Massachusetts

Opportunity Zones Overview

An affiliate of LISC
NMSC
New Markets Support Company

LISC
Helping neighbors build communities

National Equity Fund INC
an affiliate of LISC

What are Opportunity Zones?

The Opportunity Zone tax incentive is a bipartisan initiative to spur long-term private investment in low-income urban and rural communities, established by Congress in the 2017 **Investing in Opportunities Act**.

Up to 25% of LICs in a U.S. state or territory may be designated as OZs.

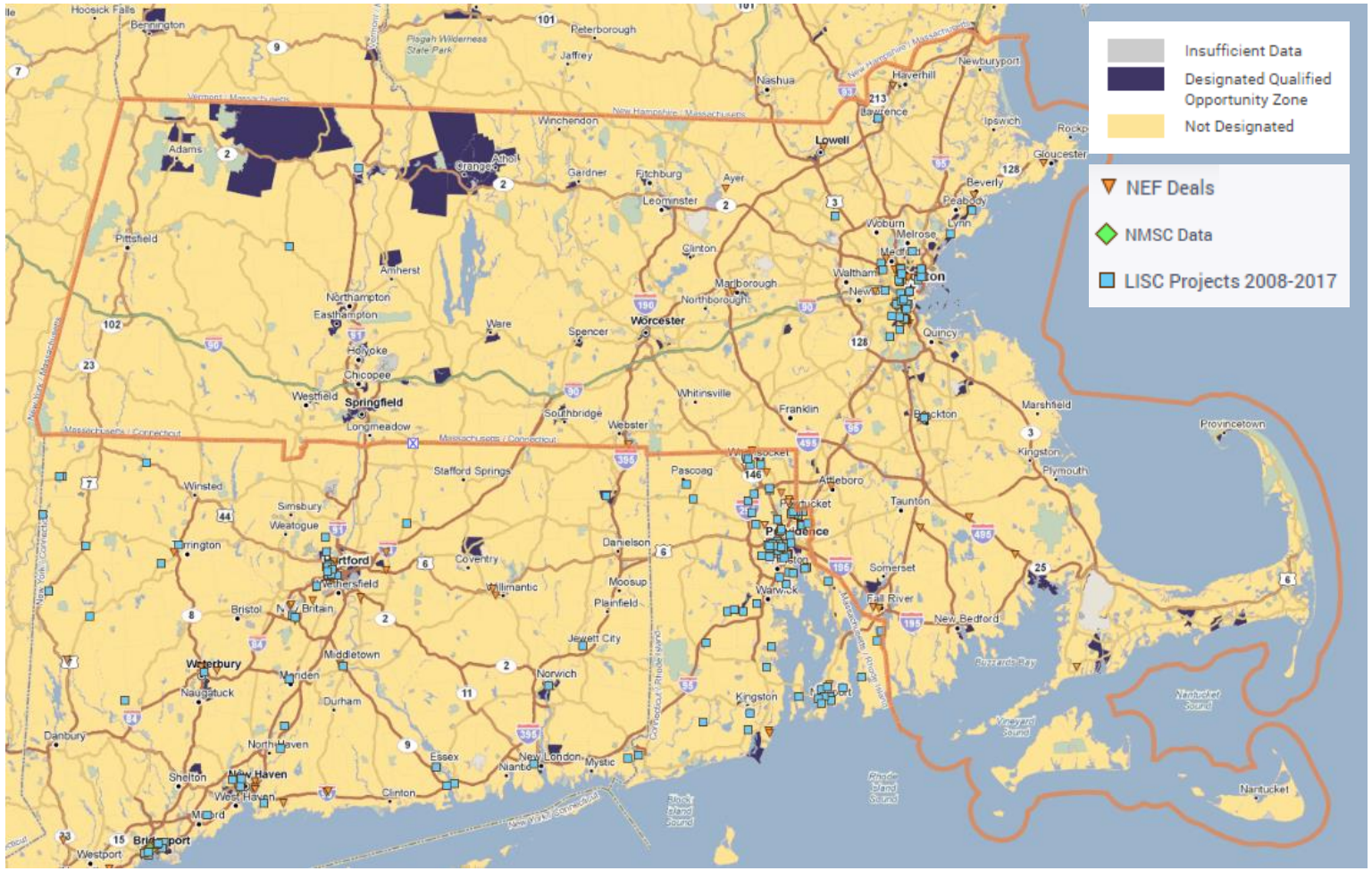
States or territories in which there are fewer than 100 LICs may designate up to 25 LICs as OZs.

Up to 5% of census tracts contiguous to LICs may be designated as OZs, if the median family income of the census tract does not exceed 125% of the median family income of the LIC to which the tract is contiguous.

Opportunity Zone: A low-income census tract **(LIC)**, as determined within New Markets Tax Credits legislation, is designated as an Opportunity Zone **(OZ)** by the governor of the of the state or territory in which it is located. Designations will stay in place for 10 years.

OPPORTUNITY ZONES

Massachusetts Designations



138

census tracts designated

79

municipalities

Rural census tracts	7
Average poverty rate	26.2%
Average unemployment rate	12.4%
Average family income in OZ census tracts relative to area median income (AMI)	53.1%

18% Rural

48% Gateway Cities

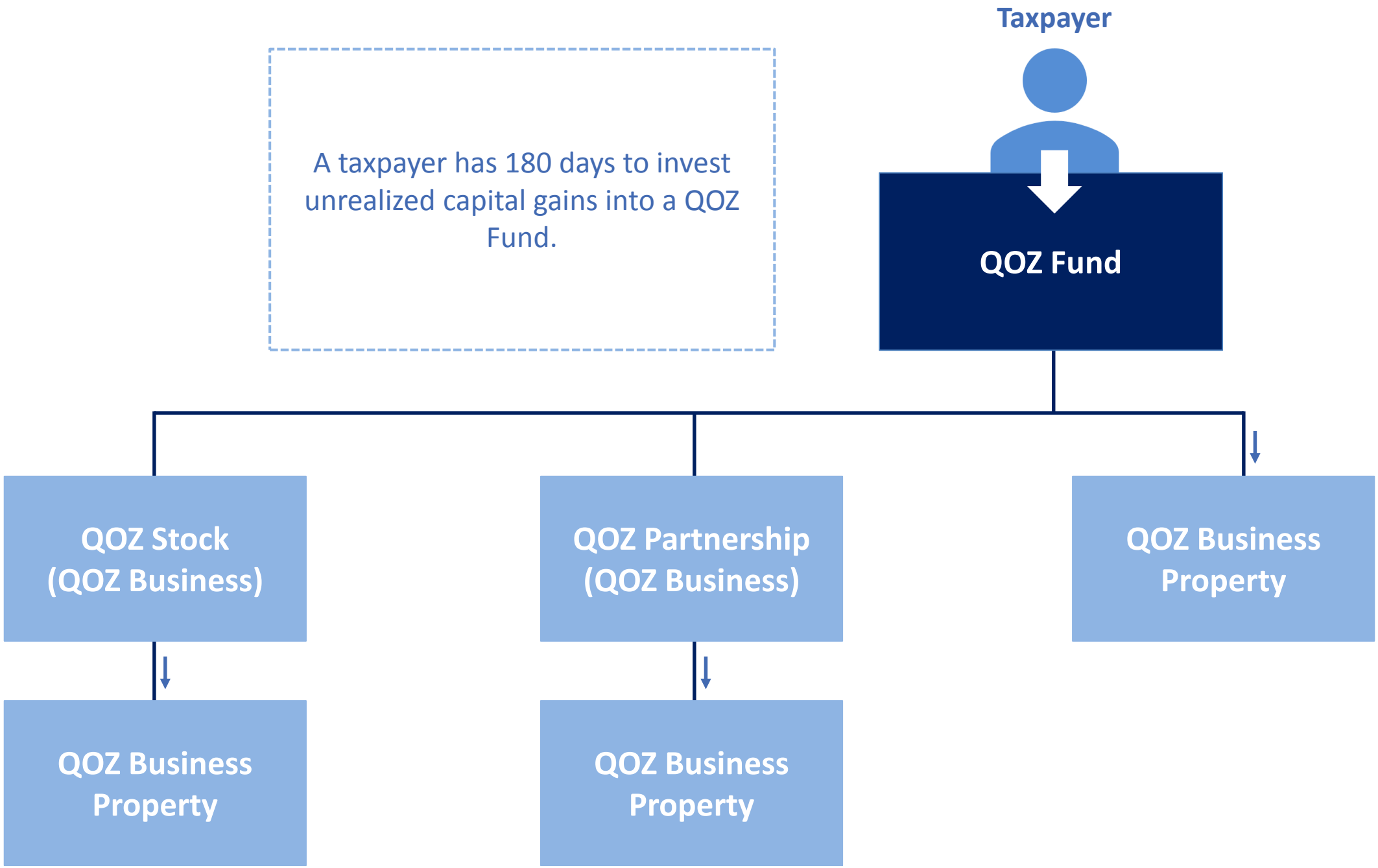
Definitions

Opportunity Fund: An investment vehicle organized as a corporation or partnership for the purpose of investing in Opportunity Zone property.

Opportunity Funds will be self-certified per IRS guidelines. They must be organized for the purpose of investing in Opportunity Zones

Opportunity Funds are required to invest 90% or more of their capital as EQUITY in Opportunity Zone property

Opportunity Zone property includes stock, partnership interest, or business property in an Opportunity Zone


Taxpayer
A taxpayer has 180 days to invest unrealized capital gains into a QOZ Fund.
QOZ Fund
QOZ Stock (QOZ Business)
QOZ Partnership (QOZ Business)
QOZ Business Property
QOZ Business Property
QOZ Business Property

OPPORTUNITY ZONES

Investor **Incentives**

Deferral of taxes

On capital gains invested in Qualified Opportunity Zone Funds

Reduction of taxes

On investments held in Qualified Opportunity Zone Funds 5+ years

Cancellation of taxes

On new gains made through Qualified Opportunity Zone Fund investments held 10+ years

Timeline for Opportunity Zone Investments

	Investment Year 2018	Year 5 2023	Year 7 2025	Year 8 2026	Year 10 2028
Tax on Capital Gain Invested	Gain realized and invested in Opportunity Fund within 180 days*	10% reduction of capital gains tax	15% reduction of capital gains tax	All taxes due on 12/31/26. Investor pays tax on 85% of original gain	
Tax on Opportunity Fund Investment		Any gain realized on Opportunity Fund investment is fully taxable if liquidated	Any gain realized on Opportunity Fund investment is fully taxable if liquidated	Any gain realized on Opportunity Fund investment is fully taxable if liquidated	Any gain realized on Opportunity Fund investment is tax free**

*** Tax is deferred until the earlier of investment liquidation (return of capital) or 12/31/26**

**** Any appreciation on Opportunity Fund investment is tax free if held > 10 years**

Key Points

Investors

- Tax incentive is most valuable for 10 year investments in appreciating assets
- Six months to invest after realizing a capital gain
- Another six months to deploy 90% of capital in Zones
- Capital is required to be an equity investment – loans from investors are not eligible for the tax incentive

Funds

- All capital must flow through an Opportunity Fund to be eligible for the tax incentive
- Funds are self-certified via an IRS tax form
- Fund must be established for the purpose of investing in Opportunity Zones
- 90% of fund assets must be invested in Zones to maximize the tax incentive

Eligible Investments

- Must be equity investments
- Real estate investments must include substantial rehabilitation – doubling basis within 30 months
- “Sin businesses” are not eligible
- Other requirements include property use in “active conduct of business” and limits on assets held in cash

Ex. 10 Year Investment: **Fully Taxable vs. Opportunity Zone Fund**

Assumptions:

- 10% annual investment appreciation
- 24% capital gains tax (federal only)

Fully Taxed Investment		
Capital Gain		$100,000
- Tax payable (24%)		$24,000
Total Capital to Invest		$76,000
Sales Price after 10 years		$197,000
- Tax on Appreciation (24%)		$29,070
After Tax Funds Available		$168,054

Opportunity Zone Investment		
Capital Gain		$100,000
- Tax payable		$0
Total Capital to Invest		$100,000
Sales Price after 10 years		$259,374
- Tax on Appreciation		$0
Deferred Capital Gain Tax (24%) paid in 2026		$20,480
After Tax Funds Available		$238,974

Eligible **Investments**

Only equity investments are eligible for the Opportunity Zone tax incentive.

1. **Business investments**

   can include investments in new stock issuance for corporations and ownership interests in partnerships and LLCs.

2. **Investments in real estate**

   must include an ownership interest of new construction or assets that will be **"substantially improved"** within 30 months of acquisition by the Opportunity Fund.

3. **New equipment and other assets**

   are also eligible investments.

Strengths

Local	Flexible	New Investor Class	Potential	Straightforward
Designations are made by states and localities, rather than Federal agencies, ensuring more local buy in and coordination.	The flexibility of the investment tool can support investments in any type of asset class.	The incentive has the ability to attract high net worth individual investors to community development finance.	The incentive could attract hundreds of billions of private sector capital into low-income communities (compared with about $10 - $12 billion annually under LIHTC and $3.5 billion annually under NMTC).	The tool is relatively straightforward from an investment and compliance standpoint, in comparison to LIHTC and NMTC.

Potential Concerns

Lack of Oversight

Lack of oversight from government entities could lead to program abuses.

Lack of Impact Incentives

Incentives focus on back-end returns, rather than investments that will result in community impacts.

Gentrification and Displacement

The tool might aid in the gentrification and displacement of residents and businesses in Opportunity Zone communities.

Future of Other Tax Incentives

The new incentive might be used as an excuse to diminish or eliminate other community development tax incentives, such as the NMTC program.

Economic Development Examples

1. **Business infrastructure real estate funds:**
   - *Industrial*
   - *Retail*
   - *Mixed use*
   - *TOD*

2. **Venture capital funds:**
   - *Seed stage investments*
   - *Series A investments*

3. **Operating business private equity:**
   - *Businesses moving or expanding into an Opportunity Zone*
   - *Equipment financing*

4. **Enhancement for other federal tax credit transactions:**
   - *NMTCs*
   - *Historic Tax Credits*

Sample Economic Development Deal

Office Supply Company

New office development for a minority-owned business creating 80 quality, accessible jobs for community residents

Type	Amount
Bank Debt	$8.0 MM
CDFI Loan	$3.0 MM
NMTC Equity	$3.0 MM
Opportunity Fund Equity	$2.0 MM
Sponsor Equity	$400 K
Total	**$16.4 MM**

Economic Development: **Issues to consider**

- The “substantial rehabilitation” rule requires all OZ investments to double the basis of the property that the QOF invests in
  - Works for new development and significant improvement of real estate assets
  - Scope of business investments expected to be limited to early stage business investment and established businesses relocating or expanding to Zones
- 50% of the QOZB’s gross income must be derived from the active conduct of a trade or business in the Opportunity Zone
- 70% of the QOZB’s tangible assets must be located in the Opportunity Zone
- Awaiting guidance regarding ability to recycle investments within a QOF

Affordable Housing Examples

1 Pairing with LIHTC or the HTC

- Tax credit investments providing housing for families at or under 60% AMI
- 15 year investment period
- Investors = corporate investors with capital gains to invest and tax credit appetite (may be a limited investor market).

2 Workforce Rental Housing

- Providing housing for families at 80 – 120% AMI (Middle Income Housing that is needed in many communities).
- 10 year investment period
- Investors = individuals or corporations

3 Lease-to-own Housing – maybe???

- Single family or multi-family
- Investors = social impact focus
- Requires ability to revolve ozone equity capital.

Example Workforce Housing Deal

- New Construction of 116 units for families with rents at 90-110% AMI
- Proven project in market (prior phases in non-Ozone locations)
- Expect this to be Single Asset Opportunity Fund with High Net Worth Individuals as investors
- Capital Stack: Between 40 – 60% from ozone equity depending on return required by investor. Remainder of financing from non-recourse first mortgage.
- Investors to get preferred annual cash payments
- Exit scenario in year 10 - either sale or refinancing. Return of capital plus split of sales proceeds

Technical Issues

- 90% invested rule
  - 180 days to invest 90% of fund capital in QOZBP per statute
  - Regulations provide for a 31 month investment period through a working capital safe harbor
- The “substantial rehabilitation” rule
  - OZ investments to double the basis of the property that the QOF invests in within 30 months of investment; land is excluded so that only the value of buildings needs to be doubled
- “Substantially all” rule
  - QOZ business is one in which greater than 70% of the tangible property owned or leased is located in the Opportunity Zone
- Early disposition
  - If an OZ Fund investor sells all of its interest in an OZ Fund before 12/31/26, the investor can maintain the original gain deferral by reinvesting into another OZ Fund within 180 days
  - Further guidance is expected regarding the ability to recycle investments within an OZ Fund

The Impact of Opportunity Zone Designation is Limited

- Ozone investments are equity investments.
- They are subject to typical business and/or real estate risks.
- In most cases, the Opportunity Zone tax benefits will not make a deal worth doing if it was not otherwise attractive to investors.

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Community Strategies to Attract Desired Investment

Public Land
Current Owners
Acquire Key Sites
Partner with Developers
Infrastructure/Site Prep

Land

Zoning

Zone for Desired Uses
Mixed Uses
Inclusionary Zoning

Community Engagement
Master Plan/Vision
Urban Revitalization Plan
Housing Production Plan
Infrastructure

Planning

Incentives

City/State Funds
Philanthropic Investment
Tax Abatement/TIF/HDIP
Community Benefits
Business Imp. District
Accelerated Permitting

Plus outreach, collaboration, connection and marketing.

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How Can Communities Position Themselves?

- ✓ Develop Community Vision and Priorities
- ✓ Use Municipal and State Tools to Attract/Incentivize
- ✓ Have a Point Person
- ✓ Consider Aggregating Resources
- ✓ Bring Anchor Institutions and other Stakeholders to the Table
- ✓ ID and Market Investment Opportunities

Land	Zoning
Planning	Incentives

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Strategies for Massachusetts Communities

924

number of Opportunity Zones where LISC, NEF and NMSC have made investments

LISC is developing a toolkit for Massachusetts communities containing designated opportunity zones, to build their capacity to define community-driven strategies for investment and growth.

Contact us to share your strategies and potential deals.

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LISC's Roles

- Fund Manager
- Service Provider
- Debt Financing
- Industry Leadership

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