

THE GUIDE TO MAKING OPPORTUNITY ZONES WORK

A Resource for Investors, Developers,
Entrepreneurs, and Community Leaders

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PROLOGUE

“Opportunity Zones convey tax advantages to investors who take the proceeds of a capital gain, like the sale of a stock or a business, and invest them through a fund into a qualifying project in a designated zone. They were a largely overlooked provision of President Trump’s tax law when Congress was debating it in 2017, but in the two years since the law’s signing, the zones have stirred interest from investors on Wall Street, along with philanthropists and city leaders looking to revitalize distressed areas.”¹

—The New York Times, [Treasury completes rules for Opportunity Zone tax breaks](#), Dec. 20, 2019

Nearly three years after the passage of the 2017 *Tax Cuts and Jobs Act* (TCJA) brought to life the first new community development tax incentive in decades, we are still in the early stages of understanding how Opportunity Zones (OZs) can and should be implemented.

There's far more that we don't know than what we do know about this new industry, given the complex rules that were released by the IRS in three tranches over the course of 2018 and 2019 and now number in the hundreds of pages. As this new marketplace begins to take shape, we wanted to share what we have learned to help interested parties – from the investor to the resident and everyone in between – avoid many of the missteps and confusion we've witnessed, and to help you better understand how to navigate this evolving environment.

We hope you think of this guide as your comprehensive, plain-English tutorial to the nuts and bolts of OZ investing, whether you invest cash or intellectual capital in creating more equitable and sustainable low-income communities. We will go beyond technical nuances to provide practical tips that can help create and support a healthier OZ ecosystem for everyone involved.

What you can expect from this guide

This guide is not intended to be an authoritative, technical treatise. For that reason you will not find extensive citations to the law or the regulations themselves. (For

those who want to dive into the weeds, you can find links to those resources in [Appendix B](#).)

What you will see throughout this guide are references to ways in which the rules were designed to advance the overall **policy intent of Opportunity Zones: Encouraging new economic activity in left-behind places**. We created this guide to show how this principle can be upheld when the various stakeholders in this broad marketplace work together to help shift economic activity to communities that need it most.

We wanted to create a resource that would both inform existing investors, fund managers, developers, entrepreneurs, and community leaders in this space, and serve as a primer for those who are new to OZs. While this guide is not meant to address every issue or explore every possible use case (and there are hundreds), we set out to provide a helpful overview of the emerging industry and address the most common scenarios we encounter.

At the core, you should read this book because OZ investing will be a significant component of community development initiatives, business plans, tax strategies, investment portfolios, and estate plans for the next decade and beyond. In fact, both President Donald Trump and former Vice President Joe Biden embraced OZs as centerpieces in their 2020 election campaigns, and you can't say that about too many other economic policy issues.

1. [Treasury completes rules for Opportunity Zone tax breaks](#), The New York Times, Dec. 20, 2019.

Opportunity Zones have not been without their share of controversy. Incentivizing private investment in low-income communities stimulates the broader philosophical debate around the most appropriate roles of the national government, state and local government, philanthropy, and the private sector. Where some predict a rising tide that will lift all boats, others fear the pressures of gentrification that can lead to displacement, and still others wonder whether there will be any impact at all. There are without question disconnects that arise between investor and community priorities. At the same time, government has fewer and fewer tools at its disposal to provide subsidy and encourage alignment. This dynamic reflects the serious issues that require acknowledgement and discussion in order for OZs – and communities – to be successful.

What's undoubtedly true, though, is that we have seen profound growth in inequality within and among communities, and OZs are generating an enormously important conversation about the best way that all stakeholders can address the vast divides we are seeing in economic, education, and health outcomes. While OZs won't solve these long-standing and serious issues on their own – this is not a silver bullet that can holistically address racism, underinvestment, and community leadership – OZs are an important new experiment that we believe merits serious consideration and engagement from all corners of civil society.

The Urban Institute, a D.C.-based economic and social policy think tank, stated in a recent report that "OZs are helping spur the evolution of a new community development ecosystem, engaging both project developers and investors who have limited historical engagement in community development work."² They also point out a need to be sensitive to how "mission-oriented" projects may struggle to compete with higher-return projects for attention and capital. It is this engagement and dialogue that is particularly exciting for all of us who believe in the urgency of developing better place-based solutions to address inequality in America.

Who should use this guide

At the end of the day, we want this guide to serve as a step toward creating a more informed dialogue and better understanding among all stakeholders, including:



Investors who have capital gains to redeploy into worthy businesses, real estate, and infrastructure projects, whether they are small "retail" investors with modest stock market gains, high-net-worth individuals who have sold high-growth companies and large real estate portfolios, or large institutions and corporations following an M&A transaction;



Fund managers who are seeking OZ capital and investment opportunities via strategies that focus on the opportunities and challenges of long-term investing in economically distressed communities;



Project/real estate developers who are looking for new sources of capital that will flesh out the financing needed to complete local projects that in the past haven't been able to get the attention of private investment markets;



Businesses/entrepreneurs who have resisted the urge to move – or been unable to move – to the handful of super-performing cities that attract so much of the country's private equity and growth capital; and



Community leaders and their constituents who have a vision to turn around their central business districts, neighborhood corridors, brownfield sites, and abandoned malls, looking to find better and more sustainable ways to support planned growth by partnering with the private sector, in their towns and cities and far beyond.

As we planned this guide, the variety of audiences who have a stake in the success of Opportunity Zones posed an interesting challenge. On the one hand, each player has unique considerations and nuances that lend themselves to discrete chapters. On the other, the success of OZ projects depends on all participants having a holistic understanding of how these investments work, and how all players' working together can ultimately support their intended outcomes.

We have organized and written this guide in a way that is intended to give readers a better understanding of the larger ecosystem, as well as an appreciation for how they can fit in. Since there are so many different approaches to fund management, capital accumulation, and asset identification,

2. [An Early Assessment of Opportunity Zones for Equitable Development Projects](#), The Urban Institute, June-July 2020.

we strove to take a balanced approach that encourages prospective investors, fund managers, investees, and all types of community entities to keep the bigger picture in mind.

What you'll find in this guide

We start with an **Introduction** that provides background on the bipartisan origins of Opportunity Zones, to help level-set the intent and spirit of the program, as well as describe our observations on how the marketplace is developing.

Chapter 1 begins to get into the meat of the guide, providing an overview of the OZ incentives, and contextualizes why we think the program has been able to attract so much capital even in its early days.

Chapter 2 answers investors' most frequently asked questions. Whether you are an impact investor or are looking to make a purely economic investment, there is a lot to understand in what you are becoming a party to and how to encourage something more sustainable and valuable to everyone. In addition to investment-specific considerations, you will also want to explore whether you will set up your own fund or entrust your capital gains to an experienced fund manager.

Chapter 3 seeks to demystify the issues and challenges confronting fund managers who seek OZ capital and investment opportunities. The Qualified Opportunity Fund (QOF) is the sole funding vehicle for capital investment and the central mechanism for the IRS to ensure compliance and oversight over the utilization of the tax incentive. As a result, there is much to understand with regard to compliance issues, and in particular the structure and timing of investments.

Chapter 4 focuses on issues specific to real estate sponsors and developers, who will always be a key component of the audience for any place-based investment opportunity. But the asset classes within real estate are diverse, and specific knowledge, data, and relationships are required to identify, acquire, and manage them successfully in an OZ context.

Chapter 5 helps entrepreneurs and business owners understand the potential advantages of being a Qualified Opportunity Zone business (QOZB), as well as the requirements for earning and maintaining that designation. As OZs get greater traction as an investment asset, the

market will pivot to even more asset class variability. Operating businesses are becoming a more important focus, bringing a much broader audience into the discussion as we think about how to rebuild communities through industry, including renewable energy, infrastructure, manufacturing, hospitality, entertainment, technology, and life sciences, to name just a few.

Chapter 6 underscores that everything needs to be about the community with respect to OZs. We encourage all stakeholders to turn to this chapter, in which we talk about what makes an OZ community attractive and how to build a strategy that considers how to navigate risks such as potential gentrification and displacement.

In our **Conclusion**, we consider how the COVID-19 pandemic and renewed calls for racial equity have accentuated the dire needs that the OZ marketplace was envisioned to address, and how broad bipartisan support for the idea makes it a rare example of an economic development strategy that is likely to continue, no matter who is in the White House.³

Whatever intention brought you to this guide, we hope you will benefit from this journey through the various aspects of the OZ ecosystem. Our goal is to enhance your knowledge and empower you to participate in the broader conversation that can produce a new community development marketplace that works for everyone.

Last, but not least, we are grateful for everyone at CohnReznick, and beyond, who contributed to the development of this guide. The gems of information you will encounter throughout the guide are directly the product of their hard work and analysis.

Enjoy!

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3. Editors' note: We wanted this book to capture the events of the exact moment in which we published it – days before the 2020 election, months into the pandemic – but recognize that the moment in which you're reading it may look different. Watch for future editions that revisit some of our more timely elements, but trust that our overall guidance on the ins and outs of OZs will remain the same.