THE GOVERNANCE PROJECT

# Municipal Toolkit for Maximizing the Impact of Opportunity Zones

**Produced by:** The Governance Project

Mayoral administrations can take a few early steps to set the course for positive and transformative cycles of investment that ensure their communities benefit from the Opportunity Zone tax incentive. With visionary leadership, the incentive can be a big step forward for the inclusion of all Americans in municipal civic and economic life. Put together by leading nonprofits establishing norms for the Opportunity Zone market,[1] this document outlines emerging best practices for identifying, prioritizing, engaging around, and advancing such projects.

## 1. Start with a Vision or Prospectus

The first step is to develop a community plan and vision for the zone. It allows the mayor to tell a story that unifies stakeholders around a vision and markets the city to investors. This often entails developing an "investment prospectus." More guidance on this can be found on Accelerator for America's website.[2] A prospectus alone will not attract investment. **But, done well a prospectus, or vision, achieves three goals:**

1. It establishes what is possible for a municipality's Opportunity Zones.
2. It allows the community and City Hall to establish a common vision for the zone.
3. It tells a story that contextualizes economic and demographic data about the zone.

## 2. Identify Zone-Specific Needs

This incentive should be leveraged to address a community need. Two broad categories community need exist: (1) the need to alleviate a problem, such as a lack of affordable housing; or (2) the need to create alternative pathways to prosperity, such as the new industry creation. Projects that address both types of need at once are the most transformative. Three steps are required to identify needs.

1. **Targeted data is necessary to gauge needs:** local officials should engage universities and state offices to retrieve such data.
2. **Convene stakeholders to establish zone priorities:** City Hall should bring local parties together to get on the same page about what they want for the zone. This process should make clear that *now* is the time to act and should focus on projects with demonstrated community buy-in.
3. **Focus on lowering downside risk:** City Hall should guide stakeholders to projects that carry low displacement risks while addressing needs. This often is vacant or brownfield land.

## 3. Identify Community Resources

City Hall should tangibly contribute to ensure socially impactful projects are also economically viable. Since investors generally seek risk adjusted returns, to make projects more investible communities can deploy resources to increase returns or decrease risk. We identify three categories of community resources that can be mobilized to credibly boost a project's risk adjusted return.

1. **In-kind Contributions:** These are the most traditional local development tools City Hall uses.
   - Public finance contributions: these include bonds, TIF districts, and other tax incentives that can be layered on state and federal incentives in zones.
   - Public land contributions: municipalities often have tracts of publicly owned land that can be contributed at below market-rate to decrease investment risk, increase affordability, and provide investors with assurance that city hall will be a partner.

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[1] Input for this toolkit was gathered from Accelerator for America and the Economic Innovation group.
[2] http://www.acceleratorforamerica.com/OZGuide

2. **Regulatory Steps:** City Hall should creatively use the permitting process and zoning code to support projects that address social needs, as well as to curb any potential program abuses.
    - Permit approval process: The Opportunity Zone statute outlines strict timelines for funds investing in projects. This makes time a critical resource for investors and developers. City Hall should think creatively about how to fast-track certain projects. This is also a key place to consider adding measurement requirements for local projects in zones.
    - Zoning code: City Hall and local groups can approach Zoning Boards to apply for non-conforming use exemptions for projects that solves community needs. Similarly, they can lobby for additions to the code – such as inclusionary zoning requirements – for areas that are quickly growing or at risk of gentrification.
3. **The Local Asset Base:** Mayors usually have a good understanding of the local asset base. It is the most important to project success. Some groups can contribute financial resources, others can contribute some degree of certainty about continued community demand for the project.
    - Local capital base: Early evidence suggests that mobilized a locally committed capital base may the critical factor that determines the success of Opportunity Zones. Evaluating and engaging this base of local capital is vital, it comes in two forms.
        1. Local investors: Some communities are home to investors, high or moderate net worth individuals, or family offices who care deeply about the future of their city.
        2. Engaged local philanthropy: local foundations or philanthropists deeply committed to solving some problem can be engaged around mission-oriented projects.
    - Anchor institutions: The presence of universities, hospitals, or other large institutional anchors in, or adjacent to, a zone provides investors with an assurance of market stability and innovative potential. If they are engaged through partnerships or initiatives, this is even better.
    - Mission-oriented developer: A number of developers operating on local and national stages focus on solving social problems as well as constructing buildings. They can be engaged through real estate project RFPs.
    - Engaged community group: Active and widely-trusted organizations in a zone should be brought in early in developing the project to ensure it has local buy-in, and therefore lower risk.
    - A talented spokesperson: Telling a good story that weaves in the project can help build attention to the project's mission and the need that it's addressing. In communities that can afford it, hiring a dedicated Opportunity Zone staff member in city hall to field inquiries, develop strategy, and provide informed communication to a breadth of stakeholders can ensure that a municipality leverages this resource.

## 4. Select Priority Projects from the intersection of Needs & Resources

Good projects for this incentive occur at the intersection of social need and market traction. City Hall should lead communities strategically leverage local resources for maximum social impact. To do so, city hall should compare zone-specific needs and resources to find projects at the intersection of each. The questions below are intended to help guide City Hall's thinking as it compares intersecting projects.

- What are the different combinations of need-asset "sweet spots"?
- How far along in the planning pipeline are projects in these sweet spots?

- How much city-owned or anchor-owned land is in the zones surrounding "sweet spot" projects?
- How do "sweet spot" projects fit within the mission orientation of the local capital base?
- Do these projects create the groundwork for entrepreneurship?[3]
- Where do "sweet spot" projects fit within the mayor's vision and the city's strategic plan?

## 5. Develop Financing Models to Refine Priorities

Once one or two projects are prioritized, City Hall should develop financing models to understand the specific magnitude of resources they'll need to deploy to make projects pencil. Based on a set of market assumptions, the model will determine the project's expected net operating expenses, revenues, and rate of return. Performing a sensitivity analysis on assumptions will allow municipal staff to deliberately leverage local resources.

1. **Building the business model:** Economic development staff should acquire quality data on the local real-estate market, especially the cap rate and construction costs to generate assumptions. The model should be developed in coordination with a nonprofit or consultant with expertise. Occasionally a feasibility study is necessary to get a better idea of local market conditions. This model will inform the project pro forma.

2. **Develop a platform for managing priority projects:** As the municipality advances projects, there will likely be multiple projects across zones. The local government should help investors to easily see and sort projects by attribute, geography, and financial characteristics. A digital platform like this can serve the dual function of allowing the city to track the progress of priority projects. We recommend that the city work with a third-party provider, like The Opportunity Exchange, to establish this platform.[4]

## 6. Progress Priority Projects into Deals

The process of moving priority projects to deal differs only slightly from the normal development process in that it requires credible engagement with equity investors as well as developers.

1. **Formalize a Pro Forma & Deal Sheet:** City hall should formalize a deal sheet, which is a one-page public-facing document that summarizes key financial facts about *one project.* It's backed up by a formalized financial pro forma. City Hall should prepare to qualify these documents and defend their assumptions.

   **The Deal sheet should include:** a rendering of the project; a short description of the offering, describing community buy-in, the developer, key surroundings, and other important information; a section focusing on investment highlights (number of units, land values, and a summary of local contributions); a section on the project's total debt capital, equity requirements, and potential social impact; and a final section focusing on notes on the local market.

2. **Progress an RFP:** The actual deal occurs through the RFP process. An RFP should go out to two audiences: developers and investors. The investor RFP should include a term sheet along with any city specifications on the investment alongside normal RFP contents.
   - Create list of relevant parties to invite to an RFP: City Hall should decide if they want to target local, national, and/or mission aligned developers and investors.

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[3] Although the Treasury Department's rules still leave ambiguities around operating business investment, certain projects like coworking spaces, public transit, and workforce housing create the groundwork for business growth.
[4] https://www.theopportunityexchange.com/

- Develop and Circulate the RFPs: The municipality should include the normal specifications for the RFP in both the developer and investor RFPs. *After the document is developed and circulated, the city should host a session for interested investors and developers and field questions.*
- Evaluate and approve: After the deadline for responding to the RFP has passed, City Hall should evaluate responses following the process specified in the RFP. It is recommended that the city employ or contract someone with investment experience to evaluate the investor RFP responses.

Questions? Or looking for assistance on this process? If you're a community or municipal leader and want to learn more, email colin@governanceproject.org, or find us at www.governanceproject.org.