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Opportunity Zones: 3 Waves of Investment

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Opportunity Zones provide investors with a Federal Tax Incentive and work to encourage re-investment of unrealized capital gains into designated low-income census tracts known as Opportunity Zones.

The initiative launched in 2017 with the passage of the Tax Cuts and Jobs Act to spur private development in postindustrial cities that have been plagued by dwindling populations, blight, and decades-long economic decline, such as Erie, Pennsylvania. Though Opportunity Zones are being leveraged to garner millions of dollars of investment for Erie, critics of the Incentive claim that, as a whole, Opportunity Zones have only added to the capital stack of deals that would have been made regardless of the Tax Incentive—and they're not completely wrong.

The final regulations for Opportunity Zones were released in April 2019, so investors who relied on this Incentive to ensure that their deals penciled-out -- primarily the second-tier market investors -- waited to make their final calculations until after this date. Meanwhile, first-tier market investors with deals that were all but closed were quickly claiming the Opportunity Zones Incentive as extra padding to their capital stack. This left those analyzing the effectiveness of Opportunity Zones up to this point with a **heavily nuanced sample** from which to draw their conclusions.

Since the release of the final Opportunity Zones regulations, a second wave of investment has begun in the second and third-tier markets for which the Initiative was originally intended. Knox Law Public Strategies contends that there are **Three Waves of Opportunity Zones Investment**:

1. **The First Wave of Investment** was made by national investors and was *seen primarily in first-tier markets* like New York City, Los Angeles, and San Francisco. These investors were quick to leverage the Incentive for "low hanging fruit" investments and for deals that would have closed regardless. For this wave, the Incentive simply added to the deal's already existing capital stack, which was not the purpose of the law.
2. **The Second Wave of Investment** is beginning to be seen after the First Wave has begun to subside. This wave is occurring in the *intended economically-distressed areas* by local, regional, and some national investors. Here, the Incentive is helping deals to pencil-out in ways that may not have been possible otherwise and is contributing to the revitalization and rebirth of struggling communities across the nation.
3. **The Third Waveof Investment** will be those Opportunity Zone investments *into businesses*. Investors are now beginning to structure funds to focus on business investments, and we should see activity in

this space starting in 2020.

Opportunity Zones provide a unique tool for which to help rebuild certain portions of our nation. As we assess the effectiveness of the Incentive, it is important to remember that the Second Wave of Opportunity Zones Investment has yet to crest. It has taken decades of economic struggle to produce the need for an Incentive like Opportunity Zones, and we cannot expect that need to be remedied overnight.



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