

Opportunity Zones Frequently Asked Questions

What are Opportunity Zones? Opportunity Zones are a new concept recently enacted in the 2017 Tax Cuts and Jobs Act. The program is designed to incentivize patient capital investments in low-income communities nationwide that have been cut off from capital and experienced a lack of business growth. There are three types of tax incentives that relate to the treatment of capital gains, each of the incentives are connected to the longevity of an investor's stake in a qualified Opportunity Fund that provides the most upside to those who hold their investment for 10 years or more.

What is an Opportunity Fund? An opportunity fund is any investment vehicle organized as a corporation or partnership for the purpose of investing in "qualified Opportunity Zone property", and that holds at least 90% of its assets in the zone property stocks, partnership interests or business property. The IRS is expected to certify funds by the end of May 2018. A fund could be of any size. It could oversee a single project or serve a defined area (city/region) or a state or be multistate.

What qualifies as an Opportunity Zone? The nominated zone must either be a "low income community" or "contiguous" to a designated low income community subject to certain statutory limitations.

- I. **Low income community:** Means any population census tract if the poverty rate is at least 20 percent. Targeted populations, areas not within census tracts, low population tracts and high migration census tracts may be eligible under defined statutory guidelines.
- II. **Contiguous:** Census tract directly adjacent to one or more low-income communities. The income of the desired contiguous tract has to be less than 125% of any neighboring low income tract.

Who designates an Opportunity Zones tract? Eligible zones must be nominated by the governor of a state within a 90-day period starting from the Act's date of enactment (December 22, 2017) to designate up to 25 percent of the total number of low-income census tracts in a state as Opportunity Zones, unless a 30-day extension is applied for and granted. Opportunity Zone designation deadline barring an extension being granted is Wednesday, March 21, 2018.

Although governors are required to nominate low income census tracts, those tracts should have opportunities for potential investment. And clustering census tracts will enhance opportunity. Investors are not likely to invest in high risk census tracts that have no potential.

How many Eligible Tracts qualify in Michigan? There are 1,152 eligible census tracts with the maximum of 25% or 288 of these tracts allowed to qualify per program rules. This number may be adjusted by CDFI.

Types of Opportunity Zone incentives

- I. **Temporary Deferral:** A temporary deferral of inclusion in taxable income for capital gains reinvested into an Opportunity Fund. The deferred gain must be recognized on the earlier of the date on which the opportunity zone investment is disposed of or December 31, 2026.
- II. **Step-Up in Basis:** For capital gains reinvested in an Opportunity Fund the basis is increased by 10% if the investment in the Opportunity Fund is held by the taxpayer for

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at least 5 years and by an additional 5% if held for at least 7 years, thereby excluding up to 15% of the original gain from taxation.

- III. **Permanent Exclusion:** a permanent exclusion from taxable income of capital gains from sale or exchange of an investment in an Opportunity Fund if the investment is held for at least 10 years. This exclusion only applies to gains accrued after an investment in an Opportunity Fund.

Opportunity Fund Investments

Preliminary information indicates an Opportunity Fund can be utilized as a primary investment in a variety of activities. Funds can be used to create new businesses, new commercial or residential real estate or infrastructure. Opportunity Funds can be used to invest in existing businesses if it doubles the investment basis over 30 months.

The incentive can also be combined with other incentives such as New Market Tax Credits (NMTC), Low-Income Housing Tax Credit (LIHTC) and historic rehabilitation tax credit, adding a valuable tool for economic and community development. State and local governments should also consider creating and targeting other resources, especially job training, that will play an important role in leveraging investments. Local activity will show that opportunities exist.

An Opportunity fund cannot engage in any of the following “sin” businesses: any private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack or other facility used for gambling, or any store where the principal business purpose is the sale of alcoholic beverages for consumption off premises.