An Economic Overview of the City of Billings and the State of Montana and a Discussion of the Potential Availability of Federal Incentives

Final Report Prepared for

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1. Economic and Employment Challenges for Billings and the State of Montana

The Billings Metro Area and the State of Montana have several imminent and upcoming challenges. These include:

1. An aging Workforce;
2. A shrinking economy; and
3. Age-related declining tax revenues

Absent a plan to address these critical challenges, Billings as well as the State of Montana will certainly experience negative consequences, potentially including loss of major employers, loss of skilled labor, loss of capital investment, declining home values, and declining of tax revenue.

If employers cannot find enough skilled employees to operate their businesses then they must downsize, move, or go out of business. When jobs leave the area, skilled laborers must also leave to find jobs or stay and take lower paying jobs. When skilled labor leaves or is forced to take a lower-paying job, other businesses that depend on induced spending also suffer. Obviously, this has an ultimate negative impact on capital investment, tax revenue, and home values. Detroit is a prime example of this trend.

1-1. A Brief Overview of the Billings and Montana Economies

In 2015-2016, personal incomes in the Billings Metropolitan Statistical Area ("MSA") held steady and declined slightly by 0.1% in 2016-2017. The percentage of households at or below the poverty level, however, also slightly declined from 10.5% to 10.2% in 2016-2017. While incomes are steady or slightly declining, the reduction in poverty is likely due to the decrease of average annual unemployment from 3.6% to 3.5% for the Billings MSA in 2016-2017.[1] U.S. average annual unemployment has declined from 4.9% to 4.4% in that same period.[2] Employment for all industries within the Billings MSA has also increased slightly by 0.5% in 2016-2017, although this is a slowdown from the 1.9% increase in industry employment from 2015-2016.[3]

The Billings MSA Real Gross Domestic Product ("RGDP") declined in 2015-2016 by 3.1%, and declined again in 2016-2017 by 2.5%. During the same period the U.S. saw positive GDP growth. The Billings MSA is ranked 371 of 389 Metropolitan Statistical Areas within the U.S. with regard to percentage change in RGDP. In Montana, the State and MSA economies look to be connected to the oil industry and fluctuate with its cycles. The annual percentage GDP change is plotted below against annual average crude oil prices (yellow curve in the background).

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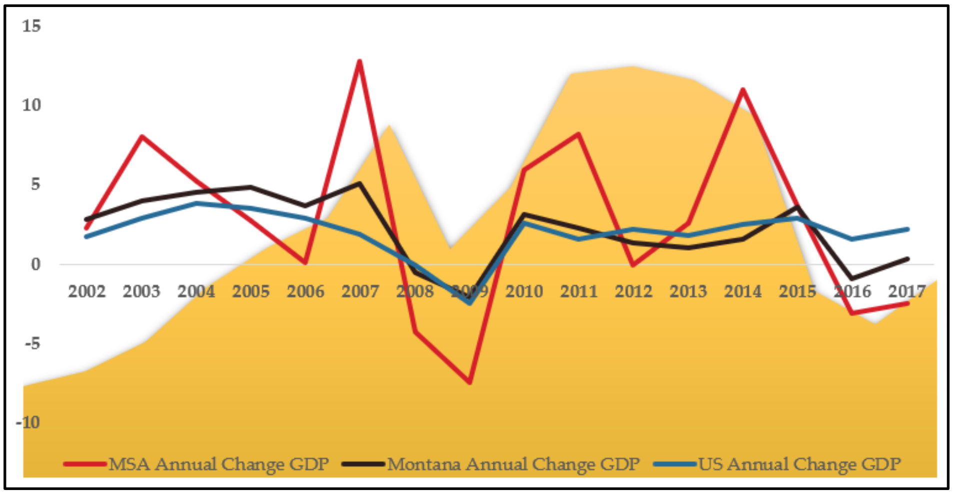
[1] U.S. Census Bureau, *2013-2017 American Community Survey 5-Year Estimates*
[2] Bureau of Labor Statistics, *Average Annual Employment by Metro Area*

[2] Bureau of Labor Statistics, *Average Annual Employment by Metro Area*
[3] U.S. Census Bureau, *County Business Patterns*

Comparative GDP Annual Change & Crude Oil Prices



Source: Bureau of Economic Analysis (www.bea.gov);
https://www.statista.com/statistics/262858/change-in-opec-crude-oil-prices-since-1960/

From 2015 to 2017, employment declined in 7 of the 11 highest paying industries in the Billings MSA. The two largest industries in the Billings MSA in terms of the number of employees, Health Care/Social Assistance and Retail Trade, both have earnings below the median earnings across all industries.

Location quotients (LQ's) are useful for studying the composition of jobs in an area relative to the average, or for finding areas that have high concentrations of jobs in certain occupations. LQs for occupation and industry employment show particularly high concentrations of petroleum-related, religious, medical, and food/beverage jobs in the Billings area.

2017 Earnings, Employment, & Growth by Industry

Industry	Median Earnings	2017 Employment	2015-17 Employment Growth
Mining, Quarrying, O&G	$84,831	1,760	(399)
Utilities	$59,625	630	(2)
Professional, Scientific, & Tech Services	$52,040	4,322	(219)
Transportation & Warehousing	$50,901	4,611	547
Public Administration	$46,153	3,146	(166)
Wholesale trade	$44,947	3,225	169
Manufacturing	$43,281	4,206	(162)
Information	$40,792	1,632	(170)
Construction	$40,111	7,564	498
Finance & Insurance	$38,400	3,932	(265)
Educational Services	$33,944	5,528	384
Median Earnings across all industries $33,906			
Health Care & Social Assistance	$33,654	13,888	1,168
Real Estate	$29,092	1,451	86
Ag, Forestry, Fishing, & Hunting	$28,097	1,596	209
Other Services	$24,941	5,049	479
Retail Trade	$24,576	10,830	(382)
Admin, Support, & Waste Mgt Services	$22,693	2,817	183
Arts, Entertainment, & Recreation	$20,679	2,368	57
Accomodation & Food Service	$16,796	7,132	(379)

Source: Bureau of Economic Analysis (www.bea.gov); ESRI Demographics (www.esri.com); American Community Survey 2010 (5 year), 2015 and 2017 for Billings MSA

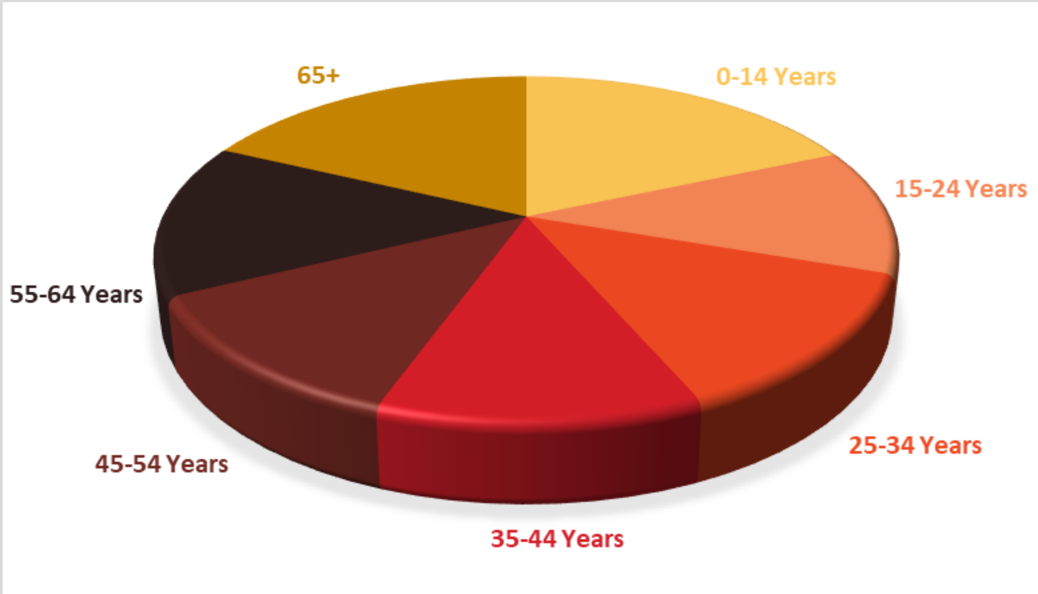
1-2. Workforce in Montana & Billings and Challenges Ahead

Aging Workforce

Montana will face a significant labor shortage as the current population ages out of the workforce without sufficient workers to fill the vacancies they leave. This leaves even fewer to fill any new jobs that would be created in the state. The Montana Department of Labor and Industry reports that 20% of Montana's Workforce will retire in the next decade.[4] The median age in the Billings MSA is 40.1 years, which is higher than the US median age of 38.3 years. By 2023, the Billings MSA median age will increase to 41.1 years.

Billings MSA: 2018 Age Distribution

[4] Montana Dept. of Labor & Industry 2018 Labor Day Report



Source: ESRI Demographics (www.esri.com)

Additionally, the labor force participation rate in the Billings MSA and across Montana is declining. While the number of MSA workers between 65 and 74 increased by 11% from 2015-2017, the labor force participation rate for the same age group declined 2.5%.[5] Finally, as the tables below indicate, the elderly age dependency ratio for the MSA is increasing and is higher than the national level. By 2023, there will be 33.8 MSA residents over 65 years of age for every 100 working-age residents, 5.4% higher than the projected national rate.

Elderly Dependency Ratio

	Yellowstone County	Billings MSA	Montana	US
2010	21.5%	21.9%	22.4%	19.4%
2018	27.5%	28.1%	29.1%	24.4%
2023	32.9%	**33.8%**	34.9%	28.4%

Source: Calculated by author using ESRI Demographics (www.ESRI.com)

The overall dependency ratio for the MSA is 57.2, which is considerably higher than the national level. By 2023, there will by 63.1 dependents (under 14 and over 65 years of age) for every 100 working-age residents.

Overall Dependency Ratios

[5] American Community Survey 2015 (5 year estimates) and 2017 for the Billings MSA.

	Yellowstone County	Billings MSA	Montana	US
2010	51.3%	51.3%	50.4%	49.0%
2018	57.0%	57.2%	56.5%	52.7%
2023	62.9%	**63.1%**	63.1%	57.0%

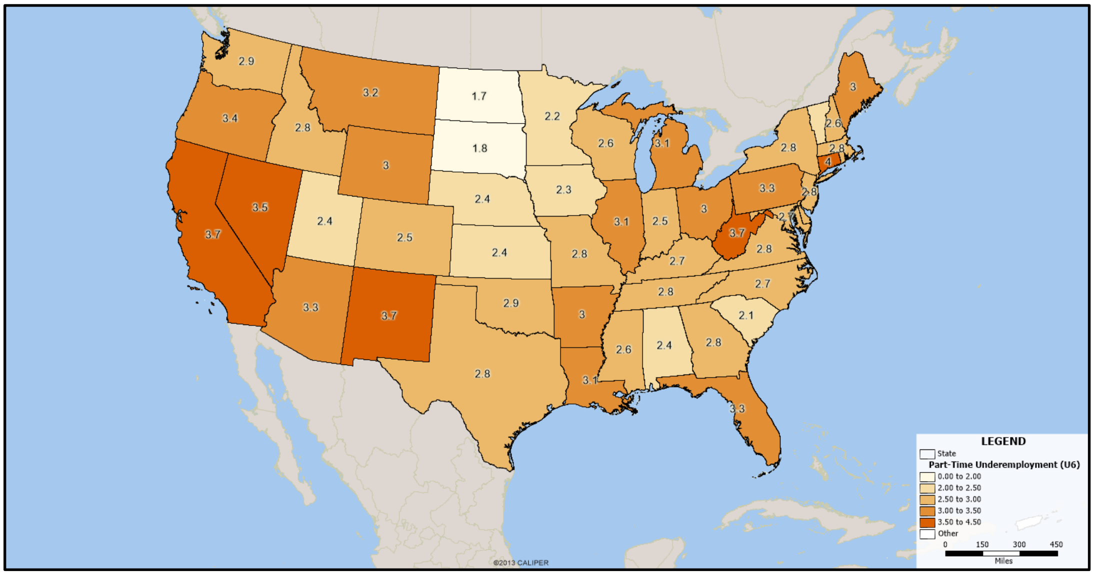
Source: Calculated by author using ESRI Demographics (www.ESRI.com)

Part-Time Employment

To combat Montana's aging population, which is contributing to the labor shortage, current workers need to be more effective and efficient. One way to accomplish this goal is to help involuntary, part-time workers transition into full-time positions. Montana has a high share of part-time jobs: only 32.9 hours worked per week per job, tied for lowest in the nation.

Across Montana, 3.2% of workers who are employed part-time for economic reasons work less than 35 hours per week, want to work full-time, are available to do so, and gave an economic reason (their hours had been cut back or they were unable to find a full-time job) for working part-time. The highest incident of this type of underemployment nationwide was 4% in Connecticut.

Part-time Underemployment



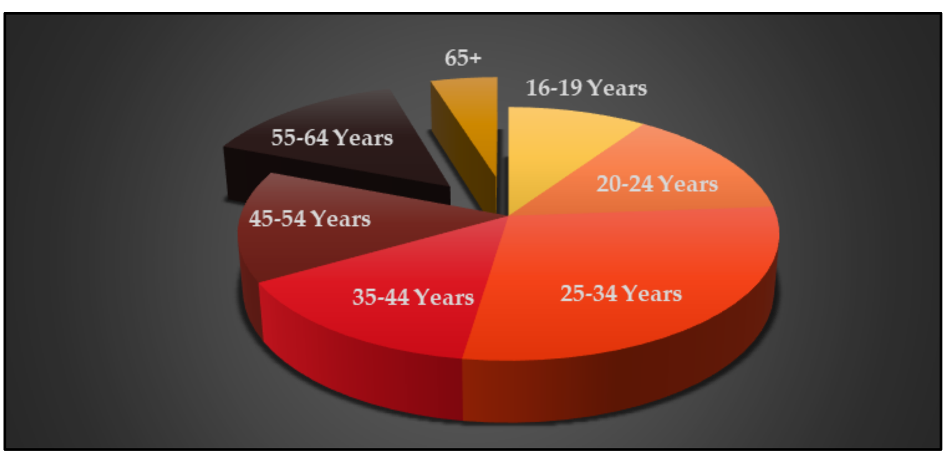
Source: Bureau of Labor Statistics (www.bls.gov) Geographic Profile of Employment and Unemployment

In 2017, Montana had a civilian labor force of 522,000. This included 277,000 men and 245,000 women. The unemployment rate for men was 4.6% and for women 3.8%. The labor force contains 24,000 women who maintain families with an unemployment rate of 6.2%.

Montana has a well-educated workforce. 161,000 or 30% of the labor force, have attained a bachelor degree or higher education. Unsurprisingly, statistics show that unemployment rates decrease as educational level rises.

The state has 387,000 employed full-time workers and 114,000 employed part-time workers. Of the unemployed workers seeking work, 17,000 are seeking full-time positions and 5,000 are seeking part-time work. Industries with the highest unemployment include: leisure & hospitality, construction, wholesale/retail, and education & health services.

Age Distribution of Unemployed



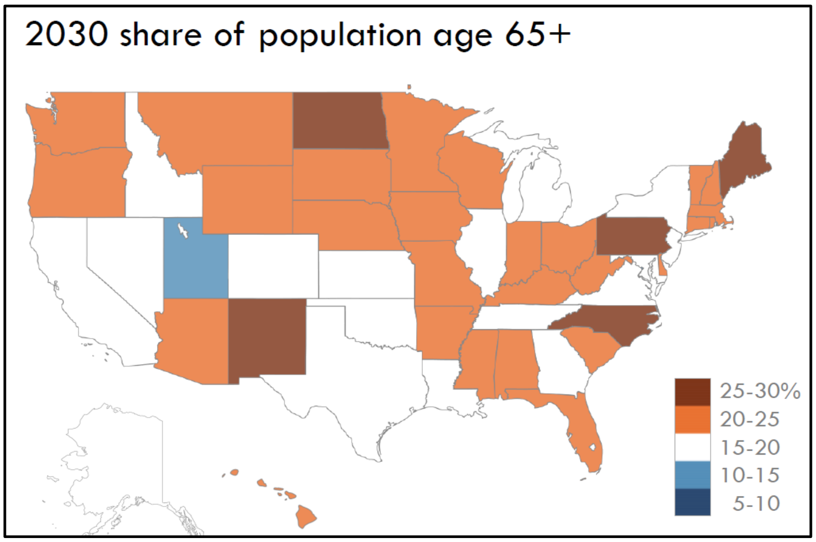
Source: Bureau of Labor Statistics (www.bls.gov) Geographic Profile of Employment and Unemployment

2. Absent Policy Changes—Potential for Declining Tax Revenues

Across the country, an aging population will lead to rising per capita expenditures & falling per capita revenue as the baby boom generation retires. Nationwide, aging will reduce per capital income tax revenue 2.4% and per capita sales tax revenue 0.5% by 2030.

Since Montana does not have sales tax, the per capita income tax impact will most likely be even greater. A study from the Federal Reserve Bank of Kansas City estimates that Montana's per capita income tax revenues will decline 3-4% by 2030.[6]

An aging population will also increase government expenditures on elderly services.



Source:http://www.ncsl.org/Portals/1/Documents/nalfo/Watkins_2016_Evolving_State_Tax_Base.pdf

2-1. IMPLAN Analysis Shows Declining Tax Revenues

An economic analysis performed by Baker Tilly estimates that Yellowstone County, where Billings is located, will lose 14,571 workers by 2027, due to retirement. Baker Tilly conducted an IMPLAN simulation to determine the impacts. In order to isolate the impacts of the aging workforce in the IMPLAN model, other labor or income changes have not accounted for in the analysis.

[6] https://www.kansascityfed.org/PhjaZ/publicat/econrev/pdf/13q4Felix-Watkins.pdf

The simulation found that Yellowstone County annual tax receipts will decline $4,827,487 (see table below). Additionally, the analysis found that the retirements will reduce state and local tax receipts by $37,275,554. Finally the analysis showed a significant negative effect on induced impacts. Induced employment will decline by 6,161, induced labor income by $275,019,445, and induced output by $787,786,916.

It is important to note that the analysis is based on an average compensation (provided by IMPLAN) of $76,733. Since this average is based on workers of all ages, and those approaching retirement are in the higher income brackets, this number is probably an underestimate. During the same period that older workers will retire, younger workers will also join the workforce. Due to this increase in younger worker making up a larger part of the workforce the incoming labor will have significantly lower wages than the outgoing workers.

	Tax on Production and Imports	Households LT15k	Households 15-30k	Households 30-40k	Households 40-50k	Households 50-70k	Households 70-100k	Households 100-150k	Households 150-200k	Households GT200k	Totals
TOPI: Property Tax	($4,457,790)										($4,457,790)
TOPI: Motor Vehicle License	($101,947)										($101,947)
TOPI: Special Assessments	($79,467)										($79,467)
Personal Transfers		($60)	($18,662)	($711)	($17,579)	($2,338)	($2,808)	($1,670)	($6,849)	($5,564)	($56,242)
Personal Tax: Motor Vehicle License		($423)	($2,850)	($5,748)	($6,991)	($18,412)	($25,126)	($22,829)	($8,940)	($9,905)	($101,224)
Personal Tax: Property Tax		($140)	($1,073)	($1,922)	($1,481)	($5,630)	($6,856)	($7,955)	($2,765)	($2,995)	($30,817)
	($4,639,204)	**($623)**	**($22,585)**	**($8,382)**	**($26,051)**	**($26,380)**	**($34,789)**	**($32,455)**	**($18,553)**	**($18,464)**	**($4,827,487)**

Source: IMPLAN Group LLC, IMPLAN System (data and software), 16905 Northcross Dr., Suite 120, Huntersville, NC 28078 www.IMPLAN.com (Yellowstone County as geographic region)

Assumptions:

The analysis based decline in *employment due to aging* on MT Dept. of Labor & Industry 2018 Labor Day Report which reported a loss of 100,000 workers by 2027 due to retirement. Age distribution for MT and Yellowstone County is from ESRI (www.esri.com). Rate of retirement by age is from http://time.com/money/4584900/ages-people-retire-probably-too-young-early-retirement/. The percentages allowed for estimates of the number of people in MT (68,984) and Yellowstone County (9,900) that are already retired today, and those remaining to retire in the future. Next, removal of the 100,000 retirements from state level workers were evaluated to determine that the state workforce over 55 years will shrink by 34%. Finally, reduction of the Yellowstone County workforce by 34% was factored in which resulted in a 55 and over county workforce of 27,736 by 2027. This means that the County will lose 14,571 jobs due to retirement by 2027. In order to isolate the impacts of the aging workforce, the analysis did not account for any other labor or income changes. Average compensation of $76,733 (www.IMPLAN.com) was used in the analysis. Note that average compensation contains the value of earnings and benefits. TOPI = Tax on Production and Imports.

3. The Importance of an Urban Growth Plan

The US economy is a system of linked metropolitan economies, each organized around a unique mix of industry specializations, labor, and housing market characteristics. It is the role of local and regional stakeholders to address the unique opportunities and weaknesses in their community. Local success depends on local leaders' ability to effectively set goals, organize firms, and reach out to target populations in ways that result in a new job for a worker and a skilled hire for an employer.

A new approach to economic development has emerged over the past few years. Gone are the days of chasing a single employer that will bring hundreds of jobs to a community, often at the expense of another community and at high tax consequence. Today, economic development strategies are shifting toward a broader approach that considers the long-term goals of the community and brings together a variety of stakeholders (firms, entrepreneurs, educators, workers).

Portland, Oregon has developed a strong economic development strategy that embodies this new economic development approach, which envisions "economic prosperity for all". The plan's specific strategies include: People: Recruit, develop, and advance the region's talent; Business: Grow business and pioneer innovation; Place: Improve infrastructure to meet the needs of people, business, and innovation.[7]

The One Big Sky District plan capitalizes on these new economic development initiatives by breaking from the tradition of silo single-project development and embracing a concept-driven plan. This plan will build a platform for long-term growth in Billings and the region.[8] [9]

4. Federal Development Incentives

Several Federal programs are available to subsidize commercial development. These programs target specific outcomes such as preservation of historically significant structures, attracting capital to low-income communities, stimulating commercial investment that results in tangible benefits to low-income persons and to stimulate jobs in areas of high unemployment. A summary of programs applicable to Billings follows.

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[7] http://www.greaterportland2020.com/#welcome

[8] https://www.brookings.edu/blog/the-avenue/2016/03/07/why-economic-development-matters/

[9] https://www.brookings.edu/wp-content/uploads/2016/02/BMPP_RemakingEconomicDevelopment_Feb25LoRes-1.pdf

4-1. Opportunity Zone Equity

Established by the Tax Cut and Jobs Act of 2017, Opportunity Zones ("OZs") are the latest federal tax incentive to attract private investment to low-income census tracts. OZs are a subset (25%) of NMTC census tracts as designated by the governor of each state and approved by the U.S. Treasury. Each designated OZ is certified for new investment through 12/31/2027, and through 2047 for liquidation.

To qualify for the OZ tax benefit, investors must reinvest capital gains realized within the preceding 180 days from a prior investment as a common or preferred equity investment within an OZ. Essentially any person or entity that would report a short or long-term capital gain is eligible to reinvest those funds and receive OZ tax benefits. OZ funding cannot take the form of debt.

OZ benefits are attractive, adding approximately 400 basis points to a 10-year IRR, but are not so compelling as to offset excessive risk. OZ tax benefits come in three forms:

1. Tax Deferral – the capital gain tax from liquidating the original investment used to make the OZ investment is deferred until 12/31/2026.

2. Discount – the capital gain tax from liquidating the original investment used to make the OZ investment paid with the 12/31/2026 tax return is discounted 15% if the OZ investment is made by 12/31/2019 (and still held as of 12/31/2026), or 10% if the OZ investment is made between 1/1/2020 and 12/31/2021 (and still held as of 12/31/2026).

3. Tax-Free Appreciation – if held 10-years or longer, the new OZ investment receives a "step-up" in tax basis equal to the liquidation price to eliminate any gains tax on the new OZ investment. Appreciation and recapture of depreciation are eliminated on the new investment.

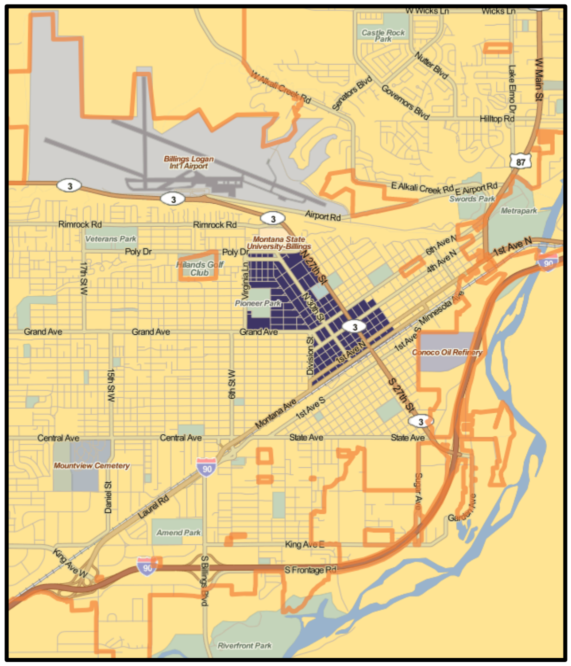
Accounting and legal professionals are seeing unprecedented enthusiasm by investors to review OZ investments, and numerous Qualified Opportunity Zone Funds ("QOFs") are being formed with various strategies to raise capital. Community Development Corporations and state and local governments are also promoting OZ-areas to attract capital to their communities, and have the potential to serve as a connection point between projects and local investors, while being mindful of U.S. securities laws as QOFs are private placements of securities.

Unlike NMTC, OZ benefits are an entitlement. So long as the census tract qualifies (see https://go.bakertilly.com/contactbtc0618), and the investment structure and deployment of funds meets other technical criteria, then the benefits will flow to the investor. Without the need for an intermediary or arbiter of community impact as seen in the NMTC and EB-5 programs, there is an expectation that a significant amount of capital could flow to these under-invested communities.

Projects within an OZ should be able to accelerate raising capital and careful structuring should allow the sponsor to share in the OZ benefit by offering a lower pre-tax IRR, where the OZ tax benefit lifts the after-tax IRR back to “market.” Given that OZ capital originates from sophisticated investors, it is unlikely that the cost of capital will be significantly below market, as the main driver of the after-tax IRR is the step-up in basis for holding the OZ equity investment for at least 10-years. For additional detail on OZ, please see Appendix A.

Opportunity Zone Conclusion

Billings has a concentrated Opportunity Zone in its downtown to attract private capital.



Similar to EB-5, to attract investor capital from outside the local and state economy, OZ projects within Billings will have to differentiate to compete with QOFs promoting investments in gateway cities. Projects with compelling demand-generators, or credit tenants will attract investors focused on quality, while the potential for tax-sheltered appreciation tax losses from depreciation will attract more aggressive investors.

4-2. New Market Tax Credits (“NMTC”)

Authorized under the Community Renewal and Tax Relief Act of 2000, the NMTC program provides flexible and below-market-rate capital to stimulate commercial investment in Low-Income Communities. The goal of the program is to create tangible outcomes that benefit low-income persons and communities. Since inception, over $50 billion of NMTC has been deployed across the country.

Congress authorizes the issuance of NMTC, which has generally been in the amount of $3.5 billion annually. Presently, NMTCs are authorized at $3.5 billion annually through the 2019 calendar year application. The 2018 application awards are expected in March 2019, and the 2019 application is expected in May/June 2019 with those awards announced in the winter of 2020. Continuation of the program beyond that date requires Congressional action.

The program is administered through a division of the U.S. Treasury called the Community Development Financial Institutions Fund ("CDFI") and implemented through intermediaries called Community Development Entities ("CDEs"). CDEs are entities with a mission to provide capital to underserved communities, and are often affiliated with:

- Banks (as part of their Community Reinvestment Act ("CRA") activities);
- Non-depository CDFIs (e.g. LISC or Enterprise Community Partners);
- State and municipalities (e.g. Commonwealth Cornerstone Group, an affiliate of the Pennsylvania Housing Finance Agency);
- Community development corporations (e.g. Montana & Idaho Community Development Corporation, now known as MoFi); and
- Privately owned CDEs (e.g. Advantage Capital and Stonehenge Capital).

CDEs are the intermediary through which NMTCs are monetized into flexible, below-market rate loans or investments for qualified businesses seeking capital to fund development or businesses located in qualified census tracts. Through a competitive process, CDEs apply to the CDFI for an allocation of NMTC. The CDFI assesses the experience and business plan of each CDE to act as a good steward of this limited resource. Each CDE defines its geographic service area (e.g. local, state, multi-state or national) and articulates a strategy to use NMTC-subsidized financing to generate specific outcomes to alleviate economic or social priorities identified within its service area.

NMTC census tracts are generally those with either an Area Median Income ("AMI") less than 80% of the statewide median income, or a census tract with a poverty rate of 20% or greater. Severely distressed census tracts meet any one of the following four criteria: (i) the census tract median income is less than 60% of the AMI; (ii) the poverty rate is greater than 30%; (iii) the unemployment rate is greater than 1.5x the national average; or (iv) the qualifying census tract is in a rural (non-MSA) county. There are other secondary criteria where meeting any two secondary criteria constitutes a severely distressed census tract.

The NMTC actually "belongs" to the CDE. The CDE is charged with monetizing the credit and combining it with other forms of capital to fund projects in qualified census tracts. The purchaser of the tax credit (typically a national bank) receives a 39% credit spread over a 7-year compliance period. Under current market conditions, each dollar of NMTC allocation will provide \$0.20 to \$0.25 of cash (net of transaction costs) to as part of the capital stack of selected projects. The cash generated from the sale of the tax credits is typically loaned to the project with an interest rate of around 2-3%, and structured such that the project can acquire the loan for a bargain price of around 10% on the dollar at the end of the compliance period. For example:

NMTC Allocation	10,000,000
NMTC Tax Credit Rate	39%
Tax Credits to monetize	3,900,000
Market Price	$ 0.82
Gross Proceeds	3,198,000
Less: Typical Transaction Costs	700,000
Net Proceeds to Project	2,498,000
Typical Annual Cost	65,000
Implied loan rate	2.60%
Typical Bargain Purchase Price	1,000
Loan "forgiveness" for tax purposes *	2,497,000
*taxable income to for-profit borrowers	

Upon receiving an allocation of NMTC from the CDFI, CDEs run a competitive process amongst projects seeking NMTC-subsidized financing. CDEs generally have over 4x the amount of request for NMTC than the amount allocated from the CDFI. NMTC is not an entitlement program, and CDEs are free to use their NMTC as they determine best fits their objectives. CDEs engage an Advisory Board, staffed by low-income community representatives, to assist in reviewing the outcomes projected by the projects under review and to help prioritize funding projects that align with the needs of their service area. In recent years, CDEs have "raised the bar" with respect to expectations of quantified outcomes since each project they fund becomes their track record, which the CDFI reviews when considering future awards.

On average, CDFI funds about 70 CDEs annually, making the average award $50 million of NMTC per CDE, with a range typically of $15 million to $90 million. Like all financial institutions, CDEs seek a level of diversification of projects to (1) spread impact across their service area and (2) to diversify their portfolio of NMTC loans and investments. Consequently, most CDEs fund 3-5 projects with each allocation and typically do not allocate more than $15-20 million to one project. Projects seeking over $20 million of allocation should plan to source allocation from more than one CDE, and generally do best after securing a local "anchor" CDE to help attract allocation from national and multi-state CDEs that can choose from a much larger pool of projects.

Finally, because of the competition for NMTC allocation, CDEs will not hold allocation for projects to mature. Projects with a runway of 9 months or more are typically regarded by CDEs as "pipeline projects" to feature in their next NMTC application as an example project, and generally only consider allocating current NMTC to projects that demonstrate an ability to be "shovel ready" within 6-months from the next award date. In order to consistently win allocation, CDEs need to quickly close current allocation and maintain an active pipeline in order to credibly demonstrate additional need for new allocation to CDFI

NMTC in Billings

Obtaining NMTC requires the confluence of several variables:

1. A CDE that (i) covers the geographic location of the project, (ii) has current allocation, and (iii) where the projected outcomes of the project fits with the strategy of the CDE.

Since national and multi-state CDEs have a significant pool of NMTC projects to choose from, those CDEs generally use their allocation in conjunction with local CDEs to support projects with significant outcomes that benefit low-income persons and/or low-income communities. The CDFI maintains a searchable database (see https://www.cdfifund.gov/awards/state-awards/Pages/default.aspx), which yielded three CDEs that won allocation in the 2016 and 2017 rounds that target Montana in a meaningful way:

b. Ecotrust won $75M in 2016 round - Established in 1991, Ecotrust CDE is a rural CDE that seeks to foster a natural model of development that creates more resilient communities, economies, and ecosystems. The organization will use its 2015-2016 NMTC allocation to invest in natural resource operating businesses that create enduring value and advance social and environmental benefits for low-income communities, prioritizing tribal communities.

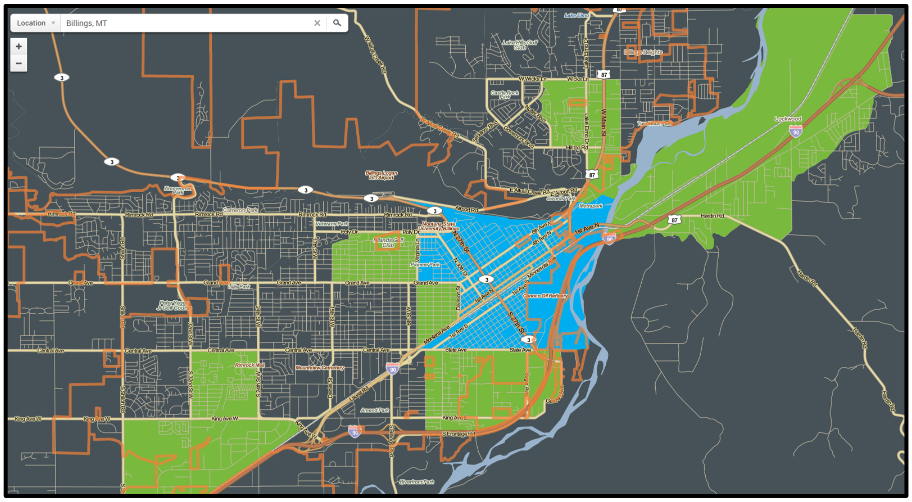
c. Clearinghouse CDFI won $65M in 2016 - Clearinghouse CDFI was established in 1996 to bridge the gap between conventional lending standards and the needs of low-income and distressed communities. The organization will use its 2015-2016 NMTC allocation to invest in a variety of projects, ranging from hospitals to infrastructure, retail to manufacturing, and hotels to community facilities, that serve people in severely distressed communities in California, Nevada, Arizona, New Mexico, and western Native American reservations.

d. Montana Community Development Corp (now known as MoFi) won in 2016 ($90M) and 2017 ($65M) and note that they describe their service area as ID, MT & WY (probably because there is not enough deal flow in MT alone) - Montana Community Development Corporation is a non-profit, rural CDE and CDFI serving Montana, Idaho, and Wyoming. The organization will use its 2017 NMTC Program Allocation to finance businesses, focusing on projects that advance state and local economic development priorities; deliver critical community services for low-income people; involve key downtown areas with vacant buildings and empty lots; and incentivize the start or expansion of manufacturing businesses. Their website has their team (https://mofi.org/about-us/team/) and board with offices in Missoula, Bozeman and Boise.

At present, all of the CDEs above have closed or committed their current allocation to other projects, but are accepting applications for their 2018 round, should they be awarded another allocation from CDFI in March 2019. Of the three above, MoFi is the best fit for the Landmark project in Billings, but a commitment from MoFi and their assistance to attract allocation from national and multi-state CDEs is required to achieve any critical mass of NMTC, which likely would not exceed $30-40 million ($6-9 million of project funding) under any conditions.

2. Qualified Census Tract. Data from CDFI states that all CDEs have committed to using at least 75% of their allocation to fund projects in “severely distressed” census tracts.

The map below illustrates those areas in Billings that are qualified (green) and severely distressed (blue).



https://www.bakertilly.com/nmtc-lihtc-tax-credit-mapping-tool

Consequently, projects located in the green zone are at a competitive disadvantage to those located in a blue census tract. Even if supported by a local CDE, it is unlikely that any national or multi-state CDE would co-allocate to a project in a green zone.

NMTC Conclusion

In summary, NMTCs provide below market-rate capital in order to stimulate growth in economically distressed areas. As discussed above, applications for allocations of NMTCs that will be awarded in March 2019 have already been made to those CDEs that target Montana. While NMTCs remain a potential resource for capital, it should be regarded as a potential medium to long-term funding opportunity.

4-3. EB-5 Financing

Like many other countries, the U.S. offers an immigration-for-investment program, which is referred to as the Employment Based Fifth Preference ("EB-5"). The EB-5 program is administered by the U.S. Citizenship and Immigration Services ("USCIS"), which is a department within Homeland Security. EB-5 financing is typically structured as below-market rate subordinated debt, which is funded by high net worth foreign individuals motivated to immigrate to the United States.

Under the EB-5 program, an investor may obtain permanent U.S. residency (a "green card") for his or herself, their spouse and unmarried children under the age of 21 by making a $1 million investment that results in the creation of 10 new U.S. jobs. The investment amount is reduced to $500,000 if made within a Targeted Employment Area ("TEA"), which is an area certified as having an average unemployment 1.5x the national average. If the investment is made through a certified Regional Center, then the job creation requirement may be fulfilled with indirect and induced jobs (in addition to direct jobs). Indirect and induced jobs are calculated using economic inputs, such as project costs or project revenue, through models such as RIMS II and IMPLAN.

Scarcely used before 2008, the program exploded in the wake of the Great Recession as developers sought alternative sources of capital. The program was massively successful in China, where an established immigration-consulting industry embraced EB-5 and added it to the existing consulting for student and H1-B (employees with special skills) visa programs. Until recently, the Chinese market accounted for over 90% of EB-5 visas.

However, the proficiency of the Chinese market to source EB-5 capital fell victim to its own success. Only 10,000 EB-5 visas are authorized annually, and each investor, spouse and child counts toward the annual limit. Demand in excess of 10,000 visas creates Retrogression, which is a backlog maintained on a country-by-country basis. Presently, a new investor coming from China has to wait 13 years for a green card after an approximate two-year period for approval of their application. The wait time has essentially killed all demand in China and the industry has moved to other countries to source investors, but those countries lack the infrastructure, thus raising capital takes significantly longer as new markets are educated about the program and the sales-cycle is longer.

Specifically, the industry has focused on India, Vietnam and Brazil as large markets with a critical mass of high net worth individuals that are interested in immigration options. Focused efforts on these markets has caused India (7 years) and Vietnam (5 years) to also go into Retrogression. Presently, the market has cooled off for larger projects and typical EB-5 capital raises are under $20 million (representing ~30% of the capital stack) and predominantly in "gateway" markets such as Miami, San Francisco, Los Angeles and New York City. Generally, EB-5 projects outside of gateway cities tend to be tied to a compelling demand generator or public-private partnership investment, such as an airport hotel or convention center repaid with tax increment proceeds.

An additional development in the wake of Chinese retrogression is an increase in the cost of capital to offer returns more commensurate with the risk position of the EB-5 capital, thus making EB-5 funding less attractive for projects that can obtain conventional financing without the transaction costs and uncertainty of how long (or if) the EB-5 capital will be raised in a challenged market.

EB-5 Conclusion

Given current market conditions, an EB-5 capital raise for a project in Billings is not recommended as a *primary* source of funding. An EB-5 strategy could be employed to replace expensive conventional limited partner capital with less expensive EB-5 debt financing. For example, an EB-5 offering with no minimum and a maximum of $12,500,000 would take-out limited partners to the extent funds were raised during construction (the period in which jobs are created):

Senior Debt	32,500,000	32,500,000
Limited Partner Capital (18% IRR)	12,500,000	-
EB-5 Capital (8-9% interest rate)	-	12,500,000
Equity	5,000,000	5,000,000
Total Project Costs	50,000,000	50,000,000

To compete with projects offered in gateway cities, a project in Billings would need to have a compelling demand driver, offer a rate of return higher than that offered in competing projects, fill a smaller portion of the capital stack and have at least 10% cash-equity behind it.

Appendix A

Opportunity Zones

A powerful new tax incentive for real estate investors, venture capital, private wealth, family offices and private equity

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OVERVIEW

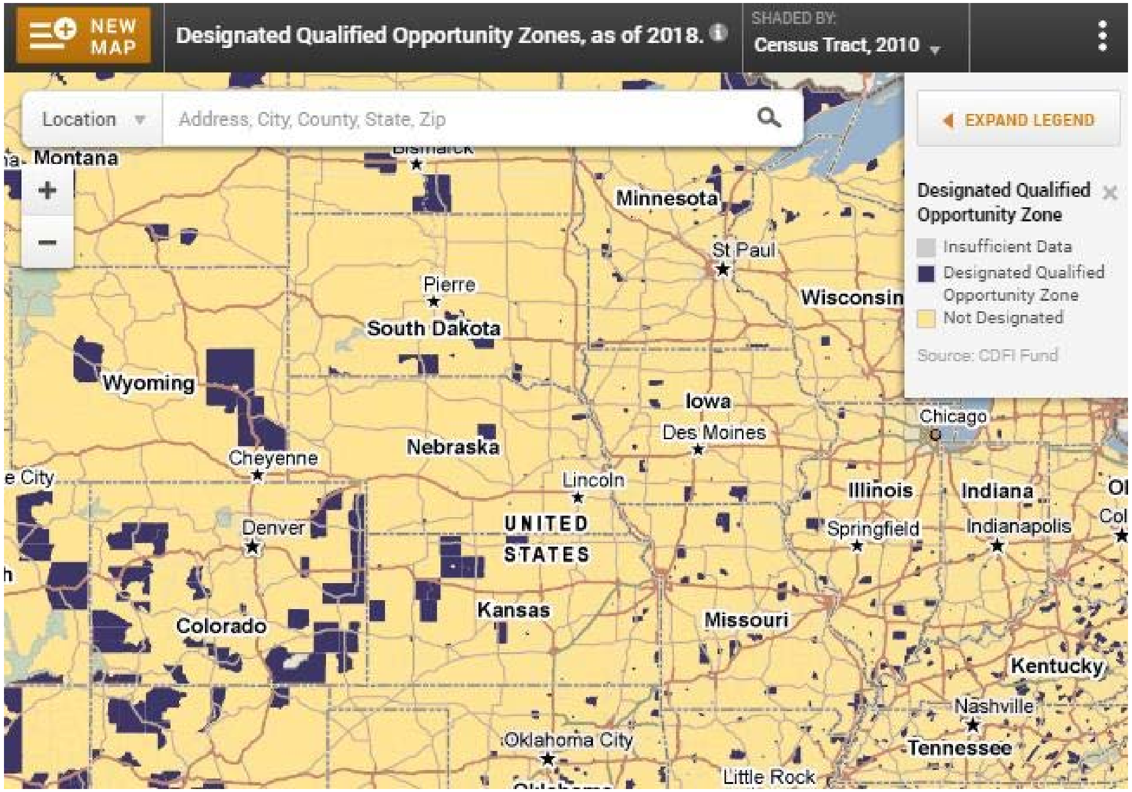
Opportunity Zones

What are Opportunity Zones and where are they?

- An Opportunity Zone (OZ) is a population census that meets the definition of a "low-income" community as that term is defined in the Internal Revenue Code in the context of the New Markets Tax Credit (NMTC)
  - Eligible areas are based on low-income census tracts and tracts contiguous to these low-income census tracts
- These census tracts have been specifically designated as Qualified Opportunity Zones (QOZs) under Section 1400Z
- IRS Notice 2018-48 includes an official list of all population census tracts designated as QOZs
- There are now more than 8,700 certified QOZs in all 50 states, D.C., Puerto Rico and the Virgin Islands
  - 11 percent of the country is designated as an OZ

OPPORTUNITY ZONES

Baker Tilly's mapping tool



Find eligible areas at bakertilly.com/opportunityzones

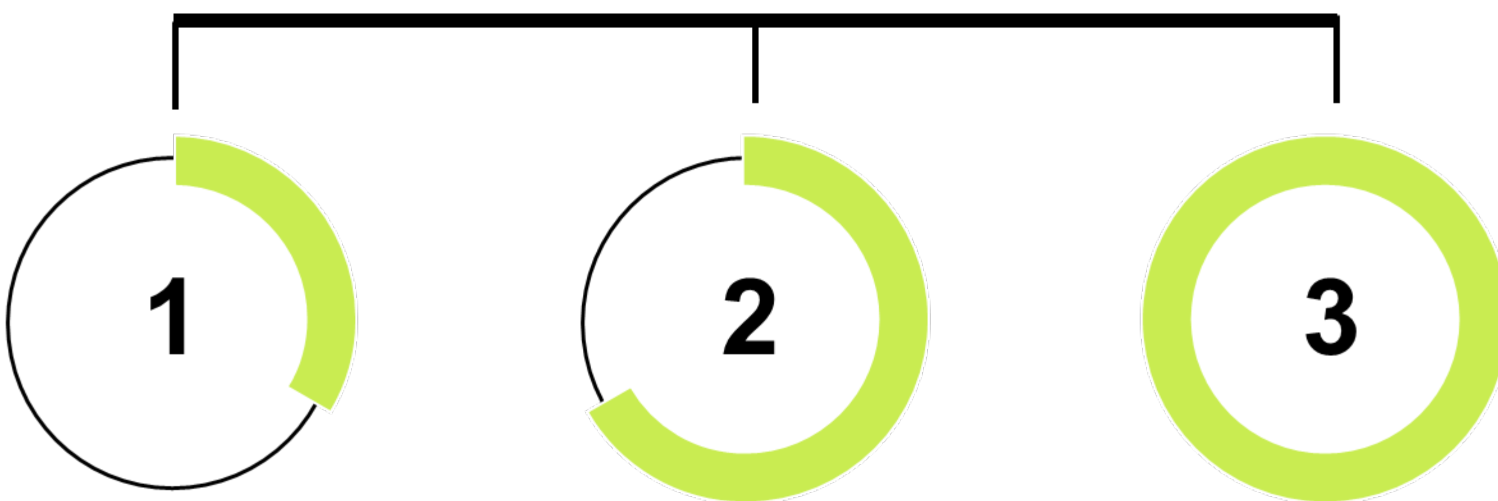
OPPORTUNITY ZONES

Overview

- Established by the Tax Cuts and Jobs Act of 2017
- Incentive to stimulate significant economic development
- Encourages investments in certain low-income communities
  - States designate QOZs
- Potential to defer and permanently reduce capital gain
  - Deferral and reduction of gain, NOT a credit or deduction
- Requires reinvestment of the capital gain into Qualified Opportunity Fund (QOF)
  - Similar to 1031 gain but gain does not have to come from a real estate investment
- Brand new, untested, thin guidance exists – no judicial doctrine

OPPORTUNITY ZONES

What are the tax incentives for investment in a QOZ?



Defer capital gain

Partial forgiveness of capital gain

Total forgiveness of tax on appreciation

OPPORTUNITY ZONES

Benefits of the OZ

- **Deferral**: The original gain invested is taxable only when the investment in the Opportunity Fund is sold or Dec. 31, 2026, whichever occurs first.
- **Partial forgiveness**: If the OZ investment is held five years, the original gain is discounted 10 percent (15 percent if held more than seven years). Investment must be made by Dec. 31, 2019, in order to qualify for 15 percent discount.
- **Tax-free appreciation**: If the Opportunity Fund investment is held for more than 10 years, the tax basis of the OZ investment steps up to its fair market value upon sale.
  - This is upon an election made by the investor on their tax return covering the period of sale, if the investment's value appreciated. If the value decreased, the election would not be made.

In effect, appreciation on the investment, but not the original deferred gain, is eliminated permanently. Depreciation losses should be a permanent benefit with a 10-year hold. We are awaiting IRS confirmation of this significant tax benefit.

What gain qualifies for tax benefits?

Participation in the OZ program begins with investing capital gain into an Opportunity Fund.

- It includes long- and short-term capital gain, collectables gain, gains from the property governed by section 1231, capital gain dividend distributions, but gains that would generate ordinary income are ineligible.
- The capital gain must originate from a sale or exchange with an unrelated party within the previous 180 days.
- Investing other money alongside capital gain is permissible, but only the capital gain portion of the investment qualifies for the tax benefits.
- When recognized, the deferred gain includes the same attributes in the year of inclusion that it would have had if tax on the gain had not been deferred.

OPPORTUNITY ZONES

How long is the designation?

- The designation of a census tract as a QOZ remains in effect until December 31, 2028
- Qualified gain must be invested in a QOZ before 12/31/2026 for the OZ benefits.
- Recent regulations clarified that if an investment is made, and during the holding period of the investment the QOZ designation expires, the investor will obtain tax-free appreciation on a sale of their investment until a hard date of 2047

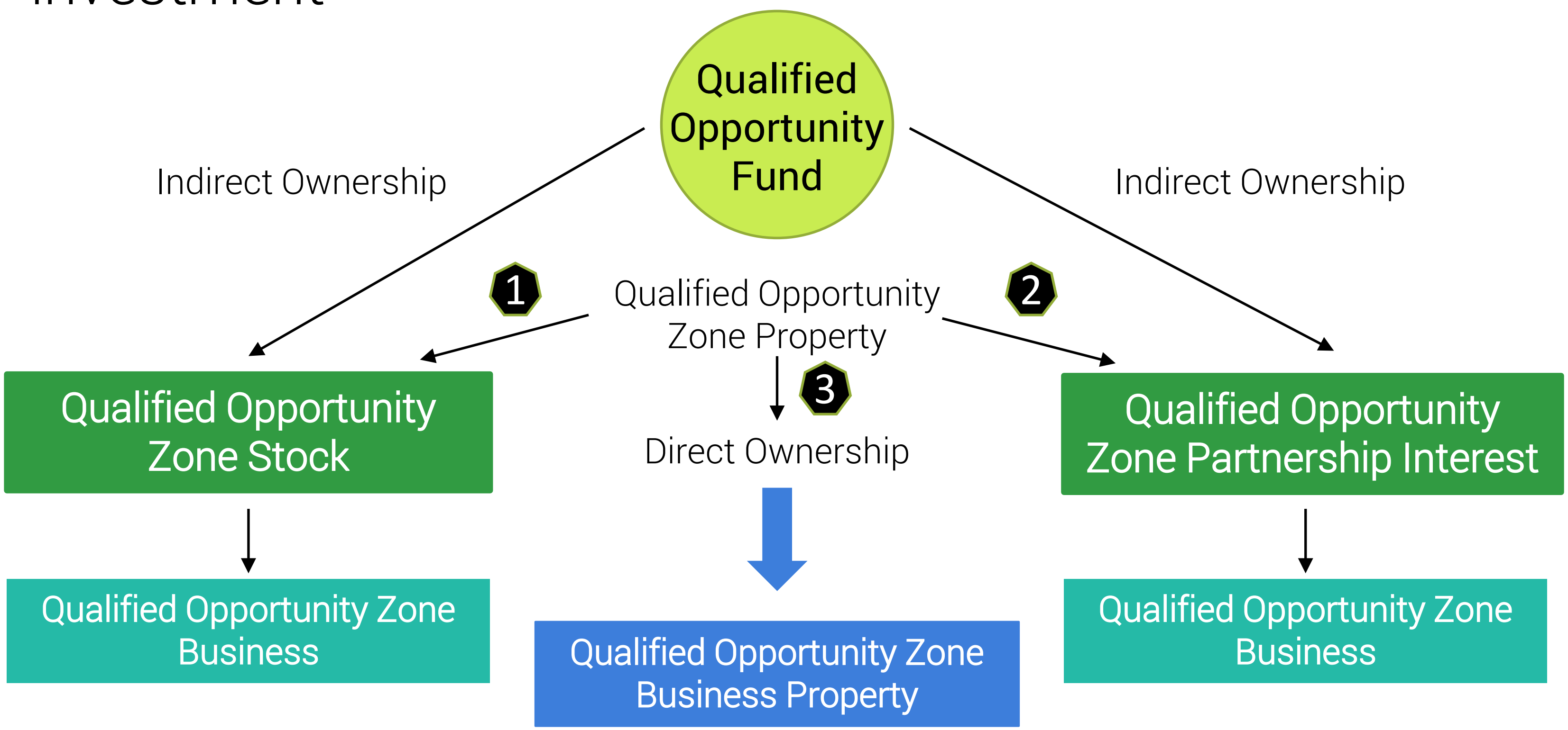
OPPORTUNITY ZONES

Taxpayers eligible to elect gain deferral—special rule for pass-throughs

- If a partnership elects to defer the gain, the gain is not included in the distributive share of the partner
  - All the tax benefits are applied at the partnership level, and the original gain is not taken into account by the partners
- If a partnership chooses not to defer the gain, then the partner has the ability to make the election with regard to its distributive share
  - The 180-day investment window generally begins at the close of the partnership's taxable year
  - Alternatively, if the partner has actual knowledge of the date the gain is recognized by the partnership, it can elect within the 180-day window beginning on the earlier date
  - Special rule also applies to other pass-through entities, such as S corporations

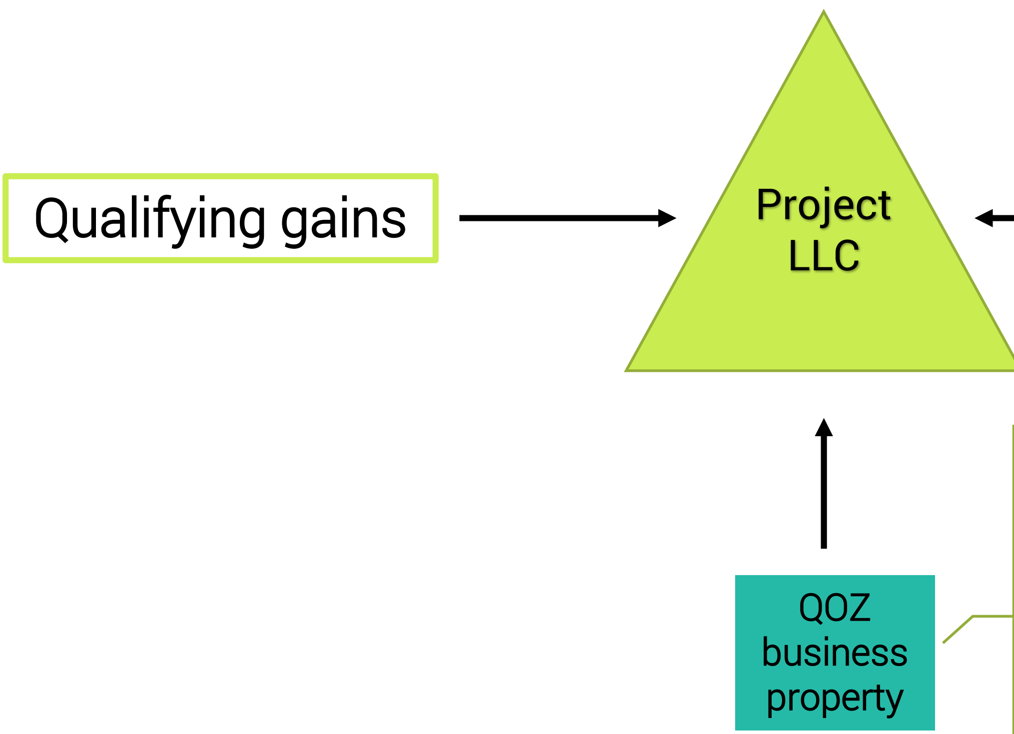
INVESTMENT STRUCTURE

Options for direct or indirect QOF investment



INVESTMENT STRUCTURE

Direct QOZ fund model for rental real estate

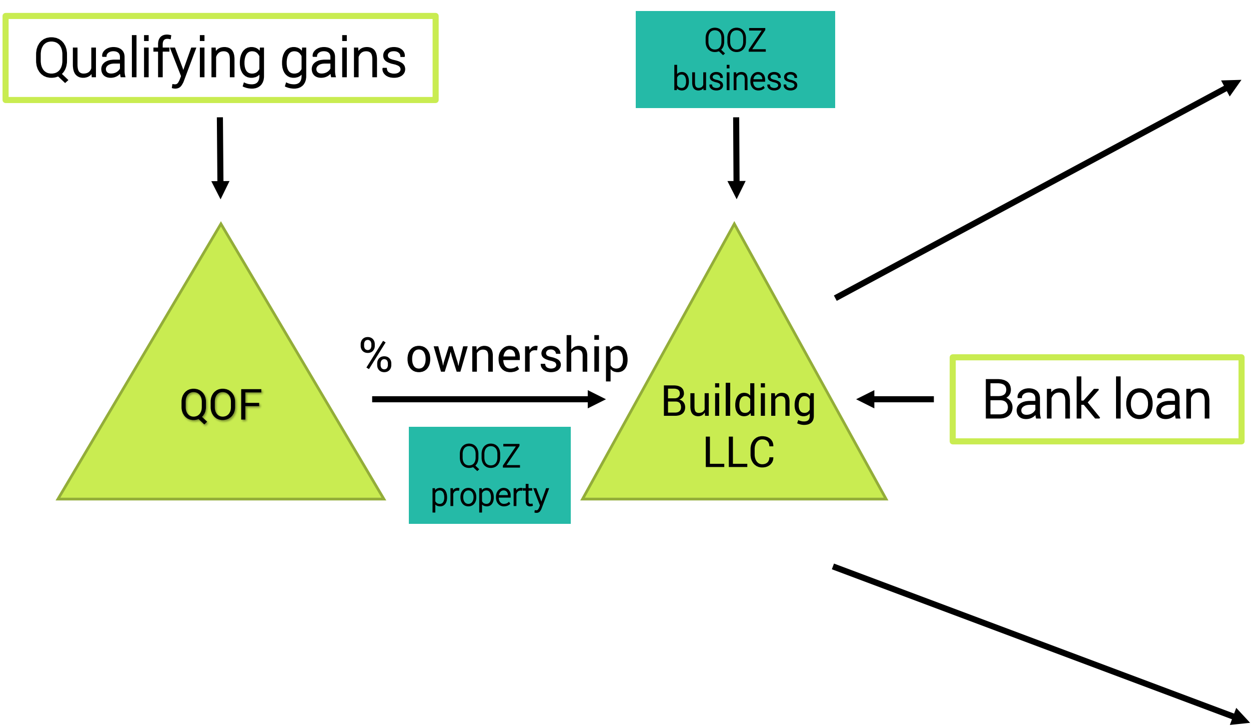


Requirements of QOZ business property

1. Tangible property used in a trade or business
2. Acquired from an unrelated party (20% standard) after 12/31/17
3. Original use commences with the QOF or is substantially improved by the QOF
4. During substantially all of the QOF's holding period, substantially all of the use of the property was in a QOZ

INVESTMENT STRUCTURE

Indirect QOZ fund model for rental real estate



Requirements of QOZ business

1. Trade or business where "substantially all" of tangible property owned or leased is QOZBP – 70/30 test
2. 50% of gross income comes from "<u>active</u>" conduct trade or business
3. Less than 5% NQFP with reasonable amounts working capital – 31 month runway
4. No "sin" businesses
5. If intangible property, must be used in trade or business

\+

Requirements of QOZ business property

1. Tangible property used in a trade or business
2. Acquired by the business by purchase after 12/31/17
3. Original use commences with the business or is substantially improved by the business
4. During substantially all of the business's holding period, <u>substantially</u> all of its use was in an QOZ

What type of investment qualifies?

Qualified Opportunity Zone business property means:

- Tangible property used in a trade or business
  - We assume rental real estate qualifies as a trade or business since it is used in an example in the newly released guidance—Revenue Ruling 2018-29
- Property acquired by purchase after Dec. 31, 2017
- The original use of such property in the QOZ commences with the qualified Opportunity Fund or the Opportunity Fund substantially improves the property
- Where the Opportunity Fund owns the property directly, substantially all of the use of such property occurs within a qualified OZ

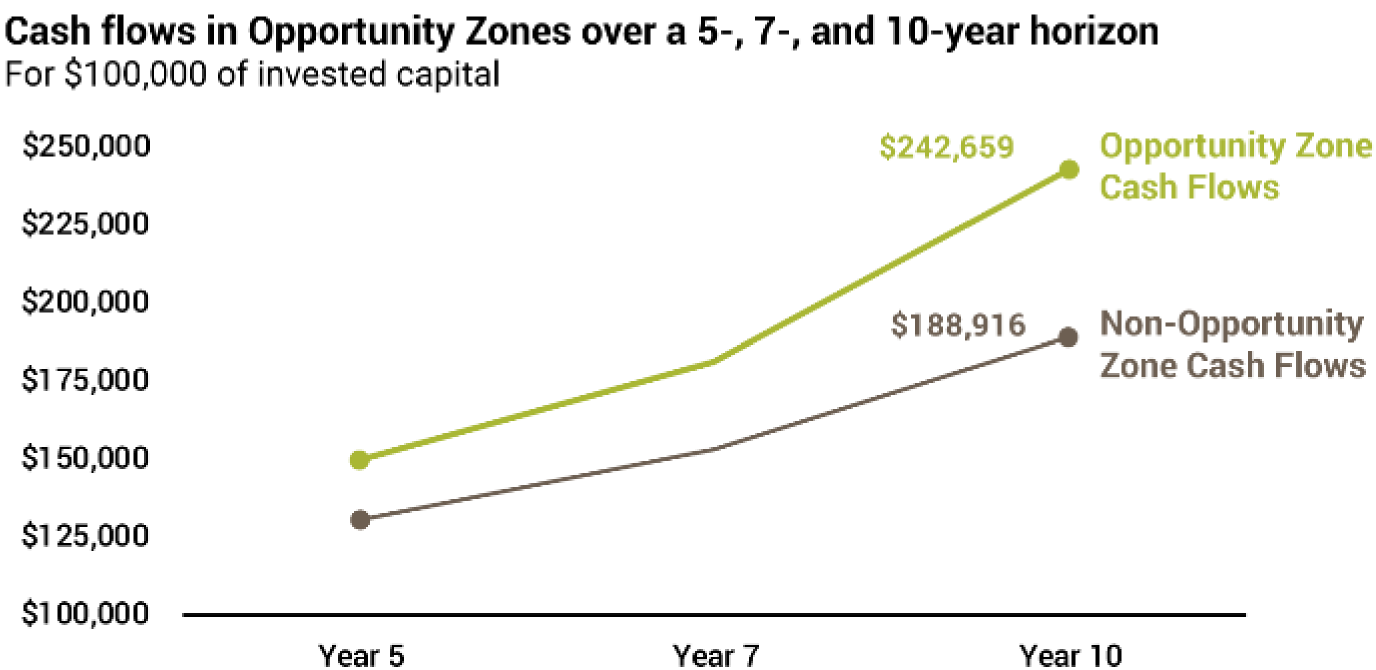
Original use or substantial improvement

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

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

OPPORTUNITY ZONES

Benefits of the OZ



This model assumes a 23.80% federal tax rate, 5.00% growth rate and 10.00% annual investment return. This model is for illustration purposes only, and contains certain financial assumptions as to the possible future results that are inherently uncertain and subjective. We make no representation or warranty as to the attainability of those assumptions or whether future results will occur as illustrated.

OPPORTUNITY ZONES

Example impact on IRR

Assumptions

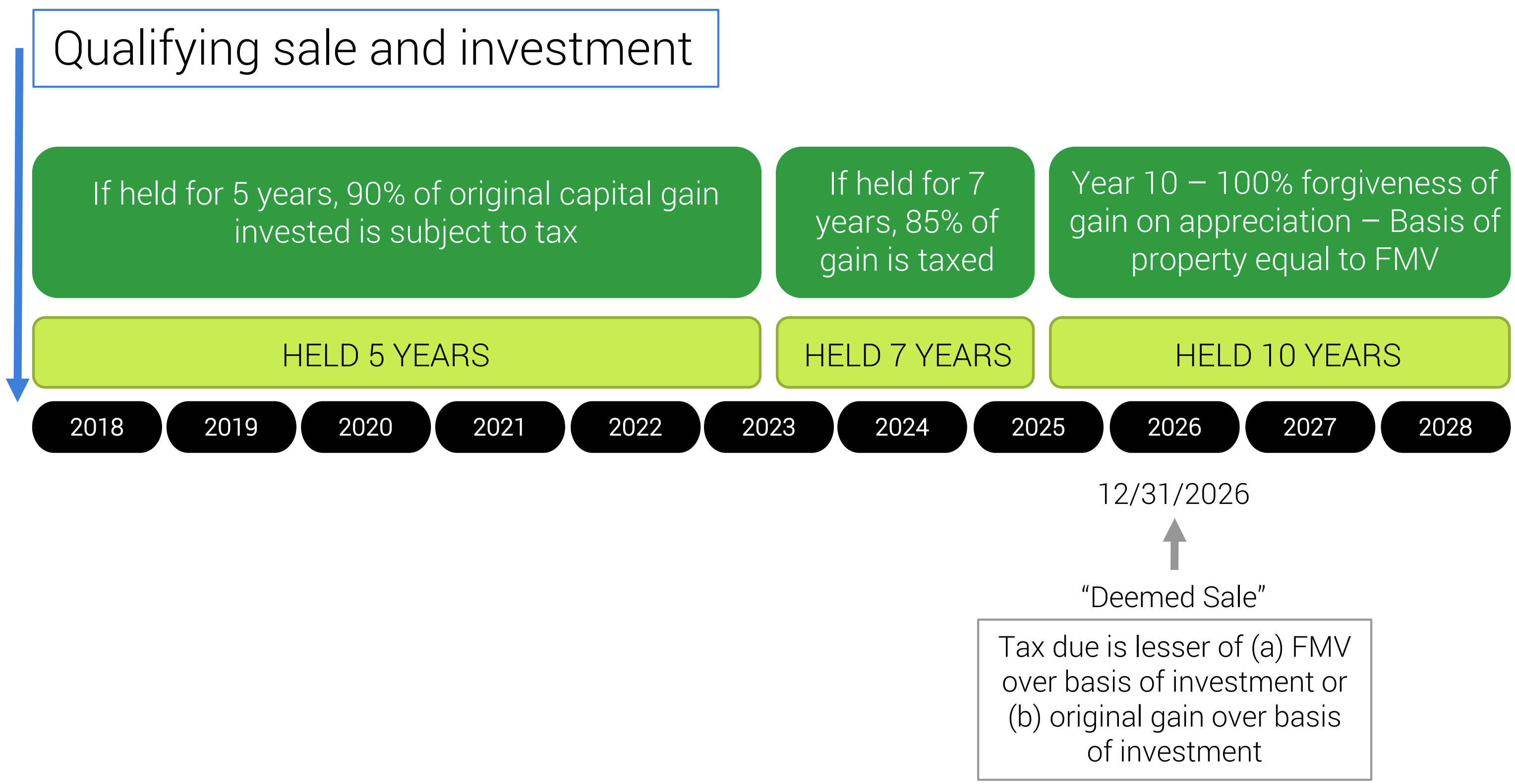
- Projects are economically identical (i.e., same cash and tax shelter attributes), but one is within an OZ and one is not
- OZ investors defer 23.8 percent in capital gain tax, while non-OZ investors pay 23.8 percent capital gains tax (all investors are assumed to liquidate an investment with a gain to make this investment)
- NOI growth of 2 percent per year, 3 percent management fee, triple net tenants, 5 percent assumed vacancy, accelerated depreciation*
- Investment sold at 6 percent cap rate, net of 5 percent transaction expenses
- Annual passive income taxed at 29.6 percent and tax losses assumed to be used in current year

*awaiting IRS confirmation on negative capital account step-up

After-tax IRR	OZ	Non-OZ	OZ improvement
5 years	7.8%	5.9%	32%
7 years	8.9%	6.9%	29%
10 years	10.9%	7.5%	45%

OPPORTUNITY ZONES

Capital gain deferral, forgiveness and tax-free appreciation



OPPORTUNITY ZONES

What about the treatment of the investment before year 10?

- Investment generates income
  - Pay tax on general operating income
- Investment generates tax losses, may be suspended
- Sale of Opportunity Fund assets before year 10
  - Investors realize gains on interim sales prior to year 10
  - Gain would be recognized by the corporation or individual investor depending on structure
- Avoidance of interim gain on recycled investments
  - Regarding the federal income tax treatment of any gains that are reinvested by the Opportunity Fund, the IRS stated that “soon-to-be released proposed regulations will provide guidance on these reinvestments…”

OPPORTUNITY ZONES

What investment types does the OZ program favor?

- **Commercial real estate**: Works well since the program is focused on long-term investment and real estate is not going to grow out of compliance like an operating business potentially could
- **New business startup in an OZ after Dec. 31, 2017**: Application is challenging without future guidance by Treasury but the OZ legislation can benefit start-up businesses
- **Expanding an existing business into an OZ**: This investment type is also contemplated, but if the business outside of the OZ is a substantial part of your business, may have to set up a regarded entity to run operations inside the OZ and also for every year thereafter to ensure compliance; new 70/30 rule for qualified Opportunity Zone business affords some leeway
- **Small business already in an OZ with large expansion**: If already in an OZ at Dec. 31, none of the assets would be Qualified Opportunity Zone Business Property; would have to meet “substantial improvement” requirement

Fund certification

IRS recently provided guidance regarding Opportunity Zone Fund certification:

- To establish an Opportunity Fund, the IRS states that there is no formal approval or action required by the IRS
- **An eligible taxpayer "self-certifies" the investment**
- An informational form (Form 8996) is completed and attached to the taxpayer's timely filed federal income tax return for the year in which the investment is made and annually thereafter
- This process appears to be very informal with no official IRS consent required for the Opportunity Fund investment

OPPORTUNITY ZONES

Open issues

- Whether and when investors can depreciate the investment that they have made in a QOZ; whether the exemption from gain on sale would avoid any recapture of those deductions
- Whether distributions of refinancing proceeds will cut against the investors having made a qualifying "investment" in the QOF
- The application of the requirement for "substantial improvement" to an operating business as compared to a real estate project
- Whether investors have to recognize interim capital gains incurred as a result of the sale of QOZ property by the QOF
- The so called "hotdog stand" deal, where one purchases land for $10M improved by a hotdog stand worth $50,000 and satisfies the substantial improvement test with an investment of another $50,000. Does this work?
- Whether the 31-month safe harbor included in the Proposed Regulations limits QOZ benefits to projects that are completed within that time, or just requires money to be spent within 31 months after it comes in
- What QOF actions lead to decertification?
- Can a QOF lend capital?
- Will states follow suit and provide QOZ benefits for qualified capital gains?

Opportunity Zones

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