Opportunity Zones 101

The Context

52.3M
AMERICANS

live in economically distressed communities. Between 2000 and 2015, more than half of these communities experienced a decline in both jobs and businesses.

FROM 2010 TO 2016

three-quarters of net job growth occurred in a narrow selection of metropolitan areas, resulting in inequalities across the country.

67% OF JOB GROWTH

comes from small businesses, for whom the most important variable for success is access to capital.

Source: Milken Institute Analysis

What is an Opportunity Zone?

- Enacted by the 2017 Tax Cuts and Jobs Act, a census tract designated by each state or territory and certified by Treasury as eligible to receive private investments via Qualified Opportunity Funds.

- Meets definition of a "low-income community" (LIC), or …

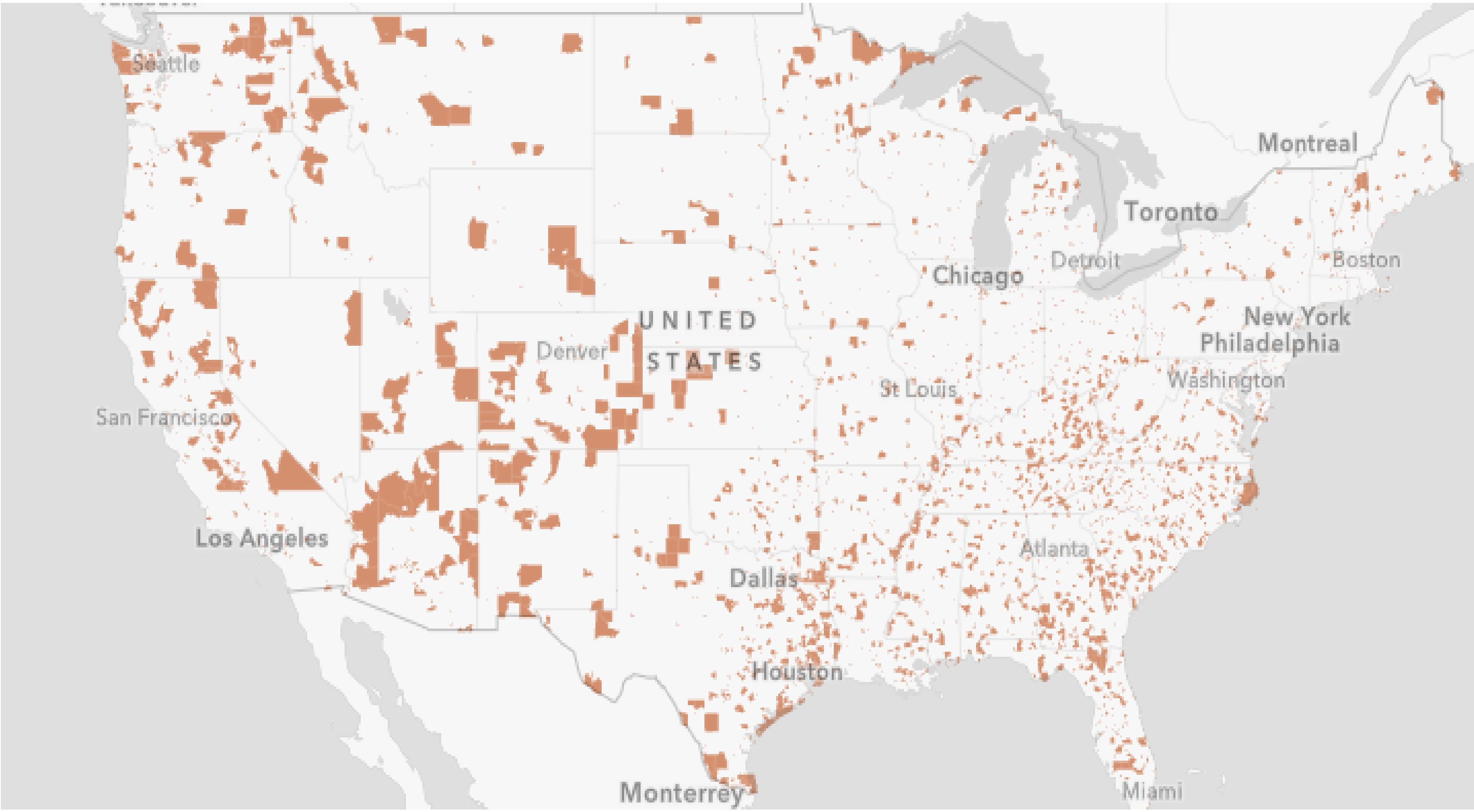
- Contiguous to a LIC and with a median family income that doesn't exceed 125% of the LIC.

- 10-year designation as an Opportunity Zone.

- More than 8,700 Opportunity Zones have been designated in the 50 U.S. states, the District of Columbia and five U.S. territories.

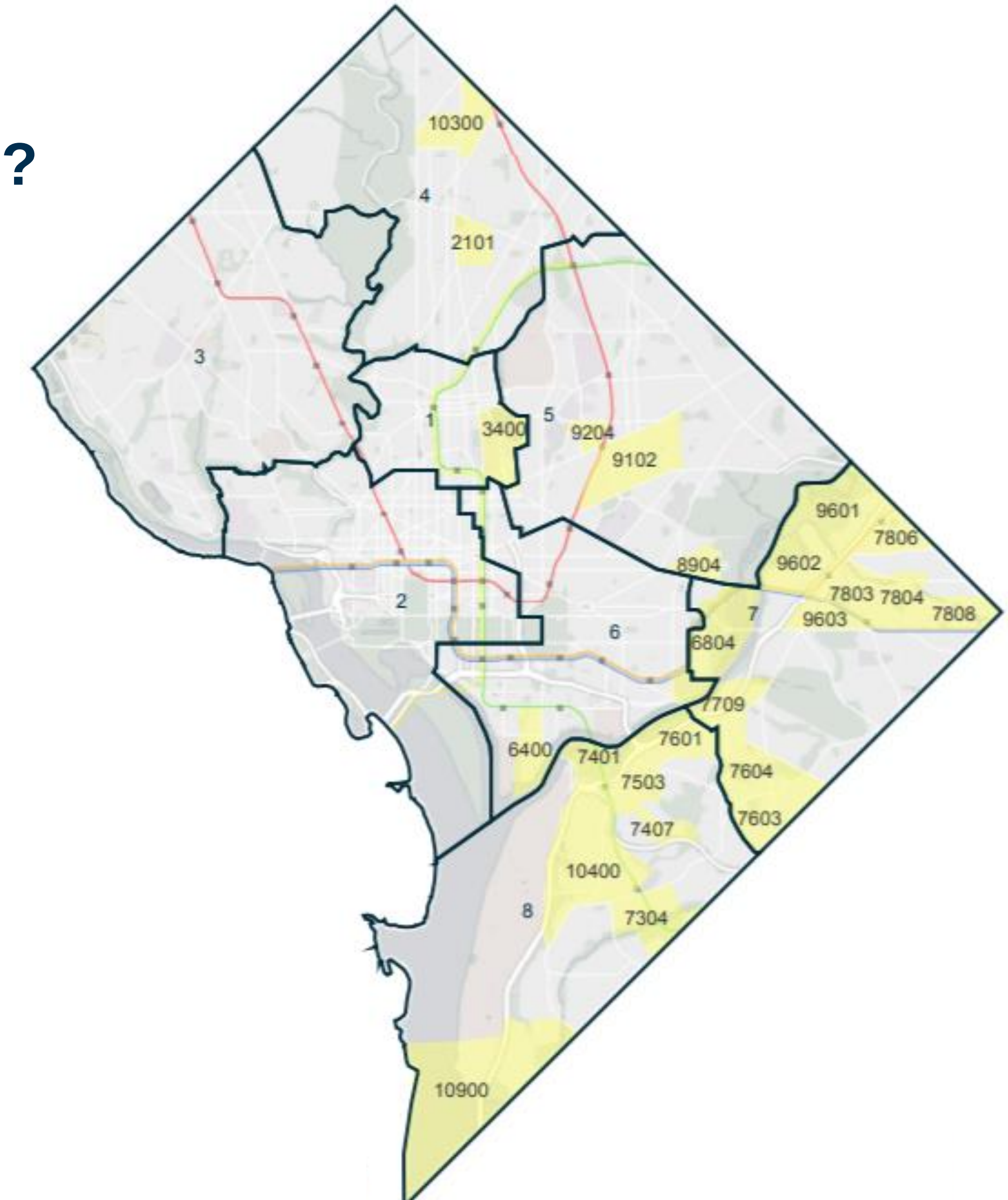
Source: Milken Institute Analysis, 2017 Tax Cuts and Jobs Act: Subchapter Z

Nationally, where are the Opportunity Zones?



Source: Economic Innovation Group

Where are the DC Opportunity Zones?



Source: Office of the Deputy Mayor for Planning and Economic Development

What is a Qualified Opportunity Fund?

- An investment vehicle set up as a partnership or corporation for the purpose of investing in eligible property that is located in Opportunity Zones.

- Qualified Opportunity Funds are capitalized by realized capital gains, within 180 days of being realized. If funds own assets directly 90% must be in the zones; if indirectly via business investment, 70% must be in the zones. Tested every 6 months.

- Broad definition of eligible investments, including real estate and operating companies. Investments in existing real estate and business projects are subject to improvement tests (100% of basis); new business formations are not.

- Qualified Opportunity Funds must self-certify they meet all requirements. IRS draft forms and first round of regulations released 4Q18. Additional revenue guidance forthcoming.

Source: Milken Institute Analysis, 2017 Tax Cuts and Jobs Act: Subchapter Z

How Do the Tax Benefits Work?

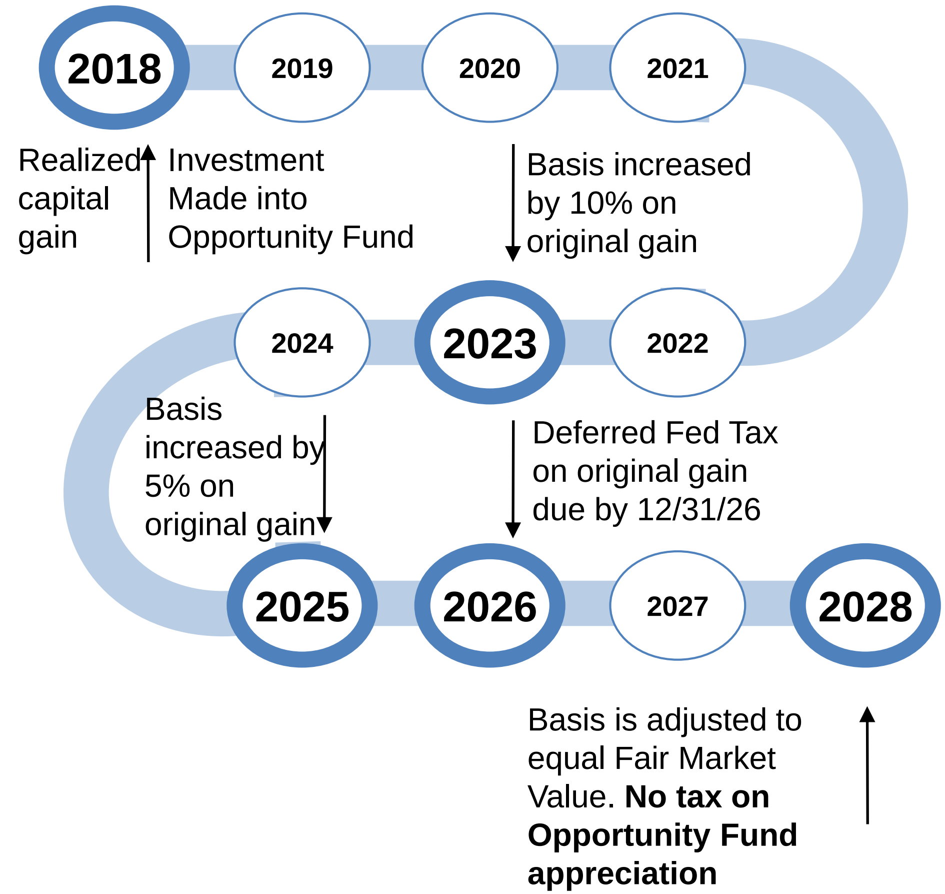
- Opportunity Funds may provide potential Federal tax incentives to investors (1,2,3)

- **Benefit 1:** A temporary capital gains tax deferral for all newly realized capital gains reinvested in an Opportunity Fund, lasting until the investment is sold or December 31, 2026, whichever is sooner.

- **Benefit 2:** A 10 percent basis adjustment on the original capital gains, which can result in tax reductions if the Opportunity Fund investment is held for 5+ years; plus an additional 5 percent adjustment if the investment is held for 7+ years.

- **Benefit 3:** If an investor holds the Opportunity Fund investment for 10+ years, the investor also may permanently avoid capital gains taxes on any proceeds from the Opportunity Fund investment itself.

Timeline of tax benefits *(4)*



1 Milken Institute does not provide investment advice and any information contained in this document is for informational purposes only and does not constitute financial, accounting, or legal advice.
2 IRS Revenue Guidelines are required for clarification and have yet to be released
3 For a more detailed explanation of Opportunity Zones and Qualified Opportunity Funds, please visit: irs.gov and cdfifund.gov.
4 Kosmont Companies graphic

Some Considerations for OZ Businesses

- **Revenue:** 50% of a company's total gross income must be derived from active conduct in the Zones.

- **Tangible Assets:** qualified opportunity funds must maintain 90% of their assets in the zone. If owning assets directly, 90% must be in the zones; if owning indirectly via business investment, 70% must be in the zones.

- **Business Property:**
  - Tangible property of the QOF acquired by the QOF after 2017 from unrelated party (<20% ownership).
  - "Original use" or "substantially improved"

- **Operating Losses:** a Working Capital Safe Harbor exists for business expenses related to the acquisition, construction, and/or substantial improvement of tangible property, but this may not provide comfort for start-ups or businesses that aren't "asset heavy."