NARC
Building Regional Communities

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Charles P. Rettig
Commissioner
Internal Revenue Service
Room 5203, P.O. 7604, Ben Franklin Station
Washington, DC 20044

CC: PA:LPD:PR (REG-115420-18)

RE: Investing in Qualified Opportunity Funds

Dear Commissioner Rettig,

We appreciate the opportunity to submit these comments on the Department of Treasury's (Treasury) proposed rules relating to the treatment of qualified Opportunity Zone Funds, and on the promise and reach of Opportunity Zones more generally. The National Association of Regional Councils (NARC) serves as the national voice for regional approaches to foster economic prosperity, improve the lives of residents, and promote efficient use of resources. NARC respectfully offers the following comments and recommendations to improve engagement with regional leaders and the likelihood of success in the communities they serve.

1) **Performance Measures and Public Accountability:**

   There has been a growing movement to tackle economic growth regionally so all communities can benefit – large and small, urban and rural. Regional councils are relied on across the county to carry out many economic development activities that some local governments do not have the capacity to carry out alone, including: being the administrative lead for workforce investment boards; conducting analyses of regional economic assets and challenges; convening locally-elected officials, industry leaders, and key stakeholders in an area to discuss how they can work together; and creating long-term economic development plans to put a region on the right track for future economic growth. Additionally, many serve as the Economic Development Administration-designated Economic Development Districts (EDDs) for their region. Through these actions, regional councils create the conditions that drive new business, spur innovation, and attract talent and investment.

   At the same time, the National League of Cities' 2018 City Fiscal Conditions survey indicates that local tax revenue growth is experiencing a year-over-year slowdown, with growth in service costs and other expenditures outpacing it. This suggests that many cities may be approaching the limits of their current period of fiscal expansion, which may have a serious impact on the regions they reside in.

   For local and regional leaders alike, Opportunity Zones represent a chance to respond to such slowdowns in new and innovative ways. Within Opportunity Zones, private investment will supplement public spending to advance public policy goals. In our view, it follows that public and private investment with Opportunity Zones should also have some alignment on performance measures and public accountability.

To that end, NARC urges support for the following accountability and performance measures:

- Creation of a system to allow the public to look up and track Opportunity Fund investments nationally;
- A requirement that Opportunity Funds file written development plans for each investment with Treasury for use in the system described above;
- A requirement that Opportunity Funds file a copy of the development plan submitted to Treasury with the local unit of government and regional council with jurisdiction over the Opportunity Zone; and
- The creation of a standardized set of performance measures to evaluate the impact of qualified investments within Opportunity Zones and against other Opportunity Zones. Such measures should include data correlated to the standard of living for current residents (those who resided in the zone prior to its designation).

2) **Coordination and Integration with Local and Regional Authorities:**
Because the strength of a regional economy relies so heavily on the cooperation and interdependence of the local communities within it, economic development remains an important priority for regional councils. This falls right in line with the main concerns of locally-elected officials, who usually make up the boards of directors for regional councils across the country. According to a comprehensive analysis of mayoral state of the city speeches released by the National League of Cities in their 2018 State of the Cities report, "economic development" stands out as the most prevalent major policy issue for the majority of cities and towns.

Opportunity Zones promise to unlock private investment for economic development in distressed communities. For regions, Opportunity Zones are a new tool, but public-private partnerships are not. In our view, success within Opportunity Zones will require coordination with regional councils and the local leaders that govern them. Conversely, uncoordinated investments, or worse, investments at odds with the regional leaders and locally-elected officials of an Opportunity Zone community, will almost certainly result in depressed outcomes or outright failure.

To that end, NARC urges support for the following:

- Measures that would coordinate opportunity-funded projects with federal and state grant-funded projects; and integrate opportunity-funded projects into long-term regional plans;
- Measures to require early engagement between Opportunity Fund managers, regional councils, and locally-elected officials to reduce the chance that factors outside private control – including regulations relating to zoning, permitting, and public and environmental health – do not result in unanticipated costs or delays; and
- A formal process for local and regional authorities to request a review of an Opportunity Fund investment that is irregular or abusive.

3) **Allowing Opportunity Funds to Invest in Infrastructure:**
The legislative history around the Opportunity Zones provision and public comments by its chief sponsors make it clear that they recognize inadequate infrastructure as a key obstacle to attracting private-sector

investment in these designated zones, and that they intend for the program to help finance improvements to often-neglected neighborhood infrastructure like streets and sidewalks, water and wastewater utilities, and the electric grid. We also recognize that most of the critical infrastructure required to make a tract economically viable is financed with debt, specifically municipal bonds. Two-thirds of all domestic infrastructure projects are financed by municipal bonds.[1] Ensuring mechanisms exist to finance infrastructure within the Opportunity Zones would recognize and respect the legislative intent behind the program.

To that end, NARC urges consideration of:

- Ways in which regulations pertaining to qualified Opportunity Funds can support and foster greater infrastructure investment, both public and private; and
- Specific proposals, including those submitted by groups like Build America Mutual Assurance Company, that would allow qualified Opportunity Funds to purchase and hold municipal bonds as qualified financial property, so long as the bonds are used to finance new or improve existing infrastructure projects that are substantially all within a qualified Opportunity Zone.

4) Asset and Revenue Requirements:

NARC is encouraged that the proposed regulations provide that if at least 70 percent of the tangible business property owned or leased by a trade or business is qualified Opportunity Zone business property, the requirement that "substantially all" of such tangible business property is qualified Opportunity Zone business property can be satisfied if other requirements are met. This threshold provides the flexibility needed for regional leaders and locally-elected officials to attract investment for local businesses. We encourage Treasury to keep the 70 percent threshold in the final regulations.

NARC is concerned with the proposed rule requiring an Opportunity Zone business to receive 50 percent of its gross income from within the Opportunity Zone. Such a requirement could dramatically reduce the ability for local communities to translate investment within the Zones into economic prosperity for residents. Because new firms represent nearly all net new jobs and over 20 percent of gross new job creation[2], it is essential that outside investors are able to invest in young and small firms.

While the intent of the requirement may be to ensure a qualified business operates and services the community, we believe it will have the opposite effect by eliminating investment in regions' most important small businesses—those that will grow. According to research by MIT economist Scott Stern, 75 percent of employment generated by small firms can be attributed to just 5 percent of startups.[3] This is because only a fraction of young businesses successfully create products and services that can be sold regionally, nationally, and globally. The 50 percent revenue rule would exclude many of the very small and young firms that this incentive was meant to encourage in distressed communities from investment.

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[1] Municipal Securities Rulemaking Board (MSRB). "Municipal Bond Market by the Numbers." http://www.msrb.org/msrb1/pdfs/MSRB-Muni-Facts.pdf

[2] Jason Wiens and Chris Jackson, "The Importance of Young Firms for Economic Growth," (The Ewing Marion Kauffman Foundation, 2015) https://www.kauffman.org/what-we-do/resources/entrepreneurship-policy-digest/the-importance-of-young-firms-for-economic-growth.

[3] Jorge Guzman and Scott Stern, "Nowcasting and Placecasting Entrepreneurial Quality and Performance," Working Paper No. 20954 (National Bureau of Economic Research, 2015), http://www.nber.org/papers/w20954.

To that extent, NARC urges:

- Reexamination of this particular rule to ensure the incentive achieves its original intent—to expand investment in to designated zones.

5) Federal Interagency Coordination:

NARC commends the creation of the White House Opportunity and Revitalization Council and supports the participation of the Treasury on the council.

To that end, NARC encourages the Treasury to recommend the following:

- Charge the Council with prioritizing technical assistance for small/midsized regions and markets that otherwise may miss out on early investment;
- Lead the Council, in coordination with other agencies, to foster a digital marketplace that can connect underserved communities and investors;
- Charge the Council with ensuring interagency coordination of federal programs and incentives that may also be active in Opportunity Zones, such as Promise Zones and Choice Neighborhoods; and
- Help investors understand their stake in the success of communities inside Opportunity Zones.

Thank you for the opportunity to submit comments on this important topic. If you have any questions regarding our responses, please contact Maci Morin at maci.morin@narc.org.

Sincerely,

Leslie Wollack

Leslie Wollack
Executive Director
National Association of Regional Councils