# House taxwriting panel praises Opportunity Zones but sees room for improvement

The Opportunity Zone tax incentives enacted in the Tax Cuts and Jobs Act of 2017 (TCJA, P.L. 115-97) won bipartisan plaudits during a May 20 House Ways and Means Tax Subcommittee field hearing in Erie, Pa., on expanding economic opportunity in the "Rust Belt"—although taxwriters and witnesses also acknowledged that the program would be strengthened by the addition of robust reporting requirements and other changes.
**URL:** https://www.congress.gov/115/plaws/publ97/PLAW-115publ97.pdf

**Opportunity Zones**

The TCJA as enacted generally provides that taxpayers using a "Qualified Opportunity Fund" to invest in an economically distressed community designated as a "Qualified Opportunity Zone" can defer and potentially reduce tax on prior capital gains rolled over into the fund, as well as permanently eliminate tax on future gain arising from appreciated investments made through the fund that are held for at least 10 years. The election to invest capital gains in an Opportunity Zone is scheduled to expire after December 31, 2026.

Tax Subcommittee Chairman Mike Kelly, R-Pa., commented in his opening statement that Opportunity Zone-funded investments have been instrumental in revitalizing downtown Erie, which is located in the district he represents.

"Stakeholders have leveraged $40 million in private capital into a $115 million investment," Kelly said. And as a result of that investment, "Erie has welcomed 110 new residential spaces, created space for 25 new businesses, restored 8 historic properties, revitalized 100,000 square feet of new commercial space, and established a grocery store in what was previously designated a 'food desert.'"

Subcommittee member Gwen Moore, D-Wis., who served as acting ranking member at the hearing and was the only Democrat to attend, likewise commented in her opening statement on the success of Opportunity Zone development projects in her home district in Milwaukee. And although she cited statistics from the Joint Committee on Taxation staff indicating that the average income of a Qualified Opportunity Fund investor is over $1 million, she also acknowledged the importance of private capital investments—and affluent investors—in redeveloping disadvantaged communities.

". . . I can understand why we might need a program to encourage that kind of private investment, in areas where the return [on] capital might not otherwise be so great. And yes, I even understand that if you're looking for capital, then you need to look to, well, people who have money," she said. "So, what you're not going to hear me say here . . . is 'these are tax cuts for the rich, and so they are bad, full stop.'"

**Need for reporting requirements:** Taxwriters and witnesses agreed that redeveloping economically underserved areas will require sustained investment over the course of years or even decades and that the Opportunity Zone program should be extended. But they also offered perspectives on how the rules of the program should be modified to make them more effective.

Subcommittee Chairman Kelly touted the Opportunity Zones Transparency, Extension, and Improvement Act (H.R. 5761), a measure he introduced last year with Ways and Means Committee Republican Carol Miller of West Virginia and Democratic taxwriters Dan Kildee of Michigan and Terri Sewell of Alabama, that, among other things, would implement reporting requirements for Opportunity Zones. (For procedural reasons related to the budget reconciliation process Republicans invoked when they moved the Tax Cuts and Jobs Act through Congress, reporting requirements were left out of the Opportunity Zone provisions when the legislation was enacted.) Kelly also noted that similar proposals were included in the "economic growth" legislation that the full Ways and Means Committee approved along party lines last June but has not been brought up for a vote on the House floor. (For prior coverage of the Ways and Means-approved economic growth package, see *Tax News & Views*, Vol. 24, No. 24, June 16, 2023.)
**URL:** https://www.congress.gov/bill/118th-congress/house-bill/5761/text
**URL:** https://dhub.deloitte.com/Newsletters/Tax/2023/TNV/230616_1.html

Kelly asked witness Shay Hawkins of the Opportunity Funds Association to discuss how adding reporting requirements would strengthen the Opportunity Zone program.

Hawkins, who is a former tax counsel to GOP Senate Finance Committee member Tim Scott of South Carolina and worked with Scott on developing the Opportunity Zone proposal that eventually was incorporated into the TCJA, commented that adding reporting requirements would enable the Treasury Department to compare the economic performance of Opportunity Zones against that of communities that applied for but did not receive an Opportunity Zone designation. Reporting requirements also would give Congress insights into how it could revise the Opportunity Zone rules in an effort to make them "even more impactful," he said.

**Expansion to rural communities:** Ways and Means Committee Chairman Jason Smith, R-Mo., who waived onto the subcommittee to participate in this week's field hearing, noted that roughly 95 percent of current Opportunity Zone investments are funding projects in urban areas. He asked Hawkins to explain how Congress could modify the Opportunity Zone program to encourage investment in rural communities. (The economic growth package that Smith shepherded through the Ways and Means Committee last year calls for the creation of "Qualified Rural Opportunity Zones.")

Hawkins replied that Congress should consider revising the Opportunity Zone rules to permit intermediary investments through "feeder funds" that can then be directed to smaller Qualified Opportunity Funds. (He explained in his written testimony that such a "'fund-of-funds' model will help smaller, regionally focused, impact-oriented funds raise capital and overcome scale challenges with institutional investors . . . [and] drive more investment into rural communities, making committee efforts to expand the [Opportunity Zone] map to include more persistently poor rural places even more effective."

**Investment in new businesses:** Subcommittee member Dave Schweikert, R-Ariz., asked how Congress can expand the Opportunity Zone program to encourage "the next generation of entrepreneurship" and bring new businesses into the communities that are being redeveloped.

According to Hawkins, one way to accomplish that goal would be to allow noncapital-gain investments in businesses located in an Opportunity Zone and provide a 100 percent basis step-up when the business is sold if the investments are held for 10 years or longer.

Serving a public purpose: For her part, Democratic taxwriter Gwen Moore agreed that adding reporting requirements to the Opportunity Zone rules would ensure the program is working as intended. She also argued that the program rules should include guardrails to ensure that a portion of Opportunity Zone investments is directed to projects that benefit low- and moderate-income taxpayers.

**Expired and expiring TCJA provisions**

Republicans on the panel also asked witnesses to assess the impact on businesses of the TCJA's phase-out of taxpayer-favorable treatment of research expenditures, the deduction for business interest expenses, and 100 percent bonus depreciation. Ways and Means Chairman Smith and Senate Finance Committee Chairman Ron Wyden, D-Ore., have sought to reverse those TCJA tax law changes (through 2025) with their Tax Relief for American Families and Workers Act (H.R. 7024), which was approved in the House this past January but remains stuck in the Senate. (See separate coverage in this issue for details on the current status of that legislation.)
**URL:** https://www.congress.gov/bill/118th-congress/house-bill/7024/text

Witness Tom Tredway, president of Erie Molded Packaging, commented in an exchange with subcommittee Chairman Kelly that the switch to mandatory amortization of research expenditures resulted in "an unexpected tax hit" for his company and was "one of the most frustrating things" he has experienced as a business owner.

Congress "needs to do everything [it] can to incentivize R&D" if the US is to keep pace with international competitors such as China, Tredway added.

Ways and Means Chairman Smith asked Tredway more broadly about how the Opportunity Zone rules have worked in tandem with some of the soon-to-expire TCJA provisions—such as the 20 percent deduction for certain passthrough income and the increased estate and gift tax exemptions—to benefit small, family-owned businesses. (Congressional Republicans have vowed to permanently extend these and other TCJA provisions that are currently scheduled to sunset after 2025 if they win control of the House, Senate, and the White House in the upcoming elections. President Biden has said that if he is returned to office next year he would support allowing these provisions to lapse for taxpayers with income greater than $400,000.)

Tredway replied that the TCJA put his company "in a better position to thrive" by allowing him to reinvest in the business, hire more people, and bring them into the community. Opportunity Zones, in turn, made the community "a better place [for his employees] to live, work, and play," he said.

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