Community and Economic Development in North Carolina and Beyond Blog: The Opportunity Zones Program

By CED Program Interns & Students

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In December 2017, Congress established a new community development program called "Opportunity Zones". This blog post will provide an overview of the program, subject to change as it evolves. The Opportunity Zones program is based on the bipartisan "Investing in Opportunity Act" but was enacted as a part of the Tax Cuts and Jobs Act in the 2017 tax reform efforts. The concept was initially created in 2015 by the Economic Innovation Group, in order to address persistent poverty and unequal recovery.

The program offers an incentive to inspire long-term private investment in low-income urban and rural communities across the country by allowing investors to utilize their unrealized capital gains by reinvesting into Opportunity Funds. Opportunity Funds will be dedicated to investing in the identified Opportunity Zones; these zones will be designated by the Governors of every U.S state and territory. Governors have 120 days from December 22, 2017 (March 21, 2018) to identify up to 25% of the total number of low income census tracts in their respective state or territory as opportunity zones. (North Carolina has requested an extension.) For the most part, the Opportunity Zone census tracts align with the qualified census tracts defined in the New Market Tax Credit (NMTC) program. Nevertheless, the governors must still identify low-income communities to receive Opportunity Zone Investments since up to 25% of census tracts can be designated.

The major draw of this program on the investor side is the federal tax incentive it offers. The program offers the following opportunities for investors[1]:

- *Temporary Deferral* for the capital gains that are invested into an Opportunity Fund.
- *Step-Up in Basis* for capital gains that are reinvested into an Opportunity Fund. The basis of the original investment is increased by 10% if the qualified opportunity zone fund is held for a least 5 years by the taxpayer, and that is increased by 5% for at least 7 years, and can exclude up to 15% of the original gain from taxation.
- *Permanent Exclusion from taxable income of capital gains* from a sale or exchange of an investment that is in a qualified opportunity zone fund held for at least 10 years.

Unlike other programs such as the Low-Income Housing Tax Credit (LIHTC) or the New Markets Tax Credit (NMTC), there is no authorized cap on the amount of capital that can be accessed through the opportunity funds and respective opportunity zone investments. The main source for these investments is the approximately $2.2 trillion of capital gains that are unrealized by individuals and corporations. These funds are essentially channels to pooled equity that will be used for equity investments into small business and real estate throughout distressed communities.

The critical challenge at the moment however, is the matter of selecting the Opportunity Zones for nomination by March 21 st

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. States may only nominate 25% of the number of Low-Income Communities within a state for this program. This means, if a state as under 100 Low-Income Communities, it can designate up to 25 Opportunity Zones. In this program, a Low-Income Community must meet at least one of the following requirements:

- The census tract has at least a 20% poverty rate
- The median family income in the tract is below a certain threshold (determined differently for rural vs. urban)
- The census tract's population is less than 2000 people and it is within an empowerment zone and is contiguous with another Low-Income Community

EIG recommends the appointment of a point person or agency that would lead the state efforts in Opportunity Zone nomination, as well as investor outreach and public engagement. Additional recommendations crafted by the Economic Innovation Group (EIG) include nominating census tracts that:

- Are poised to absorb private equity capital in a way that would help promote positive economic growth
- Are currently the focus of mutually reinforcing state/local/private development initiatives
- Have already demonstrated success in geographically targeted development programs
- Have recently experienced layoffs due to business closures or locations

Once Governor's submit their Opportunity Zone nominations, the Treasury must approve or provide feedback within 30 days of the governor's submission. Both entities can request an extension of up to 30 days. From the approval state, the Treasury has to certify Opportunity Funds, and although the process is still unfolding, many speculate that existing community development entities will provide the structure for certifying the Opportunity Funds. The statute does outline two qualifications – that the entity must be organized as a corporation or a partnership, and that they must invest a minimum of 90% of assets in Opportunity Zones. It is unclear if more requirements may be added or considered later on.

For more on how local governments can take advantage of Opportunity Zones, see Tyler Mulligan's post, Federal Opportunity Zones: What Local Governments Need to Know, and visit DFI's Opportunity Zone Resource Page.

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[1] Description of investor incentives taken from EIG – http://eig.org/opportunityzones

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