OPPORTUNITY ZONES 101

What Are “Opportunity Zones”?
The 2017 Tax Cuts and Jobs Act established Opportunity Zones to encourage investment in low- to moderate-income communities through Qualified Opportunity Funds, fueled by tax incentives. This provision is based on the bipartisan Investing in Opportunity Act (S. 1639) introduced by Senator Cory Booker (D-NJ) and Senator Tim Scott (R-SC). Given the significant interest among investors, it is possible that this new incentive could attract hundreds of billions of dollars in private capital, making it one of the largest economic development initiatives in U.S. history.

• 52.3 million Americans live in economically distressed communities. Between 2000 and 2015, more than half of these communities experienced a decline in both jobs and businesses.
• From 2010 to 2016, three-quarters of net job growth occurred in a narrow selection of metropolitan areas, resulting in inequalities across the country.
• 67% of job growth comes from small businesses, for whom the most important variable for success is access to capital.

This legislation offers potential to significantly increase jobs and accelerate wealth creation in areas that most need it by unlocking some of the nation’s pool of unrealized capital gains, which are estimated to be more than $6 trillion.

What is a Qualified Opportunity Zone?
A census tract which has been designated by each state or territory, and certified by Treasury, as eligible to receive private investments via Qualified Opportunity Funds.

A census tract can be designated as a Qualified Opportunity Zone if it falls into one of two categories:

• It satisfies the definition of a “low-income community” (LIC) in § 45D(e) of the U.S. Code.
• It is a non-LIC tract that is contiguous with an LIC designated as a Qualified Opportunity Zone and the median family income of the non-LIC tract does not exceed 125 percent of the median family income of the contiguous qualified zone.
More than 8,700 Opportunity Zones have been designated across all 50 states, the District of Columbia and 5 U.S. Territories. Once certified, an Opportunity Zone retains its designation for 10 years.

**What is a Qualified Opportunity Fund?**

An investment vehicle set up as a partnership or corporation for the purpose of investing in eligible property that is located in an Opportunity Zone. Qualified Opportunity Funds are capitalized by realized capital gains and must deploy 90 percent of capital into Opportunity Zones.

Investing in Opportunity Funds may provide potential tax incentives to investors:

- A temporary capital gains tax deferral for all capital gains reinvested in an Opportunity Fund, lasting until the investment is sold or December 31, 2026, whichever is sooner.
- A 10 percent basis adjustment on the original capital gains, which can result in tax reductions if the Opportunity Fund investment is held for 5+ years; plus an additional 5 percent adjustment if the investment is held for 7+ years.
- If an investor holds the Opportunity Fund investment for 10+ years, the investor also may permanently avoid capital gains taxes on any proceeds from the Opportunity Fund investment itself.
The Opportunity Zone Players

GOVERNMENT

- Easing local regulatory barriers
- Develop incentives to attract and build OZ projects
- Ensure project pipeline is fully fledged out
- Key Players: US Department of Treasury, HUD, State Governors, State Governments, Local Governments

BANKS

- Providing complimentary debt financing in Opportunity Zones
- Key Players: JP Morgan Chase, Wells Fargo, Citi, Bank of America, Morgan Stanley, Credit Suisse, Goldman Sachs

PRIVATE CAPITAL

- Investing equity capital through received capital gains
- Developers investing in low income areas, with the benefit of a tax incentive
- Key Players: High Net Worth investors, Family Offices, Developers, Corporates

NONPROFITS & PHILANTHROPY

- Enable community engagement to stabilize and sustain struggling neighborhoods
- Address community specific needs by supporting efforts at the local level
- Partner with public and private entities
- Seed initiatives that encourage and leverage private capital investment
- Key Players: Milken Institute, CalOZ, Economic Innovation Group, Cal FWD, LISC, Enterprise Community Partners, Kresge Foundation, Rockefeller Foundation, Governance Project, Accelerator for America, EJF Philanthropies, Parker Foundation
Opportunity Zones as a Tool for Economic Development
Milken Institute State Approach Framework

1. Establish a Community Finance/OZ Reporting Framework
   • Defining standards and tangible metrics of community benefits alongside a system of data collection, analysis, evaluation, and reporting to assess the effectiveness of OZs in meeting community development goals.

2. Provide Technical Assistance
   • Provide local jurisdictions with needed capacity: (1) Coordinate with state/local community partners and investors in forming OZ prospectuses, (2) Measure local assets, (3) Prepare potential projects in reaching shovel-ready status, (4) Provide information on state/local resources.

3. Identify State and Local (Regulatory) OZ Project Inhibitors
   • What are we willing to compromise on (i.e., local labor, land use, tax, environmental regulations) in order to direct private capital investments in realizing returns in tangible community benefits (i.e., affordable housing, jobs/business formation, social infrastructure and resiliency)?

4. Insulate Local Deal Flow
   • How do we retain community benefit once the OZ timeline expires (i.e. mitigate risk and insulate local/state regulations)?

5. Align Financial Toolkit and Incentives to Accelerate Community Development and OZ Project Pipeline
   • How do OZs fit with other community finance tools (i.e., value capture models, public private partnerships, etc.)?

6. Support a Regional Call for Projects
   • TA-style “Race to the Top” prepositioned with state standards and incentives, as well as strictly defined guidelines for local compliance (e.g., “if you have ABC and X amount of jobs, you will get priority”)
Policy Brief: How Can My City/Community Take Advantage of Opportunity Zones?

From Transactions to Transformation: How Cities Can Maximize Opportunity Zones

By Bruce Katz and Evan Weiss, in partnership with Accelerator for America

The broad objective of the Opportunity Zone incentive – expanding economic opportunities for places and people left behind -- cannot be achieved by the market and outside investors alone. Cities in the broadest sense – local governments, urban institutions, networks, and civic leaders -- will need to act decisively if Opportunity Zones are to engender not only a large volume of individual transactions but broader growth that is inclusive, sustainable and truly transformative for each city’s economy. The promise of Opportunity Zones is not just to match private capital to investable projects but to inspire cities to reexamine and rediscover the fundamentals of economic development for all by channeling the resources of their own communities. Cities who are able to coordinate and focus investment will drive not just growth in the near term but institutional and financial reforms that will reposition cities for success over the long haul.

The new incentive differs from other federal tax incentives in several ways. First, it is more market driven; it does not use a federal or state agency to distribute the incentives but rather relies on the decisions of individual investors and fund managers, meaning local governments will likely not be even aware of most Opportunity Zone investments in their communities. Secondly, it can be used for a wide variety of projects -- residential, commercial, industrial, infrastructure – rather than being restricted to a relatively narrow purpose like low-income housing or historic preservation. Third, there are no requirements for investors to ensure a certain outcome, such as job creation or local financial matches. Finally, there is no cap on the amount of the benefit if regulations are followed.

The federal law governing the Opportunity Zone incentive does not provide any guidance on the role of cities, yet city governments and other local entities can shape markets and maximize economic and social outcomes by smartly deploying their complex set of powers, resources, assets and relationships. Cities, unlike the federal government and state governments, are networks of institutions and individuals that can “think like a system and act like an entrepreneur.” In this way, cities are primed to aggregate and align public, private and civic capital for
strategic investments in economic development, schools and skills, infrastructure and affordable housing, the critical ingredients for long-term inclusive growth.

Since the Opportunity Zones incentive was introduced, two dominant, overly simplistic narratives have taken hold. On one hand, there is the view that all cities should merely compile and bundle a list of investable projects and reveal the true strength of the market for some distant investor on Wall Street or in Silicon Valley. This perspective treats the market failure that Opportunity Zones was intended to resolve as one primarily involving information and marketing rather than underlying business demand and economic realities. On the other hand, there is fear that Opportunity Zones will put gentrification on steroids, spiking housing prices and displacing residents. This perspective assumes that the principal challenge facing all cities is excessive value appreciation rather than poverty, high vacancy and low demand.

This policy brief advocates for a more balanced approach that reflects the market variance and complexity within and across cities, organized around Seven Principles to guide city analysis and strategy for leveraging newly established Opportunity Zones. The principles are designed both to enable cities to further capital investment in traditionally disadvantaged places in order to spur job creation and broader opportunities — the core objectives of this new tax incentive — as well as sharpen local strategies and modernize the institutions that design and deliver those strategies. To actualize these principles, we offer 10 Steps to leverage local advantages, knowledge and experience to fully realize the economic and social potential of this unique tax incentive.

**Seven Principles**

**Principle One:** See the big picture. Investors naturally focus on the merits associated with individual transactions or financial products. Cities, by contrast, can think about impacts beyond the tradeoffs involved in a particular transaction to advance systemic goals, like enhancing the public sector’s fiscal capacity or strengthening the regional economic ecosystem. Cities should create the conditions for long-term growth rather than chase capital for short-term outcomes.

**Principle Two:** Act as networks, not as governments. Cities are more than governments and elected officials. They’re networks of institutions and leaders who
co-produce the economy and co-govern many aspects of urban life. Maximizing the potential of Opportunity Zones requires the full engagement of different sectors and stakeholders who can leverage their collective assets and align their decisions.

**Principle Three:** Identify the distinctive competitive assets and advantages of Opportunity Zones. To reduce friction in the market, cities should be an engaged, reliable source of intelligence about their overall economies and each of their Opportunity Zones. Each city should be able to state definitively what gives disparate Opportunity Zones their market traction and potential.

**Principle Four:** Balance rewards and controls, incentives and protections. Opportunity Zones are a market driven incentive; most cities won’t know how much or where Opportunity Fund investments have been made. Cities can use public resources to steer market investment, particularly towards historically disadvantaged areas. Cities should ensure that every Opportunity Zone is included in a citywide inclusive zoning, procurement, and development policy that focuses on residents and require data transparency for deals that receive public subsidy.

**Principle Five:** Structure strong, inclusive partnerships. Opportunity Zones could catalyze the aggregation of smart public, private and civic capital for a positive, compounding effect. Smart public and civic investments in community infrastructure and human capital can provide a platform for private sector investment. In low-demand Opportunity Zones, smart public, private and civic financial instruments can attract and de-risk tax advantaged capital.

**Principle Six:** Link market investments to investments in human capital and other strategies that maximize impact for lower income residents. Cities have a unique potential, given the localization of many schools and skills institutions and initiatives, to focus on human capital by giving students and residents who live in or near Opportunity Zones the ability to access existing and future employment opportunities. Cities can go further and drive inclusive growth through supporting minority owned businesses, homeownership, affordable housing and neighborhood amenities.

**Principle Seven:** Use Opportunity Zones as a catalyst for modernizing local institutions. In many communities, fragmented local governments simply do not have the capacity or professional expertise to design, finance and deliver sophisticated market and social initiatives. On the private and civic side, most
communities collaborate through loosely organized informal networks that do not have sufficient capital or capacity, or with a scope too limited to drive sustainable broad impact. Cities should use Opportunity Zones as a vehicle for modernizing and redefining their institutions to act with purpose and discipline to maximize economic, social and environmental impact.

**Ten Steps**

**Step One: Design and market an Investment Prospectus to showcase the distinctive assets of -- and investable projects in -- a city’s Opportunity Zones** – Set the context of the regional market, offer detail on local organizations and projects, and the advantages of individual opportunity zones through a marketing tool with a strong, cohesive narrative.

**Step Two: Maximize the economic impact of anchor institutions, particularly institutions of higher learning** – Spread the word to community anchors about Opportunity Zones and seek to understand their needs that the incentive might meet; encourage their own formation of Opportunity Funds or to serve as a clearinghouse for potential investors and projects.

**Step Three: Maximize the economic impact of publicly owned assets** – Ensure each public entity’s assets are widely known and easily identifiable; agencies should use their own property holdings to shape and incentivize markets to serve the broader public as part of a city-wide strategy.

**Step Four: Accelerate employment density, business demand and smart place-making** - With careful rezoning and planning, cities can spur the co-location of corporations, university assets, start-ups and scale-ups, driving the enhancement of commercialization and tech transfer efforts in ways that support the regeneration and animation of public and private spaces.

**Step Five: Ensure that Opportunity Zone related infrastructure is high quality and meets performance and sustainability standards** – Cities should market their infrastructure, including freight rail, wastewater, and storm water investments, and align tax increment financing opportunities from Opportunity Zone investment to ensure project and community infrastructure is high quality and meets performance and sustainability standards.
Step Six: Align city investments, procurement, tax preferences, zoning, and other decisions with the distinctive competitive assets of each Opportunity Zone — Available local incentives should be well-publicized and easily accessible to potential investors to determine eligibility; cities can also use incentives as regulators to monitor Opportunity Zone investments. Fast tracking entitlements, given the time limitations of the Opportunity Zone incentive, offers a significant competitive edge.

Step Seven: Support local entrepreneurs and developers (particularly female- and minority-owned businesses) gain access to capital, technical assistance, mentoring, legal services and other resources — Spur inclusive growth through a legal and financial entrepreneurship clinic to help community members gain access to capital and technical assistance, including mentoring, legal services and other resources, to support citywide inclusionary development and purchasing policies.

Step Eight: Help local residents obtain the skills or competencies necessary to meet existing or future labor demand — Work closely with local school districts to create “cradle-to-career initiatives” and better link anchor employers to workers; cooperation should be incentivized.

Step Nine: Support the production and preservation of affordable/workforce housing — Maximize impact of existing housing institutions and intermediaries and leverage other tax incentives that support housing, such as Low-Income Housing Tax Credits and New Markets Tax Credits.

Step Ten: Repurpose existing institutions and build new institutions to carry out core missions — Understand existing institutions and explore new governance structures to create a suite of adequately-resourced modern institutions. Move quickly and get started by offering a front door to investors, a clear lead, and an engaged community.