Opportunity Zones

By Sarah Brundage, Senior Policy Director, Enterprise Community Partners

Administering Agency: U.S. Department of the Treasury

Year Enacted: 2017

Number of Persons/Households Served: There are 8,700 certified Opportunity Zones nationwide, encompassing 35 million people.

Population Targeted: Low-income census tracts with an individual poverty rate of at least 20% and median family income no greater than 80% of the area median income (AMI). Each state, territory, and Washington, D.C. was eligible to nominate up to 25% of its total eligible census tracts. Up to 5% of that 25% could be comprised of contiguous census tracts that are adjacent to a low-income community as long as the adjacent census tracts had a median family income that did not exceed 125% of the median family income of the adjacent low-income community.

The Opportunity Zones tax incentive is designed to drive long-term equity capital in a diverse range of activities in designated low-income census tracts.

HISTORY

The Opportunity Zones tax incentive was originally conceptualized in the "Investing in Opportunity Act." This bipartisan, bicameral legislation was sponsored by Senators Tim Scott (R-SC) and Cory Booker (D-NJ) and Representatives Pat Tiberi (R-OH) and Ron Kind (D-WI) in the 115th Congress. The law was enacted as part of the "Tax Cuts and Jobs Act" in December 2017.

PROGRAM SUMMARY

The Opportunity Zones tool is technically not a program, but a tax incentive. The Treasury has certified 8,700 Opportunity Zones; these are low-income communities and adjacent census tracts that are now eligible to receive private investment through Opportunity Funds.

Opportunity Funds are a new private sector investment vehicle that must invest at least 90% of its assets in qualifying Opportunity Zone businesses and/or business property. There are three tiers of tax incentives to encourage taxpayers to invest capital gains into a Qualified Opportunity Fund:

- A temporary tax deferral for capital gains reinvested in an Opportunity Fund. The deferred gain must be recognized on the earlier of the date on which the Opportunity Zone investment is sold or December 31, 2026.
- A step-up in basis for capital gains reinvested in an Opportunity Fund. The basis of the original investment is increased by 10% if the investment in the qualified Opportunity Zone Fund is held by the taxpayer for at least five years, and by an additional 5% if held for at least seven years, excluding up to 15% of the original gain from taxation.
- A permanent exclusion from taxable income of capital gains from the sale or exchange of an investment in a qualified Opportunity Zone fund, if the investment is held for at least ten years. (Note: this exclusion applies to the gains accrued from an investment in an Opportunity Fund, not the original gains).

Certain activities, known as "sin businesses," are not eligible for Opportunity Fund investments. These include operating a country club, golf course, massage parlor, hot tub facility, suntan facility, racetrack or other gambling facility, or liquor store. Other than these prohibited items, eligible investments opportunities are broad and flexible.

FUNDING

The Opportunity Zones tax benefit is not funded through federal appropriations; it is a tax expenditure, meaning that the federal government forgoes tax revenue in order to incent an activity. The Joint Committee on Taxation estimates that Opportunity Zone tax expenditures will total $16.9 billion over the course of 2019 through 2023. Recent estimates suggest that upwards of $6 trillion in unrealized capital gains currently sit on the books of U.S. taxpayers.

FORECAST FOR 2020

The Department of the Treasury and Internal Revenue Service (IRS) released the final regulations in December 2019. The regulations combine and update the prior two tranches of proposed regulations (previously released in October 2018 and April 2019). The final regulations are expected to be effective after March 13, 2020. The final regulations provide technical clarification for stakeholders interested in making Opportunity Zone investments and/or managing a Qualified Opportunity Fund.

However, the final regulations do not directly address the broader concerns from low-income community advocates about the potential consequences of these private investments. There are no provisions in the statute nor final regulations specifying that investments must benefit low-income people, build affordable housing, employ low-income residents, or provide affordable capital for local small businesses or minority-owned or women-owned businesses. Nor are there protections to prevent the displacement of low-income people or local small businesses as a result of new investments in distressed communities. Also not included in the final regulations are data collection and reporting requirements that would allow Opportunity Zone stakeholders to assess the outcomes of the new tax incentive.

The Opportunity Zone legislation requires investments to be made by December 31, 2019 to be eligible for the maximum 15% reduction in capital gains for holding investments seven years. While there is currently no single, comprehensive log of Opportunity Funds and investment activity, several third-parties have created resources to collect volunteered investment information. As of December 2019, the National Council of State Housing Agencies' (NCSHA's) Opportunity Zone Fund Directory listed 196 funds representing nearly $45 billion in anticipated investments. NCSHA's directory estimates that 64% of the funds plan to invest in affordable or workforce housing or community revitalization. The Novogradac Opportunity Funds Listing is tracking 366 funds, representing $65.77 billion in community development investment capacity, with nearly $4.5 billion raised as of December 2019. Opportunity Zone investments will continue in 2020.

Meanwhile, the administration will likely continue to propose and implement incentives to prioritize Opportunity Zones through other federal policies and programs. President Trump signed an Executive Order on December 12, 2018 establishing the White House Opportunity and Revitalization Council chaired by HUD Secretary Ben Carson. The primary purpose of the Council is to target existing federal programs to Opportunity Zones. The Council will assess actions each federal agency can take under existing authorities to focus federal programs in Opportunity Zones. It will also assess actions each agency can take to minimize regulatory and administrative costs. As of December 2019, the White House Opportunity and Revitalization Council has identified more than 190 federal programs that could target or provide preference or additional support to Opportunity Zones. As of December 20, 2019, the Council has already taken action on 183 grants or programs, which are detailed in a public memo on completed program targeting actions.

In November 2019, three bills were introduced in Congress that would tighten the statute that created Opportunity Zones. These bills S. 2787, H.R. 5042, and H.R. 4999, were introduced by Senator Ron Wyden (D-OR), and Representatives James Clyburn (D-SC) and Hank Johnson (D-GA), respectively. All together they would limit the Opportunity Zone tax benefit associated with any housing projects to those occupied by either very-low or extremely low-income residents, remove census tracts that are not low-income from an Opportunity Zone, require advisory boards appointed by local elected officials, and require some diversity in investment. A fourth bill (H.R. 5252) introduced by Representative Rashida Tlaib (D-MI) would repeal the provision in the Internal Revenue Code authorizing Opportunity Zones.

WHAT TO SAY TO LEGISLATORS

Opportunity Funds should be required to report on their investment activity to ensure accountability of federal resources. The "Investing in Opportunity Act" included language requiring the Treasury Department to report on the impacts and outcomes of Opportunity Fund investments; however, when the tax incentive was ultimately enacted as part of the "Tax Cuts and Jobs Act of 2017," reporting requirements were not included.

Since the Opportunity Zone tax incentive was enacted, Enterprise has been urging Congress and the Administration to commit to reporting public data on investments in Opportunity Zones. Enterprise believes that the Opportunity Zone tax incentive should be used to advance equitable and inclusive growth, and that an important part of assessing this new tax incentive is transparency and accountability through data and reporting requirements. Enterprise believes that the federal government must require public data collection and reporting on Opportunity Fund investments and outcomes, allowing Congress and the public to evaluate whether this new tax incentive is driving equitable investments.

In May 2019, Senators Cory Booker (D-NJ), Tim Scott (R-SC), Todd Young (R-IN), and Maggie Hassan (D-NH) introduced a bill, S. 1344, that would require the Secretary of the Treasury to collect data and issue a report on the Opportunity Zones tax incentive. Since then, several other related proposals have been introduced.

Advocates should urge Members of Congress to enact meaningful reporting requirements on Opportunity Zones investments, similar to those outlined in S.1344.

More broadly, any future opportunities to reform or modify Opportunity Zones should consider the impact on the designated low-income communities above all. If implemented with local needs and priorities in mind, Opportunity Zones have the potential to catalyze investments that revitalize distressed communities and connect local residents to opportunity. If implemented without a commitment to direct and sustained community benefits to existing low-income residents and businesses, there is a danger that local residents and businesses could be displaced if Opportunity Zone investments cause property values and costs of living to rise.

Successful implementation of Opportunity Zones should include many of the same best practices that the affordable housing and community development industry has developed over the past several decades. The Low-Income Housing Tax Credit and New Markets Tax Credit, two proven and effective tools that use a tax credit to encourage activity that otherwise would not occur, provide a model for successful public-private partnerships that benefit low-income residents.

A statutory requirement to collect and publicly report meaningful data on Opportunity Zone investments is the first critical step necessary toward strengthening the accountability and transparency of this new tax incentive.

FOR MORE INFORMATION

Enterprise Community Partners, 202-649-3410, www.opportunityzonesinfo.org

The IRS Opportunity Zone webpage, https://bit.ly/2Etzdce