PitchBook

A Window of Opportunity

An overview and analysis of Opportunity Zones

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Introduction

While the *Tax Cuts and Jobs Act of 2017* garnered attention for its cuts to income taxes, it also introduced the *Investing in Opportunity Act*, a piece of legislation that uses tax breaks to incentivize investment in low-income communities referred to as Qualified Opportunity Zones (QOZs). The legislation dictates that if taxpayers reinvest capital gains from recent investments into Qualified Opportunity Funds (O-Funds), vehicles organized for the express purpose of investing in QOZs, they may be eligible to receive preferential tax treatment. With an estimated $6.1 trillion of capital gains income tied up in capital markets, the act could funnel an unprecedented sum of private capital toward community development.[1]

Given that regulations are not yet finalized, many investors are still waiting for guidance on vaguely worded parts of the legislation. Early movers, however, have mobilized funds to capitalize on the opportunity.

In this analyst note, we review the legal definitions of QOZs and O-Funds and provide a high-level overview of tax incentives as outlined by the IRS. We also review considerations for investors and potential externalities for residents of QOZs.

1: "Opportunity Zones: Tapping into a $6 Trillion Market," Economic Innovation Group, March 21, 2018

Published on February 21, 2019

Key takeaways include:

- The QOZ legislation is particularly well suited for real estate and impact investors as nuances of the tax code narrow investable opportunities to businesses primarily serving communities in QOZs and properties that are majority-operated in a QOZ. VCs may find it challenging to find investable opportunities given a restriction in the current legislation that requires at least 50% of an investee's gross income to come from within the QOZ.

- We expect to see commercial real estate investors concentrate QOZ investments in up-and-coming census tracts such as downtown areas, suburbs, or college towns that will deliver high yields. Impact investors, however, will likely target more economically distressed regions in order to realize the legislation's economic development goals.

- The legislation could create a host of externalities for recipient communities including job creation, economic development, and—most concerning—price inflation. The effects of QOZ investments on recipient communities will be largely influenced by how investors and communities do or do not engage with one another.

*A **Qualified Opportunity Zone (QOZ)** is a low-income census tract or a census tract contiguous to an LIC, designated by the US government to be eligible to receive investment from O-Funds.*

What is a Qualified Opportunity Zone?

Officially enacted on December 22, 2017, the *Investing in Opportunity Act* introduced the concept of a QOZ, which the IRS defines as "an economically-distressed community where new investments, under certain conditions, may be eligible for preferential tax treatment."[2] QOZs were identified in 2018 through a process whereby state governors nominated up to 25% of eligible census tracts in their state. Census tracts eligible for nomination had to meet the IRS' definition of a low-income community (LIC) or being contiguous with LICs.[3]

According to data released by the CDFI Fund, 8,764 of the 41,133 eligible census tracts were selected to receive the QOZ designation, which they will retain for 10 years.[4]

Table 1: Proportion of eligible low-income and contiguous census tracts selected for QOZ designation

QOZs	Designated	Eligible	% selected
LIC	8,566	31,680	27.0%
Contiguous	198	9,453	2.1%
Total	8,764	41,133	21.3%

Source: CDFI Fund

*A **Qualified Opportunity Fund (O-Fund)** is a vehicle organized for the purpose of investing in QOZs. By reinvesting recently realized capital gains into an O-Fund, investors can receive preferential tax treatment.*

How do taxpayers invest in QOZs?

Investors can tap into tax benefits by reinvesting capital gains income into an O-Fund. Per the IRS, capital gains must be rolled into a fund within 180 days of the event in which the gains were recognized. Any taxpayer that can recognize capital gains on the sale of an asset is eligible to invest in an O-Fund. It is worth noting that taxpayers cannot receive tax benefits by making direct investments in QOZ businesses or property—investments are only eligible for preferential tax treatment if made indirectly through the O-Fund intermediary.

2: "Opportunity Zones Frequently Asked Questions," IRS
3: The IRS defines a low-income community as a census tract where "the poverty rate for such tract is at least 20%, or in the case of a tract not located within a metropolitan area, the median family income for such tract does not exceed 80% of statewide median family income, or in the case of a tract located within a metropolitan area, the median family income for such tract does not exceed 80% of the greater of statewide median family incom or the metropolitan area median family income." The IRS indicates that a non-low-income census (LIC) tract is still eligible to be a QOZ if it is "contiguous with an LIC that is designated as a QOZ (the contiguous LIC QOZ need not be in the same State)" and "the median family income of the non-LIC tract does not exceed 125% of the median family income of that contiguous LIC QOZ." The IRS states, however, that "not more than 5% of the tracts designated [as a QOZ] in a State may be non-LIC, contiguous tracts."
4: "Designated Qualified Opportunity Zones," CDFI Fund, December 14, 2018

O-Funds can be structured as a corporation (c- or s-corp) or partnership and must be organized for the purpose of investing in QOZ properties. If the investor is classified as either of the above, it can self-certify as an O-Fund by filing Form 8996 (of which only early forms are yet available). While there is no restriction on preexisting entities self-certifying as O-Funds, any investments made prior to the fund's certification as an O-Fund are not eligible for tax benefits.

90% of the O-Fund's assets must be holdings in a QOZ business or property at all points throughout the fund's life. The 90% asset base is tested semiannually, and if the amount falls short of the 90% requirement, investors must pay a penalty fine for each month the fund fails to meet the requirement.[5]

What are the restrictions on eligible investments (QOZ businesses and properties)?

Per the IRS, only equity investments (including preferred equity and partnership interests) are eligible for tax benefits. Funds can make debt investments, but they will not receive the same preferential tax treatment. Equity interest must be original issue stakes in QOZ businesses and properties and must be purchased after December 31, 2017.

QOZ businesses are defined as having "substantially all of the tangible property" owned by the business in the QOZ. Additionally, at least 50% of total gross income derived from the conduct or trade of the business must come from activity within the zone. If this rule is violated, the business is no longer qualified, and the O-Fund investor will need to adjust accordingly to ensure its holdings still meet the 90% rule.

Funds cannot invest in the following businesses: golf courses, country clubs, massage parlors, hot tub facilities, suntan facilities, racetracks or gambling facilities, and liquor stores. Real estate property cannot be bought from an individual or entity related to the O-Fund.

Additionally, the IRS specifies that either i) the "original use" of the property must begin with the O-Fund (for example, a greenfield construction project) OR ii) that the O-Fund must substantially improve the property (by doubling the base of the property within 30 months of acquisition).[6]

5: "Federal Register, Vol. 83, No. 209," GPO, October 29, 2018
6: Ibid.

Tax incentives

Here we provide an overview of tax incentives outlined in the IRS' QOZ guidance released on October 29, 2018. We also outline a simple example of possible returns from investment in an O-Fund versus gains reinvested in a comparable asset. Investors, service providers, and researchers are still waiting for clarification on a several vague points before proceeding.

Table 2: Summary of preferential tax treatment for capital gains reinvested in QOZs

Asset	After 5 holding years	After 7 holding years	After 10 holding years
Capital gains rolled into O-Fund*	Base of capital gains tax liability is reduced by 10%. Recognition of capital gains in taxable income can be deferred until either the O-Fund investment is sold or December 31, 2026.	Base of tax liability is reduced an additional 5% for a 15% total reduction.	Base of tax liability maintains 15% reduction.
Additional gains from O-Fund investment	Any gains in excess of original investment value are subject to 20% capital gains tax.	Any gains in excess of original investment value are subject to 20% capital gains tax.	Any gains in excess of original investment value become tax-exempt.

Source: IRS

**In all instances, the capital gains tax liability rolled into an O-Fund is still subject to 20% capital gains tax if the asset is sold.*

Per the IRS, the following tax benefits apply to capital gains income invested in an O-Fund:

- Capital gains income may be temporarily deferred until the earlier event of either: 1) the investment being sold, or 2) at December 31st, 2026, at which point the tax liability must be recognized in taxable income.
- Investors that hold the investment for five years may reduce the tax base of the original liability by 10%. Investors that hold investments for seven years earn an additional 5% reduction on the tax base of the original capital gain income for a 15% total reduction. Any additional investment income created by the fund in excess of the original capital gains investment is still subject to capital gains tax. However, if investors hold for 10 years, appreciation on the reinvested gains become tax-exempt and the original tax liability also retains the 15% base reduction.
- The December 31, 2026 timeline acts as a hard stop for liability reductions, incentivizing taxpayers to invest in O-Funds by the end of 2019 to realize the maximum benefit of the seven-year holding period.[7]

7: "Federal Register, Vol. 83, No. 209," GPO, October 29, 2018

Table 3: O-Fund tax advantage breakdown by holding period for $100 million investment, assuming no appreciation of the asset*

		End of year 1** *Tax on capital gains invested in O-Fund is temporarily deferred.*	End of year 5 *Initial tax base of O-Fund is reduced 10%.*	End of year 7 *Initial tax base of O-Fund is reduced additional 5%.*	End of year 10 *Initial tax base of O-Fund maintains 15% reduction.*
Asset	Asset value ($M)	$100.00	$100.00	$100.00	$100.00
	Asset appreciation ($M)	--	--	--	--
O-Fund	Tax base ($M)	DEFERRED	$90.00	$85.00	$85.00
	Asset value net taxes ($M)	$100.00	$82.00	$83.00	$83.00
Comparable asset	Tax base ($M)	$100.00	$100.00	$100.00	$100.00
	Asset value net taxes ($M)	$80.00	$80.00	$80.00	$80.00
O-Fund tax savings ($M)		--	$2.00	$3.00	$3.00
O-Fund tax savings as % of asset value net taxes		--	2.44%	3.61%	3.61%

Source: PitchBook
**This table is for illustrative purposes only.*
***This example assumes assets are held for at least one year. At five-, seven-, and 10-year holding periods, final asset values net of taxes are calculated assuming the asset is sold in the specified year.*

In the case of no appreciation of the O-Fund asset, there is no additional tax benefit for holding more than seven years.

Table 3 illustrates the effects of the preferential tax treatment on the tax base of capital gains income when reinvested in an O-Fund versus a traditional fund. For the sake of simplicity, we start by assuming no appreciation in fund assets over time. If an investor commits $100 million of capital gains income to an O-Fund at the beginning of 2019, the capital gains tax liability is deferred until the fifth year of holding. At five years, the base for the tax liability is reduced by 10% to $90 million. At seven years, the base of the liability is reduced an additional 5% (15% in total) to $85 million. At 10 years, the base for the liability retains the 15% reduction, so the investor will pay capital gains tax on $85 million. Because this example assumes a constant fund value over time, the investor does not need to account for capital gains tax on any additional investment income created by the fund.

If the fund does generate investment income, however, the investor must also incorporate tax considerations for the appreciation of the original $100 million investment.

Table 4: O-Fund tax advantage breakdown by holding period for $100 million investment, assuming 9% asset appreciation annually and 20% capital gains tax rate*

		End of year 1 *Tax on capital gains invested in O-Fund is temporarily deferred.*	End of year 5 *Initial tax base of O-Fund is reduced 10%. Appreciation is still subject to capital gains tax.*	End of year 7 *Initial tax base of O-Fund is reduced an additional 5%. Appreciation is still subject to capital gains tax.*	End of year 10 *Initial tax base of O-Fund maintains 15% reduction. Appreciation becomes tax-exempt.*
Asset	Asset value ($M)	$109.00	$153.86	$182.80	$236.74
	Asset appreciation ($M)	$9.00	$53.86	$82.80	$136.74
O-Fund	Capital gains tax base ($M)	DEFERRED	$90.00	$85.00	$85.00
	Capital gains tax liability ($M)	DEFERRED	($18.00)	($17.00)	($17.00)
	Appreciation tax liability ($M)	($1.80)	($10.77)	($16.56)	$0.00***
	Asset value net taxes ($M)	$109.00	$125.09	$149.24	$219.74
Comparable asset	Asset tax base ($M)	$109.00	$153.86	$182.80	$236.74
	Tax liability ($M)	($21.80)	($30.77)	($36.56)	($47.35)
	Asset value net taxes ($M)	$87.20	$123.09	$146.24	$189.39
O-Fund tax savings ($M)		--	$2.00	$3.00	$30.35
O-Fund tax savings as % of asset value net taxes		--	1.6%	2.0%	13.8%

Source: PitchBook
*This table is for illustrative purposes only.
**This example assumes assets are held for at least one year. At five-, seven-, and 10-year holding periods, final asset values net of taxes are calculated assuming the asset is sold in the specified year.
***This figure would be -$27.35 million without tax exemption.

Table 5: O-Fund and comparable asset IRRs by holding period, assuming 9% asset appreciation annually*

	5 holding years	7 holding years	10 holding years
O-Fund	4.58%	5.89%	9.14%
Comparable asset	4.24%	5.58%	7.35%
Difference	0.34%	0.31%	1.79%

Source: PitchBook
*This table is for illustrative purposes only.

We use the same example to illustrate tax outcomes at five-, seven-, and 10-year horizons, this time assuming the fund's value appreciates 9% annually for 10 years.

If investors were to sell an asset at the five-year holding period, they would save \$2.0 million in taxes compared to a similar reinvestment in a comparable asset appreciating at the same rate, creating a 0.34% premium in five-year returns over that period. At seven years, we see \$3.0 million in tax savings over the alternative and a 0.31% differential between O-Fund returns over the comparable asset. Finally, the 10-year holding period produces the most staggering tax benefits. While the tax base of the original capital gains liability maintains the 15% reduction (again saving \$3.0 million on the capital gains liability), the investor also enjoys a full tax exemption on additional gains from the fund investment, which would equate to over \$27.35 million in savings. We also see a 1.79% differential between returns on the two comparable investments in favor of the O-Fund investment. Assuming a significant appreciation in the fund's assets, holding an investment for at least 10 years is the most beneficial from a tax perspective.

Outstanding questions

Many aspects of the proposed legislation and IRS guidance are still in need of clarification. Although the IRS is expected to publish updates in the coming months, numerous questions remain outstanding. Among the most pressing are:

- Once a QOZ loses its designation, will investors retain the ability to claim tax liability reductions if they invest before the 10-year window?
- Do individual investors need to be accredited? As currently worded, the proposed legislation seems to imply *any* individual investor can participate, which may allow non-accredited investors a loophole to invest in private market investment vehicles.
- What is the tax treatment of additional gains from the fund that are reinvested back into the fund?
- How will preferential tax treatment of O-Funds interact with other preferential tax treatment from incentives like 1031 exchanges, qualified small business stock, the New Markets Tax Credit (NMTC), and so on?
- What conduct would lead to a fund being declassified as an O-Fund?

Implications for investors

The success of a fund will depend heavily on an investor's experience with and understanding of the local market, and subsequently, the investor's ability to source quality investment opportunities.

While the underlying assets of O-Funds are expected be predominately real estate property, commercial infrastructure, and equity stakes in local business, the risk and return considerations of an O-Fund will vary significantly depending on which QOZs the fund targets and on the underlying assets of the fund. Additionally, the success of a fund will depend heavily on an investor's experience with and understanding of the local market, and subsequently, the investor's ability to source quality investment opportunities.

Real estate

The legislation leans heavily in favor of real estate investments, given the requirements for "substantially all" of a business' property and at least 50% of gross income to be generated within a QOZ. Taking into consideration the backdrop of the local markets and business ecosystems, we expect to see more commercial real estate investors concentrate capital in up-and-coming census tracts such as downtown areas, suburbs, or college towns. The legislation does not require investors to disburse capital evenly across urban or rural geographies, so investors have free reign to focus investment in regions they perceive to be less risky and/or have high-yield potential. Real estate investment management firm JLL highlights fast-growing urban areas such as downtown Los Angeles, for instance, as "likely to be favored by developers."[8] These O-Funds may produce healthy financial returns for investors but may lack in their contribution to the economic development of a region—the intended purpose of the legislation.[9]

So far, a number of real estate investors have announced they are raising large-scale O-Funds. The CIM Group, for example, recently filed tax documents with the SEC to launch a $5 billion O-Fund that is reportedly focused on large metropolitan areas including Los Angeles, San Francisco, and Chicago, among others.[10] Virtua Partners has also announced the raise of a $200 million vehicle that is expected to finance the development of a Marriott hotel, single-family townhomes, and an apartment complex near the local university in Phoenix, AZ; Virtua notes that these projects would have been done with or without an O-Fund.[11]

8: "What Investors Need to Know About Opportunity Zones," JLL, November 8, 2018
9: "Opportunity Zones: An Analysis of the Policy's Implications," State Tax Notes, Rebecca Lester, Cody Evans & Hannah Tian, October 15, 2018
10: "CIM Group to Launch $5B Opportunity Fund," Bisnow, Allison Nagel, January 25, 2019
11: "New Hotel or Affordable Housing? Race Is On to Define Opportunity Zones," The Wall Street Journal, Ruth Simon and Richard Rubin, July 13, 2018

Venture capital

While VC investments seem a natural fit for QOZ investments, restrictions stating that at least 50% of a business' income must come from within the QOZ, may severely limit investable opportunities for traditional VC funds.

VC investments may also seem like a natural fit given that qualifying investments must be equity stakes, but a VC strategy may prove more challenging to execute in QOZs. The aforementioned requirement, that at least 50% of a business' income must come from business activities within the QOZ, may severely limit investable opportunities for traditional VC funds. Venture strategies are typically predicated on fomenting exponential growth, which almost assuredly means scaling operations to a national or global level. While startups at the earliest stages may meet the QOZ requirements, a large share of their revenue is likely to be derived outside of the company's locale as they scale. This is particularly salient for software companies or online businesses that might be headquartered in a QOZ but serve customers anywhere.

Investors, including Steve Case (Revolution Ventures, AOL) and Sean Parker (Hypothesis Ventures, Napster), had announced intentions to invest in QOZs before the IRS guidance released in October 29, 2018. However, the restrictive income requirements introduced in the guidance appears to have venture investors taking a step back. There is hope that the final tax rules will be amended to open up investable startup opportunities, pegging requirements more closely to the headquarter of a business rather than its customers.[12]

Impact investing

In our opinion, impact investors and community development entities (CDEs) investing in social enterprises and affordable housing opportunities are best positioned to deliver on the legislation's economic development goals seeing as they are a source of capital expected to focus on more economically disadvantaged regions some other investors may perceive as too risky.[13] Whether investors will accept concessionary returns in exchange for high-impact projects or target market-rate returns remains to be seen. Because social enterprises often serve consumers or businesses in underserved or low-income demographics, they may not have as much difficulty deriving the majority of their revenue from within a QOZ, though scaling may still be a challenge given the previously mentioned restrictions.

12: "Capital Gains Tax Gift Gets Dialed Back for Tech Investors," Accounting Today, Noah Buhayar, October 31, 2018
13: The Social Enterprise Alliance defines social enterprises as "Organizations that address a basic unmet need or solve a social or environmental problem through a market-driven approach."

In terms of affordable housing, many impact investors and CDEs have experience investing in such projects following their engagement with NMTC, an existing tax incentive program encouraging investment in economically disadvantaged regions, similar to QOZs (more details below). There's potential here for the tax benefits to create a greater yield in affordable housing investments, attract co-investment from more commercial investors, or even combine O-Fund benefits with NMTC incentives.[14]

Some of the announced impact-oriented projects thus far include Access Venture's Blueprint Texas fund and the Oregon Opportunity Zone Initiative. The Blueprint Texas fund is a partnership between a number of experienced investors from Access, Village Capital, and Brown Advisory that intends to prioritize community engagement and development indicators in its startup and real estate investments. The Oregon Opportunity Zone Initiative is also led by a partnership, in this case local foundations and local economic development agencies, to focus on the most underserved regions of Oregon.[15]

14: "Pairing NMTCs with Opportunity Zone Incentives," Novogradac, George Barlow & John Sciarretti, April 5, 2018
15: "Oregon Opportunity Zone Initiative," Mission Investors Exchange, August 2018

Community development finance institution is an umbrella term that encompasses private-sector, community-focused banks, credit unions, and lending institutions that serve low-income communities in every state throughout the US.

The NMTC & CDFIs: A brief history of community development in the US

This section provides an introduction to the community development finance institution (CDFI), a key component of financial infrastructure in a low-income community, and reviews historical tax legislation similar to the *Investing in Opportunity Act*. By observing the results of previous similar programs, we can make informed expected externalities of the current legislation.

CDFIs have long been a key component of community development in the US, as they provide access to credit and financial services for low-income communities. CDFI is an umbrella term that encompasses private-sector, community-focused banks, credit unions, and lending institutions that serve low-income communities in every state throughout the US. CDFIs are certified and funded by the US Treasury's CDFI Fund, a federal government agency founded in 1994 to support the development of regional CDFIs.[16] With regard to the QOZ legislation, CDFIs will likely play a critical part in brokering financial relationships between communities and investors, as they tend to keep a close pulse on local residents and also act as a financial representative for many low-income communities.

The *Community Renewal Tax Relief Act* of 2000 introduced the New Markets Tax Credit (NMTC) program, a program that has leaned heavily on CDFIs as intermediaries between investors and recipient communities.

The NMTC program provides individual and corporate investors relief from income taxes in exchange for equity investments in Community Development Entities (CDEs). CDEs are community entities such as CDFIs, government institutions, or nonprofits that are certified by the US Treasury's CDFI Fund and have a primary mission to serve low-income communities or individuals (the majority of entities that received the CDE certification are CDFIs, according to research from the Tax Policy Center).[17] Using cash infusions from equity investments, CDEs may act as financial intermediaries by providing investors with credits against their federal income tax and using their equity investments to make loans and equity investments in local businesses, manufacturing facilities, commercial properties, healthcare facilities, schools, and a number of other projects.[18]

The NMTC has seen relatively successful implementation, with the national CDFI Fund reporting that for every $1 in government investment, the NMTC has brought about $8 in private investment and has disbursed a total $54 billion in tax credits as of 2017.[19,20] Those critical of the program, however, assert that what was intended to revitalize low-income communities ended up as a means for tax breaks for real estate investors.

Still, research aggregated by Stanford suggests that the NMTC has had small positive effects on the poverty rate and employment, though the subsequent increase in prices may have crowded out the residents the act initially intended to serve. The researchers note that the similarities between the NMTC and QOZs legislation provide insight into potential expected outcomes; however, the relatively less stringent QOZs legislation could produce greater effects by inviting a broader swath of investors and larger scale of capital.[21]

16: "What Are CDFIs?," CDFI Coalition
17: "The Tax Policy Center's Briefing Book," Tax Policy Center
18: "New Markets Tax Credit," IRS, May 2010
19: "New Markets Tax Credit Program," CDFI Fund
20: "NMTC Qualified Equity Investment Report," CDFI Fund, December 3, 2018
21: "Opportunity Zones: An Analysis of the Policy's Implications," State Tax Notes, Rebecca Lester, Cody Evans & Hannah Tian, October 15, 2018

Potential externalities for communities

The QOZ legislation has the potential to be either an unprecedented windfall for recipient communities or a harbinger of inflated cost of living. With a unique opportunity to invite large-scale investment, engender job creation, and create trickle-down wealth for local residents, many municipal governments and CDFIs are actively strategizing how to market and prepare their communities to receive investment.

Cost of living

Among the chief concerns expressed by communities is the possibility that investment from O-Funds will drive up pricing in housing and consumer goods, which will make the cost of living unmanageable for original residents of low-income census tracts, forcing them to move elsewhere. While some level of price increases is inevitable with economic development, the key question faced by communities and local governments is how they will assuage gentrification and accrue benefits for the intended population. Some governments are hoping to include provisions for the benefit of local communities in QOZ deals, such as regional beautification, so that residents in spaces surrounding new developments will also be able to participate in the upside of increased housing prices.

Job creation

O-Funds carry the potential to spur economic revitalization that will create and improve the quality of jobs. The first source of increased employment could be from labor needed for real estate, infrastructure, and construction projects, should such projects source from the local community. Local businesses that receive investment could also source talent locally, creating another new, quality source of employment for local residents. Additionally, a stronger business environment could bring in a "rising tide that will lift all boats," spurring employment in surrounding businesses as well. Findings aggregated by Stanford researchers point to small but positive effects on employment rates from a program similar to QOZs, the NMTC.[22]

22: "Opportunity Zones: An Analysis of the Policy's Implications," State Tax Notes, Rebecca Lester, Cody Evans & Hannah Tian, October 15, 2018

More capital

Proposed budget cuts threaten reduced capital previously allocated to funding CDFIs and, sequentially, low-income communities. While funding has seen a slight cut so far (rather than total removal), O-Funds may fill potential gaps created by CDFI budget cuts and extend sources of growth capital for businesses outside of debt instruments. In our previous report on VC ecosystems, we discuss how financial resources are one of the three key components to the development of entrepreneurial ecosystems. For regions with a scarcity of risk capital, O-Funds (particularly those managed by impact investors) could be catalytic factors in developing such ecosystems. However, some QOZs may be more suited to intake large infusions of capital than others. Funds raising billion-dollar sums, for example, might target census tracts in larger metropolitan areas such as Los Angeles rather than rural regions with small local markets. Additionally, market dynamics could very well push a majority of funding toward regions with lower perceived risk and higher potential return expectations rather than underserved communities most in need of capital.

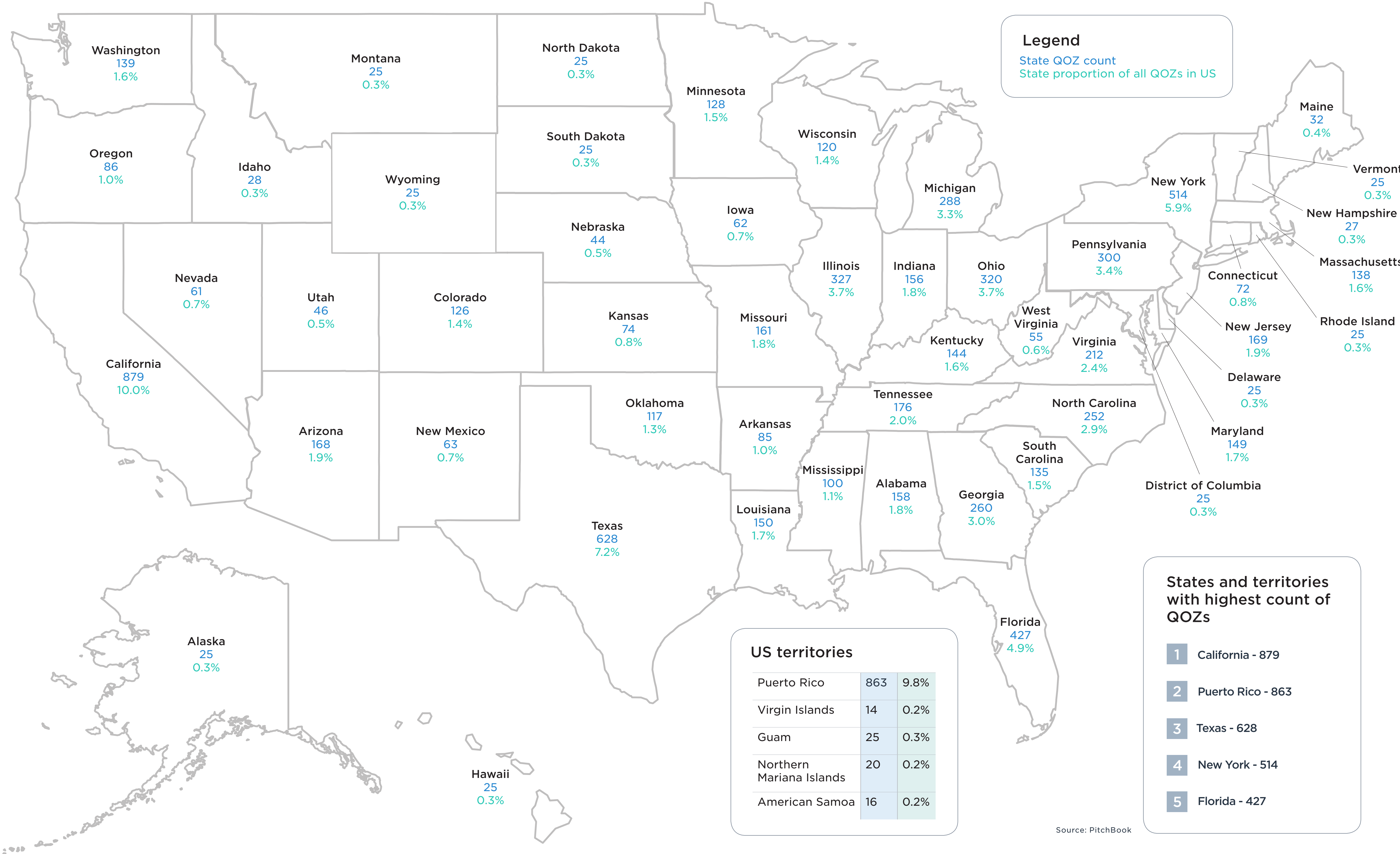
Conclusion

As the current legislation stands, real estate investors and impact investors are best positioned to take advantage of tax benefits, as the restrictions on where a business derives its revenue limit the ways tech investors can participate via startup investment. Whether the IRS amends this restrictive language will inform the participation of venture investors in QOZ.

In terms of economic development, the ways that investors and communities do—or do not—engage with one another will play a large part in how the program develops. Municipal governments, CDFIs & CDEs, and nonprofit organizations throughout the US are galvanizing to attract and curate investment in local business and real estate and ensure residents can participate in the upside of any economic development. Washington state's Thurston Economic Development Council, for example, has developed an online platform called "Opportunity Zone Investments" (OZI) that lets QOZ businesses and properties list and be discovered by potential investors. The Council is also using its OZI program to help local investors with capital gains create or invest in an O-Fund. In lieu of large-scale investment, these local programs can facilitate the creation of smaller, community-focused funds that also put profits back into the pockets of residents.

Qualified Opportunity Zones in US

Total QOZs: 8,764



US territories

Puerto Rico	863	9.8%
Virgin Islands	14	0.2%
Guam	25	0.3%
Northern Mariana Islands	20	0.2%
American Samoa	16	0.2%

States and territories with highest count of QOZs

1. California - 879
2. Puerto Rico - 863
3. Texas - 628
4. New York - 514
5. Florida - 427

Source: PitchBook

Table 6: US QOZs and 2018 VC deal activity by state/territory

Region	State/territory	QOZ count	State % of total	VC deal count	Capital invested ($B)
Great Lakes	Illinois	327	3.73%	253	$1.99
Great Lakes	Indiana	156	1.78%	95	$0.37
Great Lakes	Michigan	288	3.29%	114	$0.47
Great Lakes	Minnesota	128	1.46%	125	$0.78
Great Lakes	Ohio	320	3.65%	152	$1.06
Great Lakes	Wisconsin	120	1.37%	79	$0.26
Mid-Atlantic	West Virginia	55	0.63%	2	$0.01
Mid-Atlantic	Pennsylvania	300	3.42%	273	$1.51
Mid-Atlantic	Virginia	212	2.42%	154	$0.78
Mid-Atlantic	New Jersey	169	1.93%	97	$0.74
Mid-Atlantic	New York	514	5.86%	1,076	$13.52
Mid-Atlantic	Maryland	149	1.70%	139	$1.33
Mid-Atlantic	Delaware	25	0.29%	55	$0.19
Mid-Atlantic	District of Columbia	25	0.29%	62	$0.68
Midwest	Iowa	62	0.71%	34	$0.08
Midwest	Kansas	74	0.84%	22	$0.16
Midwest	Missouri	161	1.84%	75	$0.36
Midwest	Nebraska	44	0.50%	19	$0.03
Midwest	North Dakota	25	0.29%	7	$0.02
Midwest	South Dakota	25	0.29%	3	$0.02
Mountain	Utah	46	0.52%	108	$1.16
Mountain	Wyoming	25	0.29%	7	$0.01
Mountain	New Mexico	63	0.72%	19	$0.09
Mountain	Nevada	61	0.70%	39	$0.11
Mountain	Montana	25	0.29%	10	$0.04
Mountain	Colorado	126	1.44%	289	$1.60
Mountain	Idaho	28	0.32%	27	$0.06
Mountain	Arizona	168	1.92%	92	$0.62
New England	Maine	32	0.37%	23	$0.03
New England	Connecticut	72	0.82%	96	$0.64
New England	New Hampshire	27	0.31%	32	$0.12
New England	Massachusetts	138	1.57%	675	$11.70
New England	Vermont	25	0.29%	24	$0.04
New England	Rhode Island	25	0.29%	21	$0.05
Other Territory	Puerto Rico	863	9.85%	3	$0.00
Other Territory	Virgin Islands	14	0.16%	--	--
Other Territory	Guam	25	0.29%	--	--
Other Territory	Northern Mariana Islands	20	0.23%	--	--
Other Territory	American Samoa	16	0.18%	--	--
South	Oklahoma	117	1.34%	14	$0.07

South	Kentucky	144	1.64%	37	$0.09
South	Louisiana	150	1.71%	10	$0.02
South	Arkansas	85	0.97%	27	$0.05
South	Tennessee	176	2.01%	80	$0.23
South	Texas	628	7.17%	441	$3.01
Southeast	South Carolina	135	1.54%	38	$0.08
Southeast	Alabama	158	1.80%	21	$0.03
Southeast	Florida	427	4.87%	245	$1.82
Southeast	Georgia	260	2.97%	121	$1.15
Southeast	North Carolina	252	2.88%	186	$2.65
Southeast	Mississippi	100	1.14%	6	$0.01
West Coast	Oregon	86	0.98%	112	$0.54
West Coast	Hawaii	25	0.29%	6	$0.01
West Coast	Alaska	25	0.29%	3	$0.00
West Coast	California	879	10.03%	3,224	$77.78
West Coast	Washington	139	1.59%	381	$2.96

Table 7: US QOZs and 2018 VC deal activity by region

Region	QOZ count	% of all QOZs	VC deal count	Capital invested ($B)
Great Lakes	1,339	15.28%	818	$4.92
Mid-Atlantic	1,449	16.53%	1,858	$18.75
Midwest	391	4.46%	160	$0.68
Mountain	542	6.18%	591	$3.69
New England	319	3.64%	871	$12.57
Other Territory	938	10.70%	3	$0.00
South	1,300	14.83%	609	$3.46
Southeast	1,332	15.20%	617	$5.75
West Coast	1,154	13.17%	3,726	$81.29