City of Adrian Opportunity Zone Development

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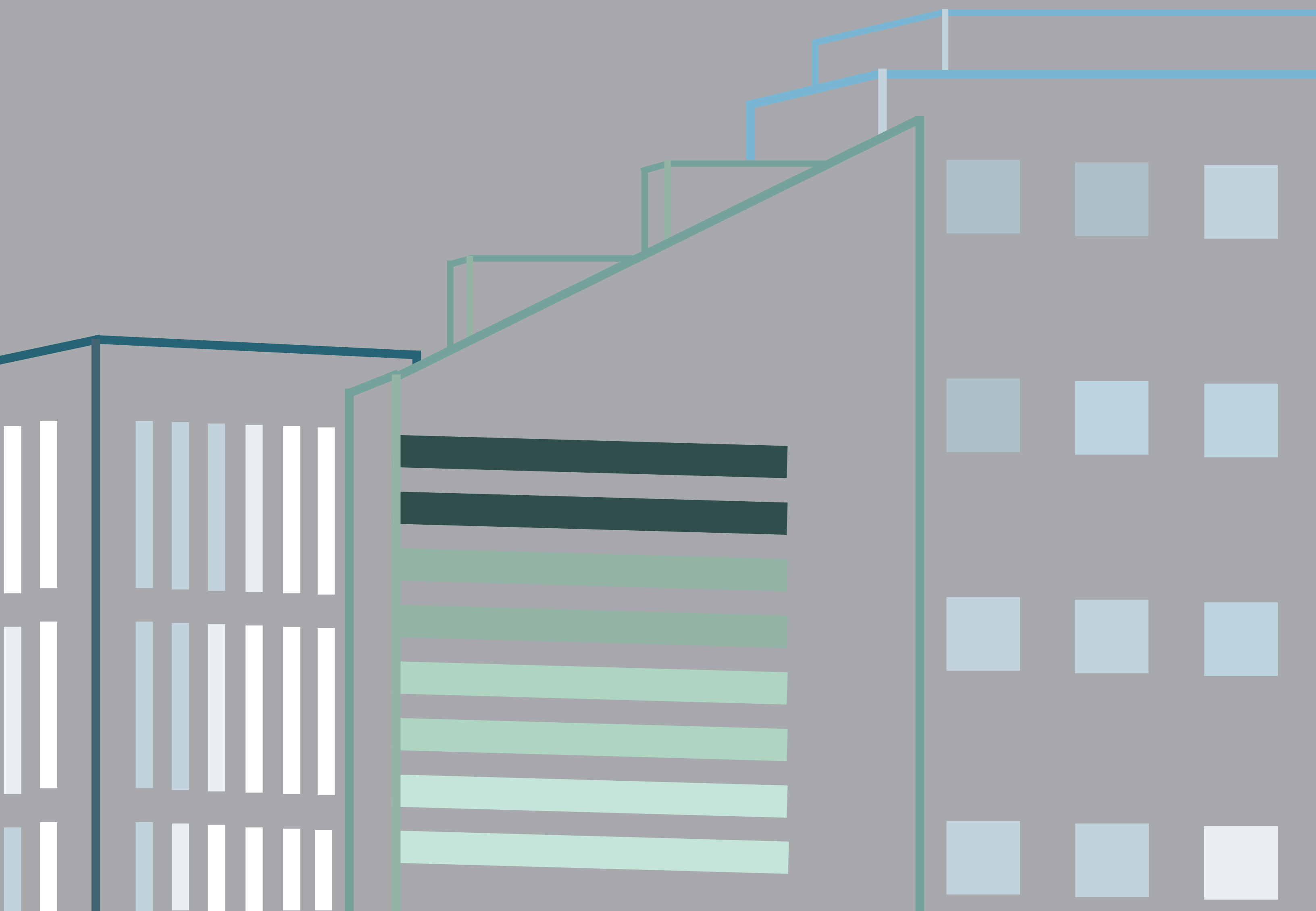

Michigan State University
EDA University Center for
Regional Economic Innovation

2019 Co-Learning Plan Series

MICHIGAN STATE UNIVERSITY
Center for Community
and Economic Development
University Center for Regional Economic Innovation

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U.S. ECONOMIC DEVELOPMENT ADMINISTRATION

Bring Opportunity Zones and Local Investors Together in Your Community:

City of Adrian Co-Learning Plan

EDA University Center for Regional Economic Innovation
Center for Community and Economic Development
Michigan State University

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INTRODUCTION

The Opportunity Zone (OZ) legislation established by Congress in the Tax Cuts and Jobs Act of 2017 encourages long-term investments in low-income urban and rural communities nationally. This legislation has influenced economic development as the architects of the law provided a capital gains incentive designed to entice the wealthy to invest in financially distressed and under-invested areas. A significant element in the work at the City of Adrian is to ensure local, non-accredited investment can also be included in the capital stack.

Being so new, much is yet unknown with regard to low population density and small settlement census tract areas. It is the aim of this Co-Learning Plan (CLP) to help small towns and rural areas navigate how to use this Act and supporting resources to their benefit based on the experience of a small city within Michigan, the City of Adrian, and its opportunity zone and fund development.

Additionally, within this CLP the City of Adrian and partners will provide a way for communities to use community capital strategies as part of social and/or environmental justice solutions and discussing the importance of *who* is allowed to invest. In other words, the impact of community capital is about much more than just the money. Opportunity zones and "fund work" have the potential to harness investment power for collective impact.

Using community capital strategies, this CLP looks at investment offerings that are open to both high net worth individuals, institutions, and community (non-accredited or retail) investors. The current model for capital raising, even in many social and environmental justice enterprises, is to reach out to the wealthiest accredited investors within national networks when capital is required. That model is not wrong, but choosing *only* that approach means that enterprises are missing the opportunity to engage all supporters, regardless of their wealth.

Community capital strategies democratize our economy in a variety of ways. Community capital allows everyone to invest in alignment with their values. Currently, non-accredited or community investors are not permitted to invest in most private enterprises, including social and environmental impact companies. Most people are limited to putting investment dollars into Wall Street offerings: publicly traded stocks, mutual funds, and money market accounts. Offerings that are open to communities allow those members to invest in businesses, cooperatives, nonprofits or other enterprises who are committed to good environmental practices, and/or are supporting social justice missions.

It is the practice of impact organizations to reach out to communities to help shape their missions and the foci of their work. Therefore, the question must be asked: why are those community members left out of the investment opportunity when it is time to implement the ideas that a community helped define? When a broader segment of a community is invited to invest, those investors will be more diverse than most existing high net worth investors and funding institutions. Entrepreneurs who receive funding will likely reflect the values of the community that is investing in them. Community members are also more likely to choose specific entrepreneurial ventures that speak their language (literally and figuratively), echo their values, and are committed to impacts that solve problems in their community. This creates a cycle of local investment, impact, wealth creation, and community reinvestment. The process is one of regional fertilization and does not extract resources out of the local economy.

OPPORTUNITY ZONES AND IMPACT INVESTING

Opportunity Zones are first and foremost an incentive and investment tool and secondly a possible redevelopment and social equity catalyst utilizing empowered partnerships. Hotly debated as both a solution and a giveaway, much still remains unclear about zones. In an attempt to blaze an empowered path, the City of Adrian is sharing its journey to create an opportunity fund, build a zone prospectus and lead its use for socially just outcomes as a small city surrounded by a rural region.

BACKGROUND

Opportunity zones (OZ) were established by Congress in the Tax Cuts and Jobs Act of 2017 with the purpose of incentivizing long-term investments in low-income urban and rural communities nationally. Through this policy, a tax break is offered to those investors who wish to re-invest their unrealized capital gains into opportunity funds (OF). The idea driving this development was originally introduced in a 2015 publication by the Economic Innovation Group, *Unlocking Private Capital to Facilitate Economic Growth in Distressed Areas*, meant to address persistent poverty and uneven recovery written by Jared Bernstein of the Center on Budget and Policy Priorities and Kevin A. Hassett of the American Enterprise Institute.

Recently, investment firms have increased their focus on community investment funds as a critical tool to move the needle forward to a more inclusive and equitable society. There was a refrain recently overheard at a partners' gathering of community organizers that sums up this idea: "Nothing about us, without us, is for us." While these words echo a centuries-old Latin slogan ("*nihil de nobis, sine nobis*"), they also reflect a profound truth as relevant today as it has ever been. The meaning can be interpreted as: "Don't try to solve our community's problems for us. We understand our problems and their solutions better than anyone. We simply lack the resources and tools to solve our problems. You can help us by providing those resources and tools." The distinction is subtle, yet critically important. It's about empowerment.

In the world of impact investing, wealthy (yet conscientious) investors and institutions seek to invest in ways that help to improve the plight of others, typically while still making a good return on their investment. While this type of impact investment is certainly a good thing, the "impact" too often addresses the *effects* of underlying systemic problems without addressing the actual root causation in a meaningful way. By continuing to concentrate wealth (and reinforce class distinctions between the haves and the have-nots), this type of impact investing could even exacerbate the very problems it seeks to remedy.

Opportunity Zones are low-income community census tracts established by the New Markets Tax Credit program. Each state's governor and territory had through March 21, 2018 to send their identified tracts to the U.S. Treasury. Up to 25% of eligible tracts could be nominated. Of those, 5% could be nominated that were contiguous. With guidance from the Internal Revenue Service and Community Development Financial Investment Fund, participating states have now designated their OZs as of June 2018.

Across the nation, more than 42,000 tracts were eligible with slightly less than one-quarter being designated. Of these, more than 90% were low-income communities. According to the Census Data and Economic Innovation Group analysis (2019), the average Zone has a median household income of $33,345, an unemployment rate of 13.41% and a poverty rate at 31.75%. Of these, three-quarters are in metropolitan areas. For the other 25%, such as the City of Adrian, Michigan, designated tracts are within small towns and rural areas.

Within the Zone program, three types of incentives are available for investing in low-income communities via qualified OFs. The first is known as temporary deferral, a deferred gain that must be recognized on the earlier of the date on which the OZ investment is disposed of, or December 31, 2026. The second is a step-up in basis for capital gains to be reinvested in an OF. The basis of the investment is increased by 10% if the investment is held in an OF by the taxpayer for at least five years. It's increased by 15% (at a maximum) if held for at least seven years prior to December 31, 2026. Thirdly, a permanent exclusion from taxable income of capital gains is possible for the sale or exchange of an investment in an OF if the investment is held for at least 10 years. The exclusion only applies to gains accrued after an investment in the fund.

The effectiveness of each OZ is tied to attracting capital to areas of need. However, this can vary greatly between urban and rural areas and reflects socio-economic, industry and cultural differences. The key may lie in the marketing of small cities and rural areas as attractive places to live and work for younger people. So, one of many questions to be asked is: what is it that draws an investor (from outside or locally) to put their money in small towns, for example? And next, how can locals be sure their community benefits from it in addition to the investor?

MICHIGAN'S OPPORTUNITY ZONES

In Michigan, there are 1,152 eligible census tracts with 288 of these allowed to qualify per program rules according to the Michigan State Housing and Development Authority. Funds could be used within these tracts to create new business, new commercial or residential real estate or infrastructure. This incentive program can even be combined with other incentives like the New Market Tax Credits and Low-Income Housing Tax Credit and Historic Rehabilitation Tax Credit, adding a valuable tool for economic and community development. Local governments may consider strategically aligning resources, or a new workforce innovation program for example, to further leverage support.

The Opportunity Zone incentive was designed to provide communities a chance to pursue the best mix of investments in new and expanding business, infrastructure, and energy projects, commercial real estate, affordable housing, and more. While this is a clear win for investors able to defer and reduce capital gains within urban areas there is somewhat of a unique challenge for smaller Zones due to a lack of private enterprise, banks, development groups, community development financial institutions, and regional economic developers or investor consortiums. A new model must be developed as historical efforts, such as the New Market Tax Credit, have in many cases focused on an overly top-down approach without local ownership of outcomes.

The City of Adrian

The City of Adrian understands that the only way a designated OZ will realize investment is if there are qualified projects. Therefore, the community had to create a strategy for identifying potential investments and investment areas making them into opportunities for investors. As there is currently no way for communities to report these activities to the state, or guidelines on how to coordinate this, the City of Adrian has noted a *learning opportunity*.

In many ways, small towns, and rural areas have limited, if any, resources to create economic opportunity within their Zones that is not already taking place – regardless of OZ funding. The largest benefit of this program may be to investors already having assets in the community and who are already investing. Additionally, areas extremely impoverished where low-income housing tax credit projects are being built will benefit. The City of Adrian fits both of these categories as it already has local investment from residents, and a great need for low-income and missing middle housing. Several of its redevelopment sites have been identified and assessments are underway for developer attraction.

A city of some 20,000+ residents, Adrian is making slow progress in its effort to make a comeback from the Great Recession. Therefore, its partners as much as possible seek to nurture current assets and develop new ones. In this vein, through a Governor's initiative of 2017, it joined the Project Rising Tide community development program aimed at providing at-risk communities with tools they can use to strengthen and accelerate their local economy. The Rising Tide program supports plans and projects that could result in vibrant, thriving communities that attract investment and talent. Central to the program is the creation of a sustainable path leading toward economic stability and growth. The Michigan Economic Development Corporation, Talent Investment Agency, and Michigan State Housing Development Authority–collectively, the Talent and Economic Development (TED) team–have committed assets to engaging specific communities across the state in order to empower them to shape their future and maximize economic potential.

For each of two "rounds" of this program to date, one community was selected in each of the ten Michigan Prosperity Regions using the following data, cross-matched by population: poverty, unemployment, labor participation, renter occupancy, vacancy, and households receiving assistance. Managed by the Community Economic Development Association of Michigan (CEDAM), the City of Adrian was selected in late 2018 to focus on two site redevelopments, creation of an opportunity zone prospectus, an autonomous vehicle pilot and a new pedestrian bridge connecting private industry to a college campus. Through this programming the city was also able to apply for Michigan State University Regional Economic Development funds and technical assistance for the development of this Co-Learning Plan.

IMPACT INVESTMENT

Even though mechanisms to raise community capital are available, they are not commonly used. What is standing in the way of significantly moving the needle toward a more equitable and democratic economy? In short, the US lacks a culture of community capital. Most investors (both wealthy and non-wealthy) are unfamiliar with Direct Public Offerings (DPOs) and other legal strategies of community capital. Unfortunately, so are most investment professionals and lawyers. This unfamiliarity breeds skepticism which is likely the biggest barrier to widespread adoption of the strategies of community capital. Making matters worse, the non-wealthy, those who don't meet the Securities and Exchange Commission's definition of "accredited investor," have been trained for decades to see themselves as unqualified to invest.

This is where visionaries, philanthropists, and impact investors can make a big difference. To change the culture so that community capital is as ubiquitous as corner convenience stores, visionaries and thought leaders must help educate their communities about the game-changing potential of community capital. Additionally, philanthropists may donate to nonprofit organizations seeking to promote community capital in their local areas. Any investor interested in the structures of community capital (for example, as founders of community investment funds), provide credibility, strength and momentum helping spur this economic revolution. And, of course, innovative leaders are necessary to make it happen.

A culture shift is possible and can build an economy in which every community is served by a constellation of community investment funds of various types, along with DPOs by local ventures, which together contribute to a vibrant community capital marketplace in which all may participate on a level playing field for a more equitable, prosperous, and empowered community. In other words, this is the ultimate impact investment.

However, there are gaps in the legal landscape for community investment funds – a landscape dominated by the Investment Company Act of 1940. This law imposes a heavy regulatory burden on any investment fund that doesn't qualify for an exemption, a burden so heavy that it is not financially feasible for a community-scale fund. Since 2015, a bipartisan coalition of lawmakers has advocated for tax incentives for those who invest in low-income communities, recognizing that the benefits from the economic recovery have largely bypassed those communities. Their efforts were rewarded when their proposed opportunity zone program was included as Subchapter Z of the 2017 tax law overhaul that was passed in December. While Subchapter Z wasn't specifically tailored to community capital, it offers tax incentives that will apply to some kinds of community investment funds. Therefore, applied in the correct fashion and dependent on fund type, communities can work with the 1940 Act to meet its criteria.

While the law provides tax incentives to invest in funds that serve low-income communities, it does not provide any new strategies under the securities laws. It is probably inevitable that the vast majority of qualified opportunity funds will be open to accredited investors only, like nearly all private funds. However, there are at least three strategies that allow a qualified opportunity fund to be open to its entire community, including those non-accredited investors. These are discussed below. It is important to first identify what a qualified OF is as a partnership or corporation with at least 90% of its assets consisting of qualified opportunity zone property (and acquired after 12/31/2017), which can include:

- Equity interests in a corporation or partnership that is an opportunity zone business (and issued directly by the corporation or partnership, not acquired in secondary sales), or;
- Tangible property (real or personal) located in the opportunity zone that is either first used by the fund or is substantially improved by the fund (the latter meaning that additions to its basis exceed its original basis).
- A business is an opportunity zone business if:
    - At least 70% of its tangible property is located in the opportunity zone;
    - At least 50% of its gross income is derived from operations in the opportunity zone;
    - A substantial portion of its intangible property is used in its operations in the opportunity zone; and
    - Securities comprise less than 5% of its total assets by tax basis.
    - It is not a "sin" business, like a gambling facility, massage parlor, or liquor store.

HOW TO STRUCTURE YOUR FUND TO AVOID COSTS AND TIME DRAINS

At heart, OFs are pooled investment vehicles, similar to mutual funds, and therefore must be in compliance with the 1940 Investment Company Act. The regulations of the 1940 Act are onerous and may be very expensive to manage a fund on a community scale. However, the Investment Company Act has several exemptions that can work for community investment funds, including OZ funds. Communities developing their OFs must also be aware of OZ tax rules, and securities laws that regulate the actual process of raising investment. Therefore, they'll need to find a strategy that satisfies both the OZ tax rules and the Investment Company Act. Below, four options satisfying these laws while also meeting the needs of communities are outlined. They include a Community Real Estate Fund, a Hybrid Real Estate/Business Fund, a Holding Company, or a Private Fund.

Community Real Estate Fund

Real estate investments fit all the rules, both Regulation Crowdfunding or a DPO could be used to raise capital for a real estate fund. With a DPO a community might focus its marketing efforts such that residents could be asked to invest. The entity might be an LLC, partnership or REIT (Real Estate Investment Trust). Each of these is effectively a tax pass-through entity, so it will not pay tax on gains at the fund level.

Additionally, a Community Real Estate Fund could partner with a charitable community land trust to lower net costs of acquisition and preserve land for certain uses. This might be urban revitalization, workforce or affordable housing, agricultural land preservation or historic preservation. In this way the land trust would acquire an easement on a property and by acquiring part of the rights in the property that would lower the net costs to the fund of buying the property. As long as it's operated in a way that's consistent with the easement, the OF could continue to operate or lease it out within the zone to help make it more cost-effective and serve the community.

Hybrid Real Estate/Business Fund

This is a slightly different, yet related, strategy to the above. There are two ways a fund holding real estate can reduce the compliance burdens of the 1940 Act. One is an exemption for a fund whose assets are 90% in real estate. The second is to structure the fund so that it does not meet the definition of an "investment fund." It is this latter approach that opens the door to a hybrid fund that consists of both real estate and equity in businesses.

A hybrid fund has two key requirements: First, securities investments may not be the primary business of the fund. If it is primarily in the real estate business, or primarily in some combination of real estate and other non-securities lines of business, it should meet this requirement. And those other lines of business may be conducted through wholly- or majority -owned subsidiaries. Second, investment securities may not comprise more than 40% of the fund's assets. For this purpose, the term "investment securities" generally does not include real estate, nor does it include the fund's holdings in wholly- or majority-owned subsidiaries.

For example, let's say a fund's portfolio is invested half in real estate and half controlling or majority interests in subsidiary companies. Such a fund would be excluded from the 1940 Act. It could also qualify under the OZ law (if 90% of its holdings are in OZs) and can raise capital via public or private offering.

HOLDING COMPANY
A Holding Company utilizes the same strategy as the hybrid fund described above, but without the real estate. A majority of its portfolio consists of controlled or majority-owned subsidiaries. In a sense, the fund is deemed to be in the business of its subsidiaries, rather than in the securities investing business. Appropriate acquisition targets might be a small family operated retail shop without succession plans for retirement. When owners are ready to retire, a fund could be setup to acquire these businesses, so as to retain the character of the downtown.

PRIVATE FUND
This fund model can work under the OZ structure, the 1940 Act, and work under the securities law regulating securities offerings. A private fund is the most common type of investment fund. It can have no more than 100 investors and may not advertise or conduct general solicitation for investors. However, a private fund may still be responsive to the community. It can take steps to ensure that what it does is beneficial for the community, for example by including the voices of community representatives in its governance. Sometimes a fund that is intended to be a true community capital fund – one intended to raise capital from the community – may start off seeded from accredited investors. This might be its Phase I or a multi-phase project that could result in a true community raise of public capital at a later date; for various reasons it can be very helpful to begin this way.

Ultimately, anyone, regardless of their wealth should have the opportunity to invest through a menu of investing options where they live locally and aligned with what they believe in. The authors of this CLP believe it is critical to create a shift in how communities think about investing such that Wall Street is not the go-to, but instead investing in the region in which they live, work, and play. When this happens a restoration of citizens' economic power will follow.

UTILIZING COMMUNITY CAPITAL FOR OPPORTUNITY ZONE INVESTMENT

Community capital as an investment tool means that citizens have the power to address some of the underlying systemic problems of the economic structure of our country and bring about positive improvements to our economy. Community capital refers to community-focused investment opportunities that are open to the public, including both wealthy and non-wealthy investors; in other words, everyone can participate. Community capital might be thought of as a separate asset class and an essential component of any investment portfolio because it serves as a counter-balance to the global Wall Street-dominated economy while contributing to a healthier local economy. Note that while the authors mainly use the term "community" in the sense of a geographically defined area, it could also be a dispersed community based around a common affinity or goal, such as renewable energy, biodynamic agriculture, or arts education.

MECHANISMS FOR RAISING COMMUNITY CAPITAL
In general, a venture (nonprofit or for-profit) can raise capital from their community either directly or indirectly. The direct approach is sometimes referred to as investment crowdfunding, a term that includes both direct public offerings (DPOs) and Title III exempt crowdfunding. The indirect approach to community capital is where a community investment fund (CIF) aggregates investment from the community and then invests in local ventures. Several models of these include legally compliant charitable loan funds, real estate funds, and diversified business funds. A healthy local economy may

feature a thriving mix of both. A CIF can be a particularly important component of a healthy local economy for four key reasons: scale, efficiency, diversification, and liquidity.

- A CIF can be more scalable because it can potentially raise an unlimited amount of money and finance an unlimited number of local ventures. In a CIF, the transactions should always be at a human scale, but we need a lot more of them to truly change the economy and to create a culture of community investment.
- A CIF can be more efficient because each investor only needs to do due diligence once on the fund, and then the fund handles due diligence on outgoing investments.
- A CIF is more diversified when compared to having each investor invest in one or a small number of local ventures.
- A CIF may be in a better position than individual ventures to offer its investors liquidity (i.e., a way to sell the investment). A CIF can be set up to redeem investors who need to exit the investment.

Community investment funds and individual DPOs (or other types of investment crowdfunding) are not mutually exclusive. There will also always be a need for organizations to do DPOs, particularly for ventures who prefer a direct connection with investors. Indeed, CIFs could play an important role for organizations conducting a DPO by:

- Making a small short-term loan to cover the costs of a DPO.
- Lending to the business on the strength of the equity raised in the DPO.
- Providing a sounding board to the venture on pricing and other terms of their DPO.
- Investing in the DPO early to seed it and inspire others to follow.
- Investing late in the DPO process to backstop it and ensure its success.
- Providing liquidity to DPO investors by purchasing their investment if they need an exit.

Challenges

Part of the challenge of the OF setups has been their development in a community-centered form and then implementation. This begs the question: how can capital be brought and structured within a community-oriented framework? Unfortunately, much of the capital that has gone into OFs so far have gone into projects that were ready immediately and likely were already going to be funded. These are typically pre-planned projects by 2017 or 2018 and became tax shelters for the very affluent.

Consequently, this type of investment may have an opposite effect than the intended purpose of the Zones. It is instead gentrifying many of these neighborhoods. Almost all of these Funds have been privately funded to date through very traditional systems, and often outside of community investment activity with no real connection to the Zone or those who live there. In addition to accelerated gentrification, there is no input from the community living and working there with the greatest need. For example, new housing in a real estate development OF might be market rate instead of affordable housing. As this gentrification happens, the rent also increases and becomes harder for those living there to stay.

While it may be necessary to start an OF with private investment, it doesn't have to exclude the voice of community members. Fund managers can look to local investors for representation and they can also design the Fund to take into account community needs utilizing advisory boards and other types of advisory structures. Another key piece that helps level the playing field is if there is an option through an investment entity that citizens can actually invest directly, too. This citizen investment may not be the bulk of the capital raised, but as possible accredited investors should still consider investing through a regulatory mechanism that allows for local investors and is not limited to accredited investors. These are ways to democratize the process and allow for a much greater exchange of information, transparency, guidance and advice from residents. It also helps ensure that some portion, if not most, of the returns stay within the community.

Bringing Capital to the Zone

There are several regulations applicable to bringing money into a zone. However, concern regarding the structure of the Fund itself must be addressed for representation to avoid additional expensive regulations. These include federal and state securities laws as well as the Investment Company Act of 1940. A lot of these funds are initially funded by private investment. It's important to think of a private raise – obtaining that capital necessary to meet investment needs – carefully because typically it would: be limited to accredited investors; have no public solicitation for fund investments; and lower compliance and disclosure burdens. This choice is often made because it's easy. However, as such a closed loop system, it has consequences and impacts for the community. There can be mission driven OFs that are privatized with true commitment to a community. That can be demonstrated through many of the above mentioned mechanisms such as a transparent reporting processes, acquisition, and implementation of funds, etc. While perhaps started as a private capital raise, they can be integrated and moved into a future public state.

As the funds are being structured and capitalized, additional strategies that allow for non-accredited community members include: Regulation Crowd Fund (Reg CF); Intrastate Direct Public Offerings; Multi-State Direct Public Offerings; Regulation A (Tier 1); and Regulation A (Tier 2). The Regulation Crowd Fund is limited to a million-dollar raise in a twelve-month period, but can attract investors from all 50 states. If a fund is ready to be capitalized by a small number of high net worth investors that are community-minded, a community could do a private raise to get it started and then move to a Reg CF to get up to a million dollars of community-raised capital. It's a fairly simple process and filing with the SEC. The difference between Reg CF and DPOs is that Reg CF does not involve any regulatory review or approval, whereas a DPO typically does. State-registered DPOs (either intrastate or multi-state) are great for a very geographically located fund with investors from one state or a small number of states. These allow for public advertising and non-accredited investors to participate.

The Regulation A can be used to raise larger amounts, albeit with additional levels of registration. Tier 1 of Reg A is suitable for a regional raise of up to $20 million. Tier 2 allows for a national raise of up to $50 million in one year. This type of offering is something a Fund might consider as it grows. One can view this as sequential and incremental growth steps to meet the demand of a community's fund depending on its focus. There are many tools that can fit geographical foci and small, medium, and large sized raises. What makes these community capital strategies impactful is the public nature of investment and that they're inclusive. Participation of community is the key to each of these raises that empower a more democratic process.

Within the City of Adrian, the OF will start small. Therefore, this CLP shares further information and highlights of the Regulation Crowd Fund also known as Title III. It is anticipated Adrian will use this as their Zone foundation.

Regulation Crowdfunding

Regulation Crowdfunding (also known as Regulation CF or Reg CF and Title III) was first signed into law by President Barack Obama in April 2012 as one part of the Jumpstart Our Business Startups Act, or JOBS Act. The JOBS Act was enacted to facilitate access to capital for a broader spectrum of people to invest in these ventures, such as start-ups and small business, for economic growth stimulation.

Regulation CF is an exemption to the registration requirements under the Securities Act of 1933 which means that a full registration of the security offering is not required. Although a registration and review of the offering by the securities regulators is not required, an issuer of securities under the Regulation CF exemption must meet certain disclosure requirements and must comply with regulations regarding, among others, the marketing of the securities and investor limitations.

Some of the key components of the exemption are:

- Any type of entity can utilize Regulation CF;
- Raise amounts are limited to $1M in a rolling 12-month period;
- Entities may sell securities in all 50 states;
- The offering must be hosted on an online intermediary portal that is registered under Regulation CF;
- Specific financial information must be disclosed and, depending on the raise amount, financial statements may need to be reviewed or audited by an accountant; and
- Both accredited and non-accredited persons can invest, although investors are limited to investing a certain dollar amount based on their income or net worth.

<u>The Pros of Regulation CF:</u> Virtually anyone can invest in an enterprise; issuers can offer any kind of investment (stock, notes, revenue shares); online marketing is permitted (though off-portal communications are limited); and it allows investment from residents of all 50 states. Like most capital raises, Regulation CF requires issuers to file a disclosure document that includes two years of GAAP financials, the number of employees, detail officers, directors, and significant stakeholders, share past financings as well as the intended use of funds, and all material risks.

<u>Potential Drawbacks of Regulation CF:</u> $1 million limit may not be sufficient for some businesses. Investors are limited to investing between 5% to 10% of their income or net worth each year as follows: If either the annual income or the net worth of the investor is less than $100,000, the investor is limited to the greater of $2,000 or 5% of the lesser of his or her annual income or net worth. If the annual income and net worth of the investor are both greater than $100,000, the investor is limited to 10% of the lesser of his or her annual income or net worth, to a maximum of $100,000.

Almost all advertising must be done on the investment portal. Advertisements outside the portal can only include: (1) a statement that the issuer is conducting an offering and a link to their funding portal; (2) the terms of the offering; and (3) identifying facts like name, legal identity, location, phone, website, e-mail, and a brief description of the business. The "terms of the offering" include: (1) the amount of securities offered; (2) the nature of the securities; (3) the price of the securities; and (4) the closing date of the offering period. An issuer's ability to communicate directly with potential investors about matters outside the above-described facts is limited. Regulation CF requires ongoing reporting for at least one year, including CEO-certified financial statements.

State-specific exempt crowdfunding: While waiting for the SEC's Title III regulations, more than half of the states enacted their own crowdfunding laws. Most of them were modeled after Title III, though some of them are less restrictive. For example, a few do not require use of a third-party portal. Since Title III went into effect, most of them will probably not get much use, except for those that will remain advantageous because they are less restrictive. Michigan's investment crowdfunding law, MILE, is both less restrictive and generous in the amount of money that can be raised by businesses and in the amount of money individual non-accredited investors may invest.

Nonprofit direct public offering: The SEC and most states allow a charitable organization to offer an investment without securities registration, though a notice filing may be required. For nonprofits in those states, this is the easiest way to do a direct public offering. A few states, notably California, do not have such an exemption and require registration even for nonprofits. However, an OZ fund may not be a charitable organization, so this strategy is not available to an OZ fund.

Intrastate direct public offering: This may be the most popular strategy for direct public offerings because it allows a company to raise an unlimited amount of money, as long as all investors are in the same state (along with a few other requirements). It requires state-level registration of the offering, which is not nearly as burdensome or expensive as a federal registration; and it can be cost-effective for raises as small as $250,000.

Rule 504 (multi-state) direct public offering: This strategy allows a company to take investment from multiple states, as long as you register (or otherwise find an appropriate exemption) in each of those states. The disadvantage of this strategy is that there is a $5 million aggregate cap. Still, it can be an attractive strategy because it allows for a public offering in one state, while still being able to take private investment from other states.

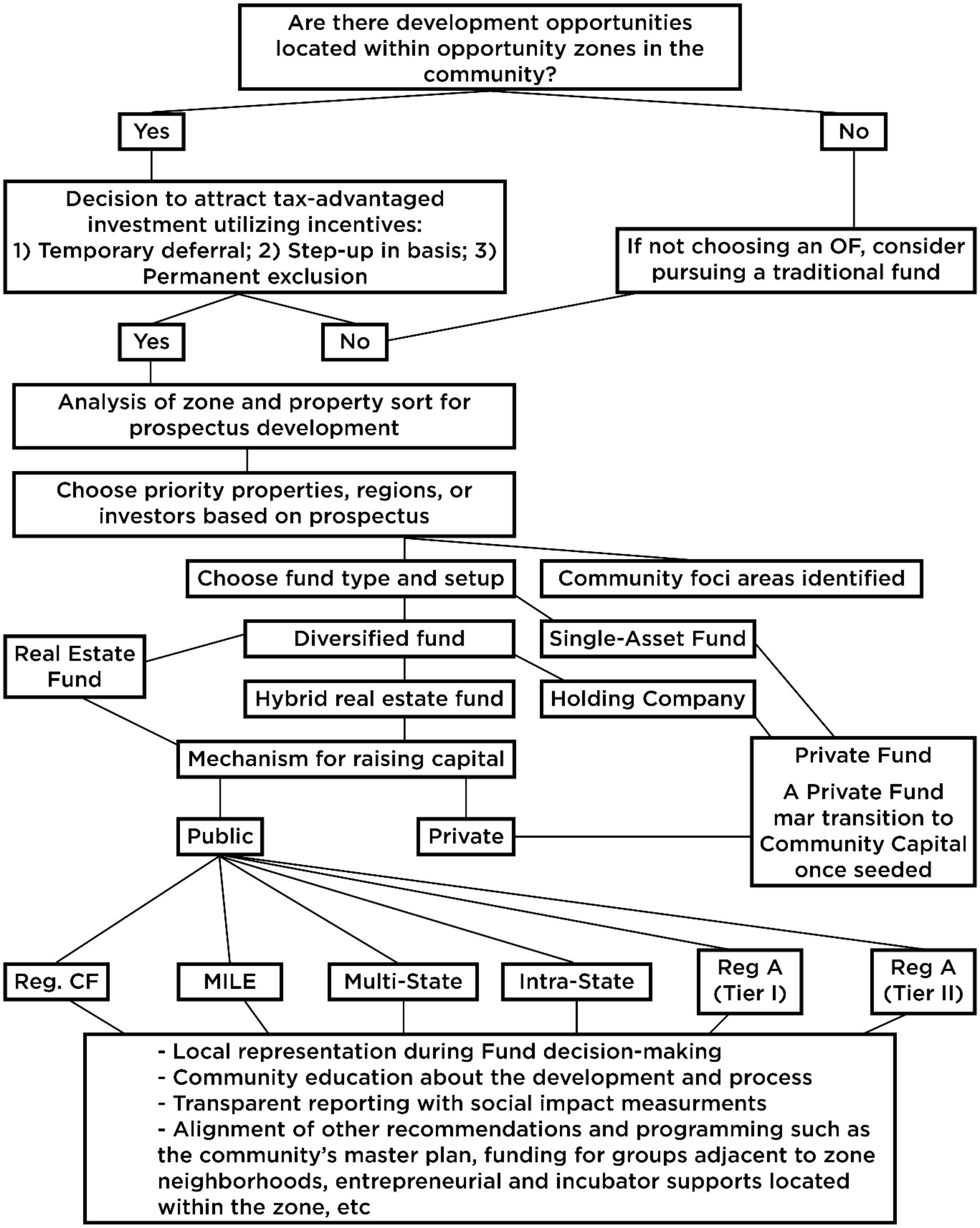
As indicated above, investment crowdfunding includes both direct public offerings and exempt crowdfunding. There are two reasons why Title III exempt crowdfunding, in particular, is not a direct public offering: First, it is not direct because the rules require use of a third-party crowdfunding portal. Second, while it has some of the characteristics of a public offering (i.e., it's open to non-accredited investors), there are limitations on the ability to market the offering (specifically, all communications must go through the portal).

Another distinction between a DPO and exempt crowdfunding is that most DPOs are vetted by either state regulator (in the case of intrastate or multi-state DPOs) or by the SEC (in the case of Regulation A). In both Title III and state-specific exempt crowdfunding there is no regulatory review. This regulatory exemption can cut both ways: While it can help launch an offering faster and at a lower cost, one may find that investors have less confidence than they might have in a registered offer that the state regulators reviewed.

Lastly, it should be noted that a lot of investment portals out there purport to be crowdfunding portals are really only open to accredited investors, in reliance on the SEC Rule 506(c) exemption that allows for general solicitation and advertising. Yet, even though an offering that is only open to the wealthiest 3% of Americans doesn't qualify as true crowdfunding, these portals can still provide a great service for entrepreneurs. By engaging community in the process and allowing them to invest and participate in decision-making, they can get behind collective impact goals. By explaining a collective mission and how it's going to make a difference, a much less extractive process will be had. Democratic processes affect how the economy is run and help wealth is kept within localities.

A decision making tree, or flowchart-like diagram, is offered below demonstrating the various outcomes stemming from a series of decisions for communities desiring to utilize these types of investment options for opportunity zone and fund development. The decision making tree is offered as a clear cut path for ease of information understanding, associated planning and anticipated outcomes. It is hoped this tree and the above information will help inform other communities, similar to Adrian, and beyond in developing a more democratic economy with collective impact-based outcomes – no matter their size.

DECISION MAKING OPPORTUNITY ZONE & FUND TREE



ON THE GROUND IN SMALL TOWN AMERICA: CITY OF ADRIAN

The City of Adrian's objective is to utilize their Opportunity Zone to accomplish a significant economic development project(s) that also accomplishes significant good in the community. In addition to taking advantage of projects that help build the local tax base, they're working towards solving other problems with a potential infusion of significant outside capital. It's also important to couple outside investment with local engagement. It is envisioned that such engagement comes in one of several iterations including site and project selection, initial and/or ongoing management of the project, and the opportunity for local investors to be part of its ownership.

At present, the city is taking the lead on potential projects after developing a prospectus from the 1,304 properties within the Zone census tract. It was sorted and prioritized with help from a small Rising Tide Opportunity Zone committee. Three high-priority sites have been identified and discussions with potential developers and existing land owners are underway. In addition, a broad outreach to the 100 largest property owners in the district is underway so that potential projects on likely properties are not missed through a mailer invitation to contact the city directly or participate in an educational workshop.

For the City of Adrian, project identification was the best first step in the OZ process toward getting to a capital raise and attracting an appropriate developer. The idea of a local real estate fund that could support a variety of projects seemed most promising. This is because the few local capital raises conducted within the region were centered on such specific projects. Therefore, it seems continuing this trajectory is most likely to yield positive results.

With respect to outside OZ investors, the city also anticipates optimal chances for success will be built around project-specific investments. Small communities like Adrian typically do not have the types of infrastructure necessary to attract significant outside investors. As such, they also do not host the cache of those investments as larger communities.

Therefore, the city is currently working with colleagues at Cutting Edge Capital in the Bay Area of California to determine their fund structure. Cutting Edge Capital will also likely assist with the Fund setup. Recent conversations have determined that the cost of establishing such a fund would be in the $30,000 range. This is not an inconsequential expense for the City and certainly not a decision that elected officials would make absent strong assurances the investment would yield a benefit that matches or exceeds its initial costs.

The local investment would either take the form of a crowdfunding raise or a DPO. The local investment model could use Michigan's investment crowdfunding law, MILE – Michigan Invests Locally Exemption. MILE would allow non-accredited Michigan investors to invest in a project as described, and would also allow that project to accumulate up to $1,000,000 from non-accredited investors, and an unlimited amount from accredited investors.

The three high-priority sites/projects that have been identified include a largely vacant mobile home park with substandard housing; a 1960s era enclosed mall on the south side of the city, and; a 5-7-acre parcel in the middle of a residential areas that is privately owned.

City of Adrian Site Priorities:

1) From the City's perspective, the most desirable site for an OZ project is the mobile home park. As noted, the project is mostly vacant, the remaining housing is substandard, the park itself has been poorly maintained, and there is strong demand for workforce housing. The park is in a challenging area of the city, with small and often poorly maintained housing in some of the area neighborhoods. There is robust employment available, however, with major employers along the Beecher Street east-west corridor that serves as a northern boundary of the OZ. Several of these employers are becoming very creative in their quest for employees.

   In a recent conversation with the park's owner, the potential opportunity to move forward with an OZ project received a boost when the owner indicated a willingness to work with the City, including selling a portion or all of his interest to facilitate a housing project on the site. The current agreement is that neither the city nor the owner will move forward with any plans for the property without a full discussion with the other party. In the meantime, the City is talking with potential developers and with the State of Michigan about what may be possible to develop on the site.

2) The Adrian Mall property is also a high priority because of its location at the most important retail and highest traffic count corner in the city and county. Sitting at the corner of M52 and US223, there is significant retail including big box stores and local food and car dealers along about ½ mile of development. The mall however is over 50% vacant, and now on its third owner in the last decade. The property has not seen adequate investment in its infrastructure or routine maintenance and upgrades for decades, and combined with the turmoil in the retail world it has devolved into an eyesore and a drag on the corner. However, out lots continue to be developed with three new restaurants constructed in the last five years and currently a 100+ room hotel under development.

3) The residential property in the middle of an existing neighborhood is an interesting option. It existed as a small agricultural area that saw single family homes built along the north, east, and west sides of the property, then ultimately multi-family rental housing closed in the property when a number of units were built on the south side of the property. The property is now effectively land locked, however, the major property owner also owns a single family residence on the north perimeter of the property that could provide satisfactory access. In this case the majority land owner is anxious to sell the property, and its location could be a good site for senior or workforce housing.

As part of the city's engagement with the Rising Tide program a planning firm from Ann Arbor, Beckett and Raeder INC, has been assigned to assist with the development of several projects including the City's OZ focus. Beckett & Raeder has staff working on the mobile home park site. The City has also reached out to the Michigan State Housing Development Authority and the Michigan Economic Development Corporation for such resources as recommended developers, incentives, and Redevelopment Ready Communities programming support – a process that assists with site development to which interested developers are then connected to community opportunities.

On many commercial and industrial sites, Brownfield incentives also may be brought to bear for specific eligible expenses, including environmental issues, blight and functional obsolescence. Brownfields can be entirely local in nature, where the additional resources provided to developers is exclusively from local Brownfield funds and tax capture, or they can also utilize state and federal grants and other resources.

Brownfields may be established if a property comes into Land Bank ownership. The Michigan Land Bank Act, PA 258 of 2003, prescribes what land banks can do with land including the ability to own, manage, maintain, and improve land, including the ability to acquire property "if the acquisition of the property is for economic development purposes." Land Bank properties are also by definition eligible for Brownfield incentives. The Brownfield Act, PA 381 of 1996, states that blighted properties "include property owned by or under the control of a land bank fast track authority."

These overlapping authorities mean that any property owned by a land bank can utilize a Brownfield redevelopment TIF to assist in the sale of this property, which accesses a revenue stream that can be exclusively local, and which can fill the gap between development costs and project income.

CONCLUSION

A challenge for Adrian and many smaller communities is the reality of what the market will support. As Adrian moves to next steps in the Opportunity Zone it is working with the Michigan Land Bank to utilize a unique combination of state law and development assets to close the gap between costs to construct projects and the income those projects will generate.

The City of Adrian is now working on two of its three OZ focused sites – the mobile home park and the vacant residential property in the middle of a developed residential block – to bring this potentially powerful development incentive to bear and to entice local and national investments. In addition, this development incentive is likely to encourage developers who can see a path forward that addresses the financial viability of challenging projects in more rural areas.

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