OPPORTUNITY ZONES: STATE STRATEGIES TO SUPPORT INVESTMENTS

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- Bipartisan, membership organization
  - Each of the 50 states and all territories
    - 7,383 state legislators
    - 30,000+ state legislative staff
- Research, education, technical assistance
- Mission:
  - Improve the quality & effectiveness of state legislatures
  - Promote policy innovation and communication among state legislatures
  - Ensure states have strong, cohesive voice in the federal system
WHAT DOES NCSL DO?

- Research
- State Legislatures Magazine
- LegisBriefs
- Invitational Meetings
- Information Requests
- Trainings, Webinars, and Testimony
- Legislative Summit
- Our American States Podcast
- Website: www.ncsl.org
Nine Standing Committees

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- Labor and Economic Development
- Law, Criminal Justice and Public Safety
- Legislative Effectiveness
- Natural Resources and Infrastructure
- Redistricting and Elections
Opportunity Zones

The potential for a new approach
What are Opportunity Zones?

• New **federal incentive** designated in the 2017 tax reform bill

• Incentive for investors to **support distressed communities** through **long-term, equity investments** in businesses and real estate ventures

• Incentive is **deferral, reduction and potential elimination of certain federal capital gains taxes**

• If properly executed, Opportunity Zones may help address a number of challenges in Colorado:
  • **Promoting economic vitality** in parts of the state that have not shared in the general prosperity over the past few years
  • **Funding the development of workforce and affordable housing** in areas with escalating prices and inventory shortages
  • **Funding new infrastructure** to support population and economic growth
  • **Investing in startup businesses** that have potential for rapid increases in scale and the ability to “export” outside the state of Colorado
Taxpayer Benefits

1. **Deferral** of capital gains tax until sale or Dec 31, 2026
2. **Partial reduction** of deferred gain
   - Tax basis increases by 10% if investment is held for 5 years
   - Tax basis increases by additional 5% if investment is held for 7 years
3. **No capital gains tax on appreciation** if investment is held for 10 years
How The Incentive Works

Roll Gains Forward
Roll gains of any kind, including gains from stock or real estate, into a qualified OZ investments. Unlike 1031 exchanges, only gains need to be rolled forward, allowing investors to extract their original basis.

Defer Taxes
Defer taxes on Gains realized today until 2026. This allows investing dollars that would otherwise be paid as taxes to increase your initial investment size, and ultimately your gains.

Reduce Taxes
If the investment is left in qualified OZ investments for 5 years, there is a 10% forgiveness of the 2026 bill. After 7 years, an additional 5% is forgiven for a total of 15% reduction in the deferred taxes due.

Eliminate Taxes
After 10 years, all gains made within the opportunity zone can be realized tax free. That’s 100% forgiveness of taxes for gains made in the OZ, resulting in as much as a 44% boost to returns.
Qualified OZ Fund

- Taxpayer has **180 days** to move gain into the OZ Fund
- Fund **must be a partnership or corporation** (LLC is allowed)
- Fund must be **90% deployed into Qualified Opportunity Zone Property**
  - This will be checked 6 months after Fund takes in capital and at the end of the taxable year
  - Safe harbor for reasonable working capital
  - Hoping that Treasury allows an additional grace period
- Declaration and deployment test will be self-certified and subject to audit – Draft IRS form 8996 was recently released
Local Concerns About the Incentive Persist

- Investment can drive displacement
- Investment can enable predatory actors
- Investment can go to projects that would have happened anyway
- National Funds and local projects potentially difficult to synchronize
The Policy Conversation Fuels Concerns

Communities are not “on the level” in the current conversation
Hurdles to Maximizing the OZ

Most municipalities face a combination of three hurdles to maximizing OZs for community development:

- Community anxieties about displacement risk/or being ignored
- Limited technical capacity or constrained resources
- Philosophical or political reluctance to drive development
Focus on bringing right parties together

Key early movement for community development in: Baltimore, Birmingham, Bethlehem, Columbia, Erie, Louisville, Norfolk. What do they have in common?

- Convene around local vision for specific project
- Engage local anchors, foundations & funders in projects
- City Hall is active driver of key catalytic projects
102 documented funds representing $23 billion of investing capacity

State of Investor Action
What Investors are doing

- Smaller and single-asset funds are ready
- Institutional investors & large foundations are still moving cautiously
- Some larger funds ($1bn+) are forming, but still in fund-raising phase
- Typologies to rate the investment-worthiness of places have developed
- Emerging series of platforms to facilitate investment (Opp sites and Opp Exchange)
- Is going on largely in parallel with (not always in conversation with) community development projects, unless driven by cities
What are early movers doing?

Foundation Support
What Foundations are doing

- Kresge & Rockefeller request letters of interested fund managers (151 reply)
- Offer to provide administrative support, training, guarantees, and potential loss coverage
- Local foundations are cautiously interested, but so far have only supported in a convening role
- Cautions because of: potential mission mis-alignment, uncertainty about supporting investor returns.
Market-Making in more detail

- **Risk Mitigation**: Many of the areas designated as Zones have a high degree of risk that the incentive does not correct for. Risk mitigation for mission-aligned projects – such as backstops – are a key leg of support.

- **Capacity Building**: Many communities and local governments in OZ areas lack the capacity to support a dedicated Opportunity Zone coordinator. Dedicating money or staff time to support local capacity is important to support transformative OZ projects.

- **Capital Stack  Support/direct sidecar investment**: OZ projects that support community benefits may not generate market-rate returns even with the incentive. Foundations – and philanthropic capital generally – can help fill financing gaps at lower returns for mission aligned projects.

- **Measurement & transparency support**: measurement is not currently required as part of the OZ program. Creating tracking requirements with philanthropic capital will allow evaluation of the program.
Be Hyper-local

The key through all of these?
What can Opportunity Zones facilitate if done well?

This work is pushing to public-interest developer model of local governance
Opportunity Zones can change local project development

Private Sector

- Understanding
- Project pipeline
- Strategic concessions

Public Sector
Example: Birmingham’s American Life Building

Symbolic Building
The American Life Building’s 30-year vacancy was a sign of the city’s decline.

Birmingham Inclusive Growth Fund
Partnership with PNC bank, city hall, local investors, and community members.

Workforce Housing +
Will be 140 units between $700 - $1,200 per month, with 5 set aside for non-profit for formerly incarcerated individuals.
Takeaways from the state of the market:

1. Substantive capacity support is required to overcome key hurdles. But we know what to do and where we’re going.

2. Business investment is still slow moving.

3. Cities best prepare by advancing projects that meet some understood, specific, local need and keep critical stakeholders (community, local government, foundations, developers, investors) active and engaged.
THANK YOU

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Questions?

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This webinar will be archived and available on NCSL’s website:

Additional resources from The Pew Charitable Trusts: