

In The News

DFW Opportunity Zones Are Desired By CRE Market But Frustratingly Scarce

06.01.20

Bisnow

When opportunity zones hit the scene two years ago, Dallas-Fort Worth developers and investors envisioned the IRS-run program offering enough tax incentives to further invigorate DFW's already-flourishing commercial real estate market.

Instead, the program has had mediocre success in the region at best, prompting local officials and fund managers to question why North Texas landed so few designated zones when hundreds of local census tracts potentially qualified for the program.

"While there have been some participants and plays that have been involved with it, I think overall, people would say it's kind of been a disappointment," Hunton & Williams attorney J.R. England said. "We've seen a number of funds raise money, and some of them a significant amount of money; and they didn't really find either a sufficient number of deals or the deals weren't priced the way they wanted."

While no data is available to show just how many opportunity zone fund-backed deals have closed in DFW, multiple sources interviewed by Bisnow say the DFW area's engagement in the program is generally considered underwhelming, with many investors spending months confused on the particulars of the program and lacking opportunities in desired communities.

Interest in opportunity zone funds has picked up nationally in the last few months as investors have sought a safe place to put their capital amid pandemic-driven economic disruption, making the OZ program's substantial tax benefits more appealing. Even in Dallas, investors started showing more interest in opportunity zone deals, but experts say there is no indication that interest has led to solidified real estate plays.

"We are seeing an uptick in calls, not only from folks that haven't found deals yet to invest in but also folks who were initially invested in other funds for ... other businesses, and those businesses fell through for whatever reason," opportunity zone fund 3LB Equities principal Adam Smith said.

Those looking in DFW for real estate deals had a limited number of opportunity zone tracts to choose from. Of the 8,700 opportunity zones designated nationwide, the Dallas-Fort Worth Metroplex is home to just 52, with 18 tracts in Dallas County, according to CoStar data. Comparatively, the city of Houston alone has 99 designated zones, with 150 in Harris County, according to the city of Houston.

"When you do an analysis of the number of qualifying census tracts in the state of Texas and the number of qualifying census tracts in Dallas, we didn't actually get the proportion of census tracts that we should have if you just look at it statistically," Munsch Hardt attorney and shareholder Phillip Geheb said.

Geheb works on DFW opportunity zones primarily from the perspective of developers and estimates a few hundred additional DFW tracts could have qualified for the program.

Developers lobbying at the state level had more to do with what neighborhoods landed in designated opportunity zones than the pure economic qualifications of a given area, a Dallas Morning News investigation this year found.

DFW's opportunity zones, rather than being spread across the Metroplex in under-recognized areas, are mostly congregated in parts of Downtown Dallas and nearby areas already subject to gentrification and developer interest. The Federal Reserve Bank of Dallas, as well as many critics of the program, raised red flags about the program's limitations in addressing economic development without fueling gentrification.

Aside from the already-popular Dallas neighborhoods of Cedars and Deep Ellum, many designated North Texas tracts have yet to attract a compelling amount of investor and developer interest, Geheb said.

"It's not a very deep incentive like some other community development programs," Geheb said of the OZ program. "At the end of the day, what is going to accelerate are census tracts where there is a lot of activity and something that is really ready to go. It's not going to incentivize projects that may be more of a long shot."

"While the tax benefits can help, they are often seen as the icing on the cake," CoStar Director of Market Analytics Paul Hendershot said. "Quite frankly, there has been no dramatic uptick in the number of deals taking place in many of these areas after being designated opportunity zones."

3LB Equities has been looking within a 40-mile radius of Dallas-Fort Worth for opportunity zone multifamily development projects to invest in. The company is considering a multifamily project in Cleburne, Texas, but Smith laments the fact that more rural and suburban areas with economic development needs failed to secure OZ designations.

"As you get closer into the opportunity zones that are within Dallas-Fort Worth proper, I think Tarrant County really got the short end of the stick on any type of zones there," Smith said.

More rural areas primed for different types of industrial or multifamily development in the Denton County area, including the cities of Justin and Decatur, also were left out, he added.

"I wish there were more opportunities right here in our own backyard," Smith added.

Plano City Director of Special Projects Peter Braster said the state of Texas chose the zones with no input from the cities. Plano has a 1980s shopping mall for sale inside its sole opportunity zone.

Plano is generally pleased with its zone east of Interstate 75, but because of how the program was rolled out, Braster said he believes the IRS initiative does little to help the city spur development in existing areas that don't have the benefit of built-up Tax Increment Reinvestment Zone funds or other incentives created over time.

"Cities like Plano are already at a disadvantage by not being able to use their 4A/4B dollars [money collected as part of local sales taxes] for economic development," Braster said. "That really only leaves [tax increment reinvestment zones] and [public improvement districts] as economic development tools. In the case of TIRZ, which only generate funds in the latter years, the opportunity zone would have to be in a long-standing TIRZ for a city to use the tool to great advantage. On the other hand, a PID could generate funds in the near term via bonds, but they are limited to public infrastructure and would put an additional levy on the property. That levy could potentially negate any gains realized by the opportunity zone."

To help cities develop the appropriate incentives to complement opportunity zones, Braster recommends that any future extensions of the program should include enough notices for cities to build up economic stimulus prior to the opportunity zone fund rollout.

"I would suggest the state nominate the next round of OZ soon, so cities could begin TIRZ to be ready on day one of the next term," he said.

The White House and lawmakers are looking at the possibility of extending the deadlines for opportunity zones to create more stimulus in deprived communities, NPR reported.

But what DFW observers like Geheb say is really needed is a congressional move that would allow the governor's office to expand the number of designated tracts in Texas and DFW in particular.

"Many areas were right on," said developer Sam Ware, who applauds the program's potential. "[But] lots of areas were totally left out. [They] need to revisit and redefine what the end result is ... and areas that need to be designated."

On the other hand, more sites may not really be the answer.

"As far as the expansion or increasing the areas in Dallas to attract additional investment, I don't believe an opportunity zone can serve as the magic bullet of development," Hendershot said. "If a deal does not pencil outside of an opportunity zone, chances are it won't work inside an opportunity zone."

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Primary Contacts



Phillip Geheb

Dallas
214.855.7560
pgeheb@munsch.com

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