program

What are OZs?

OZs are population census tracts analogous to low-income communities qualifying for the New Markets Tax Credit. Up to 25% of qualifying tracts in a state may become qualified OZs upon nomination by state governors no later than April 20, 2018, and designation by the Secretary of the Treasury no later than June 19, 2018. Because OZs are identified at the local and not the federal level, states, possessions, and the District of Columbia have more control over the development of underserved communities.

What Is an Opportunity Fund?

A qualified Opportunity Fund is any investment vehicle organized as a corporation or a partnership for the purpose of investing in and holding at least 90% of its assets in qualified OZ property. The Opportunity Fund may invest in multiple OZs. Any business or individual with capital gains arising from the sale or exchange with an unrelated person of any business or nonbusiness property, including stock, real estate, or personal property, may invest the capital gains in the Opportunity Fund within 180 days of the transaction and enjoy tax deferral on the gains. Taxes on the capital gains are deferred until the earlier of the disposition of the investment in the Opportunity Fund or December 31, 2026, with 10% and 5% increases in basis at the five- and seven-year marks, respectively (a total of up to 15%). Gains on Opportunity Fund investments (but not the deferred capital gains) held for at least 10 years will not be subject to federal income tax.

What Is Qualified OZ Property?

Qualified OZ property includes any qualified OZ stock, any qualified OZ partnership interest, and any qualified OZ business property acquired after December 31, 2017. As discussed further below, qualified stocks and qualified partnership interests must be in corporations and partnerships that are qualified OZ businesses. Qualified OZ business property is tangible property used in a business of the qualified Opportunity Fund where the original use begins with the Opportunity Fund or the Opportunity Fund substantially improves the property.

What Is a Qualified OZ Business?

A qualified OZ business is an active trade or business, consistent with the policy of the program to stimulate economic activity and create jobs. Substantially all of the tangible property used in the business must be qualified OZ business property. At least 50% of the total gross income of the business must be from the active conduct of the business, a substantial portion of the entity's intangible property must be used in the active conduct of the business, and less than 5% of a fund's aggregate unadjusted bases in assets may be in unqualified financial property, including debt, options, and certain other financial products. Certain types of businesses, including golf courses, racetracks, gaming facilities, and establishments selling alcohol for off-premise use, do not qualify.

Stay Informed

Please visit klgates.com and search Opportunity Zones (OZs) to contact one of our leading Opportunity Zones team members and learn more about our capabilities.

Our tax, tax policy, investment management, real estate, renewable energy, and tax-exempt organizations/nonprofit institutions practices coordinate to advise and provide full-service guidance to educate clients about the OZ program.

Learn more about our practice at klgates.com.

Stay Informed

Please visit klgates.com and search Opportunity Zones (OZs) to contact one of our leading Opportunity Zones team members and learn more about our capabilities.

Next K&L Gates OZs Events:

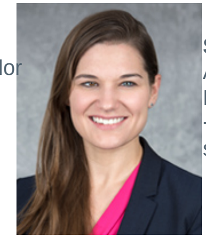
- Washington, D.C.
Tuesday November 6, 2018

Additional Opportunity Zones events are being planned around the K&L Gates platform. Please visit klgates.com and search Opportunity Zones (OZs) to connect at our next event.

K&L GATES

Our Opportunity Zones Team

Mary Burke Baker
Government Affairs Counselor | Washington, D.C.
Public Policy and Law
+1.202.778.9223
mary.baker@klgates.com



Sarah M. Beason
Associate | Charlotte
Real Estate
+1.704.331.7510
sarah.beason@klgates.com

David L. Benson
Practice Area Leader - Energy, Infrastructure and Resources | Seattle
Power
+1.206.370.7830
david.benson@klgates.com

Scott R. Bernhart
Managing Partner | Fort Worth
Investment Management, Hedge Funds and Alternative Investments
+1.817.347.5277
Scott.Bernhart@klgates.com

Todd W. Betke
Partner | Washington, D.C.
Investment Management, Hedge Funds and Alternative Investments
+1.202.778.9044
todd.betke@klgates.com

Collin W. Brown
Partner | Charlotte
Real Estate
+1.704.331.7531
collin.brown@klgates.com

Olivia S. Byrne
Partner | Washington, D.C.
Real Estate
+1.202.778.9412
Olivia.Byrne@klgates.com

Beth Clark
Of Counsel | Washington, D.C.
Investment Management, Hedge Funds and Alternative Investments
+1.202.778.9432
beth.clark@klgates.com

Robert M. Crea
Of Counsel | San Francisco
Investment Management, Hedge Funds and Alternative Investments
+1.415.882.8199
robert.crea@klgates.com

Elizabeth C. Crouse
Partner | Seattle
Tax
+1.206.370.6793
elizabeth.crouse@klgates.com

Edward Dartley
Partner | New York
Investment Management, Hedge Funds and Alternative Investments
+1.212.536.4874
ed.dartley@klgates.com

Jennifer R. Gonzalez
Partner | Washington, D.C.
Investment Management, Hedge Funds and Alternative Investments
+1.202.778.9286
jennifer.gonzalez@klgates.com

W. Ford Graham
Of Counsel | Charleston
Corporate/M&A
+1.843.579.5645
Ford.Graham@klgates.com

Michael S. Hawley
Of Counsel | Charlotte
Corporate/M&A
+1.704.331.7438
mike.hawley@klgates.com

William A. Kirk
Partner | Washington, D.C.
Public Policy and Law
+1.202.661.3814
william.kirk@klgates.com

Kevin C. Klein
Associate | Charleston
Real Estate
+1.843.579.5643
kevin.klein@klgates.com

K&L GATES

Our Opportunity Zones Team

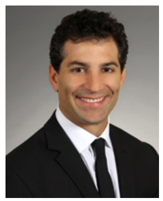
Tricia J. Lee
Of Counsel | Fort Worth
Investment Management, Hedge Funds and Alternative Investments
+1.817.347.5274
tricia.lee@klgates.com

Ashley Dantzler Wright
Partner | Charleston
Real Estate
+1.843.579.5648
Ashley.Wright@klgates.com

Robert H. McCarthy Jr.
Partner | Austin
Investment Management, Hedge Funds and Alternative Investments
+1.512.482.6836
Robert.McCarthy@klgates.com

Cary J. Meer
Partner | Washington, D.C.
Investment Management, Hedge Funds and Alternative Investments
+1.202.778.9107
cary.meer@klgates.com

Jared D. Mobley
Partner | Charlotte
Tax
+1.704.331.7535
jared.mobley@klgates.com



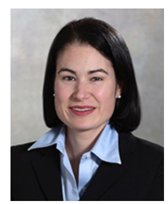
Matthew L. Ogurick
Partner | New York
Private Equity
+1.212.536.4085
matthew.ogurick@klgates.com

Cindy Ohlenforst
Partner and Chair of Women in Profession Committee | Dallas
Tax
+1.214.939.5512
Cindy.Ohlenforst@klgates.com

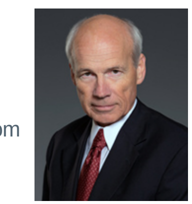
Devan R. Patrick
Associate | Charlotte
Tax
+1.704.331.7456
Devan.Patrick@klgates.com

Theodore L. Press
Of Counsel | Washington, D.C.
Tax
+1.202.778.9025
ted.press@klgates.com

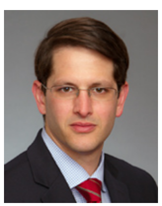
Charles H. Purcell
Partner | Seattle
Tax
+1.206.370.8369
charles.purcell@klgates.com



Emily B. Reynolds
Partner | Charlotte
Real Estate
+1.704.331.7410
Emily.Reynolds@klgates.com



Mark S. Sharpe
Partner | Charleston
Real Estate
+1.843.579.5647
Mark.Sharpe@klgates.com



Adam J. Tejeda
Partner | New York
Tax
+1.212.536.4888
adam.tejeda@klgates.com

Jason P. Walton
Partner | Charleston
Tax
+1.843.579.5624
jason.walton@klgates.com

Robert B. Womble
Partner | Raleigh
Tax
+1.919.743.7309
robert.womble@klgates.com

K&L GATES