Opportunity Zones: Nashville, Tennessee

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Introduction

This report will examine the scope and purpose of opportunity zones, focusing on Nashville, Tennessee, finishing with a proposal for regulation to support investment while maintaining community priorities. According to the Economic Innovation Group, a bi-partisan public policy organization, the Opportunity Zone (OZ) program was established to stimulate private sector investment in low-income communities[1]. This bi-partisan effort is focused on helping the economic development of poverty-stricken regions by encouraging an influx of investors through tax incentives. Through research, historical evidence, and expert opinions, an analysis will be conducted that covers the following areas: an overview of opportunity zones, opportunity zone weaknesses, the impact of community engagement, and thematic perspectives. Ultimately, this paper will conclude with a final recommendation on how to best approach Nashville's opportunity zones to ensure a future of collaborative success.

Opportunity Zone Overview

Established by Congress in the Tax Cuts and Jobs Acts of 2017, opportunity Zones were created to encourage long-term investments in low socioeconomic urban and rural communities. To stimulate these investments, this policy allows for investors to re-invest their unrealized capital gains into Opportunity Funds (specific investments vehicles with a sole purpose of investing in Opportunity Zones), therefor foregoing the normally realized taxation of such gains[1]. The more years the investment is held in the zone, the larger the capital gains tax incentive becomes. With a minimum requirement of holdings of five years, leading to a step-up basis of 10%. Additional incentives are provided for investments held over a longer period of time; if held for seven years, one

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will receive a total step-up basis of 10% and if held for the maximum 10-year period, a ceiling step-up basis will be reached at 15%[1].

Furthermore, according to attorney Robert Guth, a leader in the Opportunity Zone legal scene, there are provisions that investments must abide by in order to receive the outlined capital gains incentives. Investments may pursue two avenues, either through an individual fund or through a subsidiary. If following the route of a fund, in order to be eligible for tax incentives, an investor must have at least 90% of their assets invested through a subsidiary or in a new property[2]. Looking at the route of a subsidiary, at least 70% of assets must be invested in either a new opportunity zone property or used to substantially improve an existing property.

Policy Weaknesses

An Enterprise Zone is a geographical area, such as a neighborhood within a city, that has received government incentives such as tax breaks or regulatory exemptions. Given the general similarity between Enterprise Zones and OZ, guiding conclusions can be extrapolated from select studies. In a comprehensive analysis of Enterprise Zones by Professors of Urban and Regional Planning, Alan Peters and Peter Fisher, the Upjohn Institute for Employment Research published their study looking at 75 zones in 13 states. Ultimately, they concluded that the given tax incentives provided "little or no positive impact" on the impoverished community's economic growth[3]. Furthermore, in the UK, where this program was first tested by Theresa May's administration, it was found through government studies that relatively few jobs were created based on the magnitude of economic investment[4]. A common fear discussed with this plan is that these zones are future hubs for economic investment. Thus, tax incentives are being

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given away in communities where investments would inevitably occur. This process leads to an opportunity for investments to act as a catalyst for gentrification.

One reason this can be seen is due to the current writing of legislation. According to the Brookings Institute, states have a wide authority to select tracts that are less disadvantaged or are already seeing vast economic improvement. Due to the current guidelines, more than 57% of all neighborhoods in the US are eligible to be classified as an OZ[5]. Thus, with this free reign, zones can be chosen that already facing an appreciation in land value. Economic stimulus in an already appreciating economy can facilitate gentrification. In a brief macro-level perspective, it appears that these weaknesses in the program are prevalent but not detrimental. In following frameworks that have led to success, OZs can be created that not only spark local economic development but also ensure the integrity of the community.

Community Engagement

Given the previously stated perspective of setting up opportunity zones, a common theme that seems apparent in the success of such zones is community engagement. In order to best help these communities, it is vital to have them involved in the process. In order to benefit low-income communities and those who live within them, it is important to give engaged residents (activists, small business owners, local leaders) a voice so they can be a part of the process. According to The Hill, a great practice that will help keep the community engaged and spur success is focusing on an open data platform as well as focusing on local priorities and community involvement[6].

Case studies

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The goal of this is to provide transparent information on the regions that require investment, what types of investments are needed based on local needs, what incentives would be provided, the success and failure of previous endeavors, as well as an opportunity to communicate with local constituents. Such information should be made available on a government-sponsored website.

Thematic Approach

There is little information surrounding thematic approaches to investment practices. However, overall, it appears that most OZ investment speculation surrounds three main areas: real estate, housing, and infrastructure investment[7]. To follow theme, given Nashville's rise in population, a look at these three areas could prove beneficial for future planning. When analyzing Nashville, it is important to keep in mind what opportunities are available and what the local community desires when determining the type of Opportunity Funds to establish. An understanding of current practices can best influence an efficient approach to managing this new ecosystem.

Real Estate

Nashville is currently facing strong overall economic booms with real estate being a major focus. The city has seen an appreciation in home values of over 10% in just this past year. Looking at a more macro-scale, home prices are almost 50% higher than what they were pre-2007 recession. In areas like Downtown, residential projects such as Nashville Yards is developing roughly 4 million square feet of mixed-use real estate across 10 different buildings[8]. A report by PwC and Urban Land Institute Emerging Trends has Nashville ranked in the top ten real estate markets in the US[9].

Housing

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While the growth of the real estate industry brings opportunity, it also brings concern. Nashville is facing a shortage in housing supply, with affordable housing coming to the attention of many. With less homes, rising interest rates, an influx of residents and an appreciating land value, Nashville is struggling to provide affordable living opportunities to all of its residents. According to the Metro Human Relations Commission, as of 2015, 25% of homeowners and 49% of renters are paying more than they can afford on housing. In order to afford the average monthly rent, an individual would need an annual income of roughly $55,500. About 35% of individuals aren't even making $30,000 per year, a reflection of the crisis, one cause being a misalignment of rent and wages[10].

Infrastructure

Infrastructure is another point that many are looking at when it comes to investment in Nashville. There is heavy demand for public infrastructure improvements, specifically surrounding transportation, utilities, education, health, welfare and safety. The total needs, from the Tennessee Advisory Commission on Intergovernmental Relations, the city requires at least $45-billion of spending over the next few years[11]. Officials estimate that only $10.9 billion of the funding will be collected from state funds. Looking into public infrastructure, transportation is a huge focus with residents growing frustrated due to traffic congestion, potholes, and current public transit options[12]. Outside of the public realm, private companies are seeking infrastructure upgrades as well, such as local small business in the manufacturing industry.

An Approach to Nashville

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An important part to approaching Nashville’s opportunity zones is centered around community engagement. It is the hope that this endeavor will be beneficial for those who lie in a poverty-stricken region. The aim is to avoid profit-seeking investment that ignores local priorities. A focus on transparency of practice and opportunities can lead to a more efficient future. A proposal of practices to ensure this transparency will be proposed, along with systematic incentives, provided by the city, to encourage investors to work alongside community members, will be further outlined.

Transparency

In order to ensure that the investments in the regions align with the goals of the community, there must be a clear line of communication and ease of access to information. Based off historical research and evidence, a centralized database should be created to maintain the organization of the OZ projects[13]. This database should include, but is not limited to, the following.

- Zones available for investment
- Current investors (name, region, investment overview, project goals, contact information)
- Outline of OZ federal incentives, such as tax incentives
- Local incentives that encourage mutual reinforcing efforts between local stakeholders and investors (support of public institutions, foundations, business centers, etc.)
- Local regulations and expectations, and a progress report
- Designate a senior official as the point of contact to ensure accountability and coordination of resources

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- Peer learning sources with other states' endeavors
- Develop a mode for public input before investment selections are finalized as well as after they are finalized to help tailor the investment to local needs

This database should be available to the public on a government sponsored website.

Some states are approaching their outreach in other ways as well. In Nevada and Maine, they offered a public comment period for residents to give their thoughts and feedback on zones and investments[14,15]. The state of Vermont is hosting an Opportunity Zone summit comprised of financial expert, economic development professionals, and leaders of the designated OZ regions[16]. In the case of California, public input led to a fifth of the initially approved proposals being overturned due to misalignment with community goals[17]. While it is difficult to say which way is most optimal given the lack of time to observe direct impact of each approach, it is important to see that states are weary of this issue and each working on their own platform to spur community-oriented investment.

Policy Proposal

Nashville should establish their incentives for investment to ensure that all investments are aligned with the goals of the city and local community members. While regulations at the federal level are quite loose, Nashville has an opportunity to be a national leader in setting examples of how to efficiently spur economic development.

In order to encourage the greatest local economic stimulation aligned with the community's values, the goal of this policy will be to encourage investors to sign on to Community Benefit Agreements (CBA). In doing so, this will ensure that the investments received coincide with the community priorities, ultimately leading to an economic

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stimulation that will hopefully avoid consequences such as gentrification. Furthermore, by signing on to CBAs, it will allow for more structured investments that are regulated by these agreements. Thus, the Municipality of Nashville will not be responsible for the stipulations of the investment outlined by the community, the managing of the process, or the leading consequences as all arrangements will be held between the investor and local community groups as stated in the CBA.

In order to persuade investors to sign CBAs, the city must work to show investors the benefits of such agreement. Thus, it is proposed that the city provide its own incentives to encourage the signing of these contracts. Incentives offered by the city will be available to anyone but only followed through by those who sign the CBA, therefore avoiding political discourse of discriminative action. Attainable incentives can include, but are not limited to: fast-track to permitting, updating outdated utilities, renovating surrounding public infrastructure (i.e. sidewalks, potholes). These incentives are attractive to investors as it will provide them with a more efficient route to completing either the development of a new property or the substantial improvement of an existing one. Furthermore, by the city improving surrounding public infrastructure, it will increase the long-term value of their investment[18].

An additional avenue to look into would be the integration of Opportunity Zone investment within these projects. For example, if an investor signs a CBA and requests the local sidewalks to be improved, the city can contract out a local construction firm to take on this project as their own Opportunity Zone investment. Thus, this policy would not only be beneficial for investors in their endeavor but also would be providing more

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opportunities for local business to support the economic stimulation of impoverished communities.

Conclusion

Ultimately, OZs provide great economic opportunity for Nashville. However, this endeavor should be treated carefully as prior attempts in the UK as well as other cities have led to gentrification and a misalignment of community goals. The policy proposed can offer benefits to all stakeholders but requires more research to determine the types of incentives that are most attractive to investors as well as the likelihood of investors to see the Municipality provided incentives to outweigh the potential financial harms of signing a CBA. To ensure the success of this program, a great deal of attention must be focused on the fine details, examples of which can be seen in the recommendations detailed above.

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