Opportunity Zones Hot Topics

Qualified opportunity funds being tracked by Novogradac reported nearly $10 billion in equity investment during 2022 and we recently began another session of Congress with a possibility of legislation to extend and enhance the opportunity zones (OZ) incentive. In this week's podcast, Michael Novogradac, CPA, and John Sciarretti, CPA, discuss the state of incentive and the chances for changes either by legislation or regulation. They also discuss the role the Novogradac Opportunity Zones Working Group is playing and what might be in an "Opportunity Zones 2.0" bill. They then examine highlights of the recent Novogradac QOF equity-raising report.

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Transcript

Introduction

[00:00:11] **Michael Novogradac, CPA:** Hello, I'm Michael Novogradac and this is Tax Credit Tuesday. This is the February 14th, 2023, podcast.

In today's podcast, we're going to look at key issues concerning the opportunity zones tax incentive. Opportunity zones were created as part of tax legislation in late 2017 with final regulations released in late 2019, about a two-year span.

It's now been over three years since that December 2019 release, which means opportunity zones have been an active part of the investment world for several years now, certainly long enough to have a significant impact. The opportunity zones incentive also has passed some key investment deadlines as we approach the currently scheduled expiration of opportunity zones on Dec. 31, 2026.

Now, I should note that Dec. 31, 2026, expiration date applies to the ability of investors to make new investment in opportunity funds. At Novogradac, as many of you listeners know, we track qualified opportunity funds and the equity investment made in them. More specifically, we track funds that voluntarily provide information to us along with funds where there's public information available from sources such as the Securities and Exchange Commission filings or press releases.

By the way, if you raise capital for or sponsor opportunity funds and you want to be included in our survey, please email us at CPAs@Novoco.com or reach out to me directly at Michael.Novogradac@Novoco.com. You can also feel free to reach out to our guest on today's podcast.

Our survey of qualified opportunity funds is not an exhaustive accounting of all capital raising for opportunity funds. That said, our survey does provide a good look at capital raised and deployed over time and in various areas across the country. Earlier this month, we did release data on investment through the end of 2022. That data showed that more than $34 billion in equity has been raised cumulatively by qualified opportunity funds that we're tracking, and nearly $10 billion of that was raised in the past year.

That makes last year, 2022, the most we've seen raised any year that we've tracked. Our data-gathering demonstrates that capital raising and investment in opportunity zones continues to be very strong. I do want to note, though, that the level of reported capital raising in the fourth quarter of 2022 was slower than the first three quarters of 2022. That fourth-quarter slowdown is presumed to be due to the drop in the stock market and sluggish real estate sales, which reduced the level of capital gains available to be invested in opportunity funds. We will talk more about that in other details from our report later in the podcast.

So, my guest today is John Sciarretti. It's probably not a surprise to most listeners who have listened to the podcast regularly. John's a partner in our Dover, Ohio, office, and John leads the Novogradac Opportunity Zones Working Group, and he did write two blogs on the latest data on qualified opportunity funds, and I wrote two blogs as well.

John's been a frequent guest on Tax Credit Tuesday, often discussing opportunity zones, but he also works in a lot of areas outside of opportunity zones, including the new markets tax credit, the historic tax credit, renewable energy tax credits, state tax credits. John's an expert on most tax matters related to investments in real estate.

Now, on today's podcast, we're going to discuss some current issues involving opportunity zones, and we'll start by talking about potential legislation to extend opportunity zones and the chances of getting such an extension in this Congress. After that, we'll talk about regulatory issues for the opportunity zones incentive, including or I should say, with a focus on those areas being examined by the Novogradac Opportunity Zones Working Group.

And then we'll wrap up with some of the highlight of our recent report, as I mentioned earlier in this introduction. So, we have a lot to discuss. So, if you're ready, let's get started.

So, John, welcome back to Tax Credit Tuesday.

[00:04:22] **John Sciarretti, CPA:** Thanks, Mike. It's great to be back.

[00:04:24] **Michael Novogradac, CPA:** Well, I appreciate you joining us. You're always a popular guest for our listeners.

As I mentioned in the introduction, the opportunity zones incentive is currently scheduled to expire at the end of 2026, which does seem like a long ways away, but it'll be here before we know it. Now, there were hopes that we'd get some sort of extension legislation passed in the last Congress. News flash: Now that didn't happen.

So please explain to our listeners, John, the current state, or maybe talk a bit about what didn't happen and then the current state of efforts to extend opportunity zones.

Current State of OZ Incentive

[00:05:01] **John Sciarretti, CPA:** I'd be glad to, Mike. So, it might be good to start out just to remind everybody what was in the bill. Because it wasn't just an extension bill, it had six main parts. The extension obviously was what I think most folks were interested in. And the extension date was 2028, so that's two years from the 2026. And the interesting thing about that is it didn't matter when you invested, everyone got this extra two years. So that, that was a fantastic benefit. But it also had other, require other parts to the bill. It had enhanced reporting requirements. And that's always been something that I think everyone's interested in getting more reporting around the program. It revived the basis step-ups, the 10%and 15% and again, that generally that was available to everyone, regardless of when you invested. It did shorten the seven year 5%, to six years. It removed some high-income tracts that got some bad press. And I think everyone in the industry, most stakeholders thought that to be a good idea as well, and there was a transition period and so it didn't hurt folks that had already invested or made some sort of commitment to invest in these tracts.

And then it allowed for a fund of funds investment. Currently a QOF can't invest in another QOF. And I see a lot of qualified opportunity funds that made an investment and they maybe pushed it down to a business and the business didn't work out, so they really didn't fund it. They have cash sitting on that business and they decided they just want to join another fund and it creates a problem because you can move the money back up to the QOF, but you know that QOF can't invest in the other QOF to get into that wider fund. And so it creates a problem where you either have to merge or go side by side and, so I think that would be the most useful part of the funds of funds. And then lastly, there was this sort of $1 billion dynamism fund, which basically grants the states to help support their OZ strategy, technical assistance and capacity building and the like. So, a pretty comprehensive bill. I think everyone was pleased with it and would've been more, as you said, didn't happen.

I think it's important to point out, Mike, that the OZ bill was not specifically excluded. It would've had to been attached to another bill. And there were a number of priority tax extenders that were deferred in 2022, not just opportunity zones. And so there was no tax title in a bill, and so nothing got included.

We felt that the stars were aligned for passage in the lame-duck session. We thought that the OZ bill, along with these other tax extenders would be added to the omnibus bill that was being negotiated at the end of the year and the ominous bill, as you know, Mike, took a long time to negotiate and once Congress struck the agreement on that bill, there really wasn't a lot of time left to negotiate tax legislation, which would've likely taken a lot of time because there was a mismatch in the priorities of what tax items would be included. The Democrats seemed to be interested in the extension of the expansion of the child tax credit and that doesn't mean Republicans weren't interested in it, but that was their main priority.

And Republicans priorities included the extension of all the business tax incentives like the R&D credit, bonus depreciation is starting to phase down so that that was, something folks were interested in getting back the 100%. And then the 163-J, which is essentially the interest deduction limitations. There was an add-back, there were some add-backs, primarily depreciation that kind of help you deduct a little more interest and that was phased out as well. And so, I think the Republicans were interested in going back to the table there and maybe getting that add back in that calculation so folks could deduct more interest. So due to the mismatch of these priorities–

[00:09:05] **Michael Novogradac, CPA:** Let me just add that you said how we thought the stars was kind of aligned toward getting some type of extenders legislation that could be a vehicle for extending the opportunity zones incentive. It wasn't just us. The now-chairman of Ways and Means Committee Jason Smith, actually spoke in December saying he thought there was a better than 50% chance that there would be such a tax bill. So, when the now-head chair of the Ways and Means Committee thought that, I felt like we were in good company. We were wrong. We were in good company.

[00:09:42] **John Sciarretti, CPA:** No that's, that's a great point, Mike. As I discussed, there's this sort of mismatch in priorities, which means it's going to take a long time to negotiate the tax extenders. And so the leadership, well, actually there was a leadership vacuum, too, because no one knew who was going to be Speaker of the House. No one knew who was going to be the Ways and Means chair and so all that, I think just influenced Congress to defer any tax legislation at the end of the year. So, again, I don't think we should read into this that Congress rejected the OZ proposal. It was it was only one part of that. And so that, that's important. Now as far as reintroduction and chances of maybe passing in 2023, we're still encouraged. I mean, I think we're just as encouraged as we were at the end of 2022. It's been a challenging environment this year. Congress has actually gotten off to a slow start. It took some time to figure out who leadership was going to be. The priority issue at hand is the debt limits. And that's what you hear in the news today. The government hit its debt limit in January. The Treasury actually has employed these extraordinary measures, which, I'm not an expert in, but I think it's an accounting trick to move cash when bills are due so that we don't exceed the debt limit. But anyway, so that's where we are now, and that'll take us to July, I think before we use the extraordinary measures. And then there's some talk that in July we may get a short-term extension around the debt limit to the end of the fiscal year, which will be September. So now we're in the fourth quarter again, which by the way is the typical time for tax incentives to be introduced, or tax legislation to be introduced. So, we think it might take until the fourth quarter. It's likely to take until the fourth quarter. It could be earlier, but it's likely to take until the fourth quarter. We believe that OZ is still a priority. We know it, are we, what we're told it's still his priority for Sen. [Tim] Scott, who's a senior leader in his signature bill. And so all these tax extender priorities, like I said, were deferred and they're still priorities and there's some other priorities and there's like a, the 1099 limit for third-party payers, which used to be like 20,000, now it's 600.

And there's been kind of an uproar around that and that's something that I think the Republicans want to negotiate. And that's like Venmo stuff, you shouldn't get 1099 for Venmo payments and my daughter's a photographer and she gets Venmo payments all the time, and I always tell her they don't give me 1099s when you do these weddings and such.

So, but anyway, that's kind of where we are. And like I said, I think we're still encouraged, that we'll get this added to some sort of tax legislation at the end of the year. I wouldn't sit on your hands. I think it's important to promote the benefits of opportunity zones to your congressman, and I think that's an important step throughout this process, but as far as what it'll look like, I know folks sometimes wonder as we have to reintroduce the bill. Is it going to be the same bill? And I think largely it probably will be the same bill.

I know, there's two schools of thought. If you got another chance to introduce it, maybe you add lots of other stuff and get more sponsors, but you're always risking losing the sponsors that you have on the bill. So, it's probably going to look a lot like the original legislation. There are a number of technical corrections that have been discovered and probably will be added to a new bill and then there is some, I think there's some hope that we get the OZ designation date moved to past 2028. And what I mean by that is opportunity zones are designated through 2028. So, after 2028, there are no opportunity zones to invest in and so this bill extends the investment date to the end of '28.

So say you have a gain at the end of '28 and you were planning on investing it in '29 because you have 180 days and if it's through a pass-through entity, you have even more time, nine months or so. So, you won't be able to invest that in '29. So it is important that they move that date and it might be a good thing to move it a little further out for reinvestments and the like while people are still in their 10-year period. So we're, we are hopeful that is one change that gets into this initial modification extension bill. So that's the lay of the land there, Mike.

[00:14:03] **Michael Novogradac, CPA:** So thank you for sharing that. And if one of the listeners don't quite understand what John was just saying with respect to the extending of the investment date and all the rest, that's reason to join the Opportunity Zones Working Group. Because it's issues like that we end up discussing, little nuances that are quite important. And I would also just emphasize, John mentioned the importance of continuing to be advocates for opportunity zones and the like and how when we go through the narrative and try to analyze when such a bill might pass. And it's seeming like fourth quarter of this year. But you've got to be ready, because as John also noted, you never really know and you don't know what might happen as that would carry a tax bill and you don't want to find yourself planning on fourth quarter and then something happens in the second quarter and you're not ready. So that's the why it's important to get the bill reintroduced in getting co-sponsors and the rest so the moment a train leaves a station that has a tax bill, the opportunity zones can be on it.

So, thank you for that, John. That's a good overview as to where we stand in terms of extension or other changes to opportunity zones in the coming Congress. I did want to turn the direction a little bit. When President Biden came into office, he did emphasize how opportunity zones could help address the needs of low-income communities. So, we all appreciate President Biden's support of opportunity zones and he also noted that they could be particularly helpful by working in concert with nonprofits. So I wanted just to get your thoughts on ways the administration could use the regulatory process to enact new or clarify existing rules to help opportunity zones incentive better drive positive outcomes in low-income communities. And I know in particular the working group's focused on a lot of things, but including how to drive more investment into affordable housing and how to drive more investment into operating businesses and opportunity zones.

Regulatory Process and Opportunity Zones

[00:16:09] **John Sciarretti, CPA:** Yeah. Thanks for that, Mike. You know, as we were somewhat surprised that there hasn't been any regulatory enhancements to the administration's policy goals in the last couple of years. It was actually, actually we were surprised when opportunity zones were actually in the policy goals and then we figured one way to affect that was to do that through the regulations and it really hasn't happened.

We actually, as the Opportunity Zones Working Group, we made some recommendations to the administration on the ways that we thought that opportunity zones could be used to increase affordable housing in low-income areas, and increase operating business investments that could provide more jobs in these low-income areas. And so those are the two things we focused on and from a housing perspective, when you look at the substantial improvement rules in opportunity zones, where you have to sort of spend more than you bought it for it's a lot, it's a lot. it's a much higher bar than what the low-income housing tax credit substantial improvement rule is. And so, I think low-income housing's around $7,000 a unit that you have to spend, which you know, may or may not be as much as you bought the property for, but probably more times than not, it's not. So, we thought if they relaxed that standard for low-income housing, it'd be an easy way to promote more affordable housing in opportunity zones. In addition, there's this really complicated special inclusion rule for partnerships. And so right now at the inclusion date of '26, where it is now, you have to pay the tax you deferred, unless you got some step-ups. But primarily you're, you look at the fair market value investment and you pay the tax on that or what you deferred. When you look at affordable housing, those projects typically don't appreciate and even depreciate because of the rent limits on those projects. And so, we thought it would be a great incentive if affordable housing investors could take advantage of that decrease in value and perhaps pay a little less at that inclusion date in this special amount includable rule prohibited or precluded investors from taking advantage of that. And so, I mean, there were actually funds in the beginning, but just looking at that as part of the benefit of their fund and they were totally focused on affordable housing and because of this special includable role, you don't, they left the marketplace.

And so, we think it would be very good if in an easy regulatory fix exception for that to be implemented. And then from an opportunity zone business front, the popular interim gain deferral is something we thought would help operating businesses because they tend to be shorter holding periods. And so what that means is that if you have a gain before the 10-year period, you don't get the gain exclusion on that. You have to hold it for 10 years. And operating businesses might have probably more likely a seven-year time horizon. And it'd be nice for investors to be able to still roll over those gains and other investments at a shorter holding period and that would enable the, we think it would facilitate operating business investments, as well as there's an issue with the substantial improvement test too, for preexisting businesses because you have all this old tangible property sitting around and affects your 70% test at the business level. So, we thought there could be some exceptions there as well.

So, and then lastly, we were, we were looking at the new market tax credit and saying, "Hey, they have this portion of business rule where if a business doesn't qualify the wider business, because you might be in a number of locations and the like, then you can draw a soft circle around activity of that business and call that the qualified business." And so we thought that would be helpful in opportunity zones as well, because businesses operating in opportunity zones, if they have divisions outside of opportunity zones that wouldn't disqualify the business as a whole. So you can just look at that activity. And so, so those are some of the things that we actually proposed. and We're going to keep trying to get this done.

[00:20:24] **Michael Novogradac, CPA:** So, thank you for that, John. I'll include in the show notes a link to the letters that the Opportunity Zones Working Group had sent to Treasury with respect to the housing, the affordable housing related matters that you went through, as well as the operating business items that you referenced. I'll also note, given that we are now in a divided Congress, I do think the White House will be extra focused on regulatory matters since those are within the White House's control or within the administration's control. So, I do think that while last year maybe there's a little bit of a focus, more focus, on legislative efforts to the detriment of regulatory efforts, I do expect a strong focus on regulatory matters, so I think our chances of getting through some of these is greater over the coming two years. I'll also note here we're talking about recommendations to the administration about ways to drive more positive outcomes in low-income communities through some regulatory changes to how opportunity zones work, or at least clarity as opposed, they may not all be changes. There's also potential for the Treasury to revisit how entities certify instead of self certifying, having an application process or more robust self-certification process. So that's something that I know the Opportunity Zones Working Group is continuing to monitor and it's something that listeners should be mindful of because there could be changes that area as well. Let's not go down that tangent. We have a lot I want to cover and I don't want to leave regulatory efforts just yet because I know that the Opportunity Zones Working Group is also focused on decertification, getting some additional clarification there and more clarification on the working capital safe harbor.

Opportunity Zones Working Group Efforts

So, if you could describe the Opportunity Zones Working Groups efforts in both of these areas. First, you can briefly mention what the area is and then what the Opportunity Zones Working Group is looking to achieve. And you can give it a very high level. And I'll once again attach some of the information that the working group has submitted to Treasury on these areas as well.

[00:22:43] **John Sciarretti, CPA:** Sure thing, Mike. So, with respect to decertification, which probably is happening more now than what we'd expect because of the macro economy, COVID and the like, where folks just couldn't, the folks couldn't carry out their plans because the environment is so much different and folks would like to voluntarily decertify, but there's no guidance. The regulations actually have a reserved section for decertification, so they are clearly going to provide guidance around how to decertify or what, what the guidance is around decertification, both voluntary and involuntary. But, and I think the latest is they were supposed to release that guidance at the end of 2022, but we have not seen it yet, so we're hopeful it happens quickly. But like I said, there's currently no guidance. With respect to voluntary decertification, our suggestion is to make it a self-decertification process just like a certification process, right so folks can leave when it things don't work out without any sort of penalty for doing so.

So, so that's the extent of the voluntary and we've drafted some language around that. And then from an involuntary decertification, what that means is that folks just aren't playing by the rules. Where the IRS you know, can decertify at their own discretion when taxpayers are purposely not playing by the rules. And so our suggestion there is to have really clear guidance of what it means not to play by the rules. We think that it should be based on sort of a willful neglect standard, and that they're really clear in the guidance. So folks aren't worried about false, involuntary neglect. But, so that's the decertifications. Like I said, we're hopeful we get some guidance around that soon.

And then there's still some questions around the working capital safe harbor that you mentioned. Treasury's done a really good job, I think it started out trying to make that a multifaceted provision in the regs where a lot of things rely on the working capital safe harbor. It started out being a very difficult challenge to making the guidance clear. But they've done a nice job of modifying those rules around the working capital safe harbor. But there's still some things that need addressed. The main thing is clarity. In order to satisfy the requirements of the working capital safe harbor, the third prong of that test is you have to be substantially consistent with what you said you were going to do and we don't really know what that means. Businesses have a lot of challenges and they, as a result, modify their plans regularly, and especially in the last three or four years where the challenges were even more with the pandemic and the now the macro economy and the like. And so things just don't necessarily work like we plan them and so we just don't know what it means to be substantially consistent. And so that's our main, our primary question. And then, if plans need to be amended, when, how big a change do you have before you actually have to amend the plan, number one, and when can you do this? There are some provisions for these amendments in the event of a national disaster like the pandemic. But what about if it's not related to a national disaster? And we're going to be losing that designation soon, which is a good thing. But and so those are some of the questions we have around, around the working capital safe harbor. So that, those are the two main things, Mike and the regs that we're interested in and our members are interested in seeing a little more clarity around.

[00:26:30] **Michael Novogradac, CPA:** Great. And I would, note also, as we've discussed before, there's also the notion of maybe getting more streamlined approach to relief for late regulatory elections.

[00:26:42] **John Sciarretti, CPA:** But yeah, indeed. Yeah, indeed.

[00:26:44] **Michael Novogradac, CPA:** And that's just something that we could go on with other topics as well, which serves as a good segue to remind listeners, as I mentioned earlier, you can become a member of the Opportunity Zones Working Group and I will provide John's email address and a link to the Opportunity Zones Working Group webpage in today's show notes. There's a lot of reasons, a lot of benefits to being a member of the Opportunity Zones Working Group. But let me also say that we do welcome your thoughts on some of the issues we've discussed so far irrespective of being a member of the Opportunity Zones Working Group. Please email those to CPAs@Novoco.com and that email will be in the show notes as well.

But do give serious consideration to joining the Opportunity Zones Working Group to stay current on matters, discuss issues you might have and the rest. But anyway, I won't go into too much of a sales pitch on joining the Opportunity Zones Working Group. There's lots of benefits. I'll leave it at that.

Opportunity Zones 2.0

So John, let's now talk about something a little bit more broad with respect to the opportunity zones incentive as it stands today. We talked earlier about getting it extended for potentially two more years. As it stands today, it, the opportunity zones incentive does sunset in less than three years and even if we get it extended for two more years, I know that the working group is also focusing on a second-generation OZ, an OZ 2.0, if you will. So, if you can share with our listeners some of the working group's efforts here, and this maybe to frame it for our listeners, this is a notion right now, there's the effort to get an additional couple of years, but then there's also this other effort to develop this Opportunity Zones 2.0 that would be the next generation. So, if you could share with our listeners some of the working group's efforts here and your thoughts about what a next-generation OZ might look like.

[00:28:44] **John Sciarretti, CPA:** Absolutely. So all the work that's been done, all the money that's been raised and it's, it's been a successful program as far as raising capital, it is going to be over in 2026, and we're hopeful we get it to 2028 or maybe '29 depending on when the bill gets passed. But I think it's been a success, from a perspective of attracting money to low-income communities. No one can argue with that, it's been a success. It's been a tremendous amount of money invested and so we would like for it to be extended further and maybe in perpetuity, but significant changes to tax legislation that I think would be proposed other than a further extension, I think there's a lot of things that folks are interested in seeing changed and It takes a lot of time to make significant amount of changes. It takes a significant amount of time before a bill can even be proposed. And so, modifications that folks are interested in, they've got to be prioritized. There's always a cost to them, so you've got to understand the cost. It could be a great idea, but it's got to be, it can't cost too much for the value it presents and then, the time to draft the bill and secure sponsors and then get all this ready in time for it to wait around for the right legislative vehicle.

So, it's not too early to start and that's where we are now. And so we actually have been, have started conversations with our members. They're really, our members are interested in being part of this discussion and most of them were not part of the discussion the first time around. So now they get to have a voice and so I think they're really pleased about that opportunity, and they have lots of ideas on how to make the incentive more beneficial to low-income communities as well as more attractive to investors. And so, so that's where we are. And once we get our own list of priorities, we intend to work with the Economic Innovation Group to help to communicate all these priorities to Congress. And so that's kind of what the working group's been doing with respect to 2.0.

Some of the things, Mike, that our members would like to see, there's a lot of things, but I think the most popular item is permanency. I mean, we would like to see it extended indefinitely. And then the interim gain deferral is something that folks are interested in. We kind of talked about it from a regulatory change, but there's, there's some question of whether you can do that through regulations, so it'd be important to get that in the next, the next generation of opportunity zones. And then additional incentives for impact investments we think would be a fantastic add on to the opportunity zone incentive. And so folks have ideas on how to structure that. And we're talking a lot about that at this point and then a number of technical revisions that I'm not going to go into now, but things that would help facilitate the structuring and operation of qualified funds and qualified businesses. But you know, like I said, I'm not going to go into the details of it all, but if any of your listeners would like to be part of the conversation, do please consider joining the Opportunities Zones Working Group.

[00:32:01] **Michael Novogradac, CPA:** And I would just add to that in addition to describe, in addition to modifying and enhancing the level of incentives along with how opportunity zones operates to make it more efficient in bringing capital to distressed communities and benefiting residents of the communities, there would also, as part of that, be a redesignation of some. The opportunity zones themselves need to be redesignated periodically based upon new data and the rest. So that certainly plays in with 2.0 as well, and thoughts that listeners have on that are always appreciated.

Novogradac Qualified Opportunity Fund Report Highlights

So, John, now, let's turn to the qualified opportunity fund report that we at Novogradac recently released, and as I noted, you and I each wrote two blog posts, apiece, on that release, and this is the Dec. 31, 2022, update to our tracking report. Now, as I did mention in the intro, in 2022, nearly $10 billion–billion with a B–in capital was raised by qualified opportunity funds that we track and the total capital raised for the funds that we're tracking is north of $34 billion. Once again, billion with a B. So

John, as you examined the data from that report, what stood out the most to you or what are a few of the things that stood out the most?

[00:33:29] **John Sciarretti, CPA:** I mean, I think what stood out the most, you already mentioned, but there was a definite slowdown after the first quarter of '22. The first quarter was our biggest quarter ever, and over $4 billion was raised in the first quarter of '22. And if you look at the macro economy, interest rates didn't really start going up and the stock market didn't go down as much and things had took time through the end of the year to where, in the fourth quarter, we had what as much as 400 basis points of increased interest rates in '22. And so, as you mentioned, the stock market was down, the volume of real estate sales were down and the volume of M&A activity, which came off a huge year, I mean a record year. We see a lot of episodic gains of businesses selling and those gains being invested into opportunity zones. So, so for all those reasons, I just think there wasn't as much raw material or fodder to invest and you saw a major drop in the fourth quarter, there was only $1.4 billion invested, which is was like 14% of the year. Prior fourth quarter, it was, over $4 billion and over 40% of that year. So that's probably the thing that stood out the most.

And other than that, I mean, I think things were fairly consistent with respect to investment type. Our report, which tends to be the larger, I mean, we have a number of funds we're tracking like 1,200 funds, but I'd say the primary investment is real estate. And I think that's consistent with the wider country. Right, right. We always say our report is the actual investment's probably three to four times what's in our report. But we have, I think we report on the major funds that are in this marketplace. And, it's interesting, Mike, there was a U.S. Treasury report that was released in the fall which had actual data from tax returns through 2020. They're a little behind our report, but obviously more comprehensive because they actually have the tax data and the 2020 total assets and QOFs was $48 million. So we were at million. Sorry, billion. Yeah. They missed a lot of tax returns, so, we are at $15 billion. So it's sort of validates our thoughts that we're only about a third of the, of the marketplace. But it's definitely the trends are that we can see and the like is a very telling, subset.

[00:36:01] **Michael Novogradac, CPA:** So I would say the big differences are that the Treasury has all the corp, if a corporation's investing in a fund that they're managing themselves, they wouldn't be part of our data and they have a lot of individual funds that are managed by the individual that wouldn't be part of our data because ours is more those that are out there raising capital from third-party investors. So one of the things that I really like about our report, in addition to tracking the capital getting raised, is we're also getting information from funds as to where they're investing the dollars. And our blog posts, our blog posts include a list of the top 50 cities. as well as the top 20 states for planned opportunity zones investment. And once again, the funds themselves raised the capital, then they in turn invest in businesses throughout the country. And it was interesting to see where cities and states ranked and it was great to see that of the top 50, that the top 50 cities for planned investment are scattered across the nation, and they represent 25 states along with the District of Columbia, and that the top 10 states represented every major region of the United States. So it was great to see that opportunity zones investment is so effectively geographically distributed. And I was wondering what you think some of the main drivers of that geographic distribution are?

[00:37:35] **John Sciarretti, CPA:** Well, I think first and foremost, every state has a comparable number of zones that, which is great.

[00:37:42] **Michael Novogradac, CPA:** Fair enough.

[00:37:42] **John Sciarretti, CPA:** And real estate. Real estate investing tends to be local, and so that combination is probably is one of the reasons. But I'm fortunate enough to work with what I'll call an exceptionally talented group of fund sponsors and they're really excellent at finding value in the secondary and tertiary markets across the country. And so these communities that otherwise wouldn't be able to attract outside capital are attracting it so it's that again, I just think the incentive appears to be working as it's intended.

[00:38:14] **Michael Novogradac, CPA:** No, that's sort of good observations. I know initially there was this notion that all the investment would go in areas that were going to generate higher returns and all the rest, and then, I guess the thinking at the time that you and I talked about was as the incentive is rolled out there'll be lower-hanging fruit, if you will and then that fruit will get picked. That's great. We don't have to go to the fruit that's hanging up a little bit higher in the tree and it does seem like we've seen that over the course of the last few years. As the investment gets more and more geographically distributed, as the incentive is working as you would expect it to work. And that's all great to see. I did want to see if there were any other details in the report that particularly stood out to you before we move on.

[00:39:05] **John Sciarretti, CPA:** No, I, it'd be worth mentioning it since I'm from Ohio, that Ohio, although being ninth on the list of fundraising, which is a pretty good number, they ranked first as far as the number of QOF-funded projects at 323 in our survey. Obviously, that's our survey, but that was nice to see, being in my home state. It probably has a lot to do with the opportunity zone tax credit in Ohio. And there's not a lot of these out there in the states. And I thought we would see more through the years. But Ohio's been very successful with the program, it's a $50 million program. It was opened as a $50 million program. They doubled it to $100 million for 2023 and 2022 and '23. And so it's been real successful of attracting investment. They also opened it up to non-Ohio taxpayers, so that was good, as long as your fund does have to be 100% invested in Ohio to get the credit. But it's definitely, I think, driven or attracted fundraising to the state.

[00:40:02] **Michael Novogradac, CPA:** No, I've been surprised that more states haven't similarly created a, a state credit or something else to drive, to attract capital, because you definitely see that in other incentives, where the state will create an add-on incentive to attract capital from other states to that state. Maybe we'll see more of that in due course. I know that Jason Watkins, who works with you on the Opportunity Zones Working Group, every month one of the things he talks about are what changes are happening in opportunity zones at a state policy level. And that's always at one of the many highlights of the monthly calls.

So, John, thank you for joining us. You've provided some very helpful insight into what's happened and more significantly what could be happening regarding opportunity zones. So do stick around for our Off-Mike section. I always enjoy that part of the podcast where I get to ask guests off-topic questions and you'll have a chance to give some additional advice to our listeners, albeit it won't be directly related to opportunity zones, might be some indirect applications.

I may also say to our listeners, please do tune in next week. My guest next week will be Austin Power. He like John, is a partner in our Dover, Ohio, office, and Austin is going to discuss in detail the specific reporting requirements for new markets tax credits allocatees.

And if you're not familiar with new market tax credits, those allocatees are technically community development entities, CDEs. Austin's going to discuss how an entity's, a CDE's, compliance or failure to comply with CDFI Fund-mandated reporting can affect the likelihood of receiving future new market tax credit awards.

Off-Mike Section

So now we're on our Off-Mike section where I get to ask guests some off-topic advice and seek some words of wisdom from them. So John, I have another newsflash for you. We're in the midst of audit and tax busy season. So I was wondering, in the midst of audit and tax busy season, how do you keep your priorities straight, in terms of ensuring that you're on track and focusing on doing the most important things.

[00:42:20] **John Sciarretti, CPA:** You know, busy season is the easiest time to keep your priorities straight because everything is a priority, no matter what you're working on. So, so that's you don't have to think about it much. I think the most important thing is to be proactive in communicating with our clients information that we need when we need it, and then setting the reasonable expectations for our deliverables and right. Fortunately, I have a great, talented team that gets all that right. So that's how I would answer that question.

[00:42:48] **Michael Novogradac, CPA:** So to summarize, I would say make sure you build a strong team. .

[00:42:53] **John Sciarretti, CPA:** Yeah. Yeah. There you go.

[00:42:55] **Michael Novogradac, CPA:** I like that. I like that the team. It's all about the team.

So another question I like to ask guests, and I don't think I've asked you before, is what's the most useful app on your phone? And tell me, why it is that it's the most useful app?

[00:43:14] **John Sciarretti, CPA:** Most useful app, I haven't thought about that much. , The apps I use the most are Microsoft Outlook and Teams. I surmise they must be the most useful apps. I, especially the Teams app, it's really allowed for timely and with collaboration with the team and the like, so, so I really like that. I don't use my phone for much else other than Googling and things of that nature, but it's, I've downloaded a number of apps to help me better plan and organize my life and I've always abandoned. I always wanted to a maps app, which I use all the time, right? We all use a maps app where I could insert personal rules and it could help me navigate in real time and reroute me when I get off track. So , I think , that's stuff that I'm still waiting for and I think that would be my favorite app if it ever did come to the marketplace, so

[00:44:09] **Michael Novogradac, CPA:** Well, thank you for that. I totally agree with you in terms of that, I've had downloaded so many to do apps and all the rest, and they never kind of streamline and fit in my own operation. It's always nice when you get something that actually does fit in and I agree with you on the Teams app, and I would definitely put the teams on the list of my most useful app on the phone, and it's a relatively recent for us at Novogradac to broadly adopt Teams, but it's been quite remarkable. But your point about this app that you could put into do and all the rest and keep you on track and all the rest, since we do have our, innovation group that does a lot programming and trying to help technology enhance our business. We'll have to talk to Brad Weinberg, who heads up that group and see what he can develop

So thank you again, John, for joining me on the podcast today, particularly in the height of busy season. And to our listeners, I'm Mike Novogradac. Thanks for listening.

Additional Resources

Email

John Sciarretti

CPAs@Novoco.com

QOF Report Blog Posts

QOFs Tracked by Novogradac Reach $34.09 Billion in Equity Raised, Nearly $10 Billion in 2022

Residential Investment Remains Leading Focus for QOFs Tracked by Novogradac

Washington, D.C., Tops List for Planned QOF Investment; 54 Cities Surpass $100 Million Mark

Largest QOFs Continue to Raise Majority of Equity; 'Super QOFs' Keep Increasing

Opportunity Zones Working Group

More information

Letters to IRS