



Summary. On Thursday, June 6, Governor Kay Ivey signed the Alabama Incentives Modernization Act (the AIM Act) into law. At the heart of the Act is a first-of-its-kind framework designed to provide the best and most impact-oriented Opportunity Zone investments with (1) aligned state-level capital gains tax breaks, (2) potential state investment dollars, and (3) new impact investment tax credits to de-risk investments.

What It Means for Our Stakeholders. Every stakeholder in the Opportunity Alabama ecosystem can benefit from the new set of OZ incentives introduced by the AIM Act.

- *For Investors* – Investors in high impact OZ projects will get the same state-level capital gains tax benefits that they get at the federal level. More importantly, the AIM Act de-risks high impact OZ funds by using tax credits to guarantee investor returns. Read “STEP 3” below to find out how.
- *For Communities, Developers, and Businesses* – The AIM Act is designed to make investment opportunities with the highest level of community impact more attractive to investors. For rural areas aiming to attract more investor interest, the Act offers significant incentives for investment in high-impact projects. For urban areas addressing challenges from growing a tech ecosystem to blight remediation, the Act offers a way to make transformational investment opportunities much more compelling.
- *For the State* – The AIM Act provides Alabama with an unparalleled suite of OZ incentives. Because the state retains the ability to control who gets the incentives through a rigorous application process, it can steer the flow of Opportunity Fund equity into the most distressed places with the highest potential for community-aligned growth and investor return. And, thanks to Opportunity Alabama, we are one of the only states in the country that has already assembled a statewide pipeline of high-impact Opportunity Zone projects – so we will be ready to leverage this incentive quickly.

How the AIM Act OZ Incentives Work. Whether you are a project sponsor recruiting investors for your deal or a fund manager building a pipeline, you must complete the same series of interlocking steps to access the three AIM Act incentives described above. Each of these steps is explained in detail in the next section.

- *STEP 1 – Fund Approval and State Conformity.* Sponsors or managers must apply to the Alabama Department of Economic and Community Affairs (ADECA) to become an “approved Opportunity Fund.” This requires a solid, stable, and return-producing pipeline of high-impact projects – all of which have strong community support and will produce strong societal returns. See “STEP 1” below for additional information on this process. Once approved, fund investors will get the same OZ-based capital gains tax treatment on state income taxes that they get on their federal income taxes.
- *STEP 2 – Access to State Capital.* Once “approved,” sponsors and managers can seek investment from one (or more) of the ten state-controlled funds enumerated in the AIM Act, which are now permitted (but not required) to invest at least 3% of their principal in approved Opportunity Funds. Because fund managers must get at least a dollar of state investment in order to access impact investment tax credits, this optional step becomes mandatory if approved funds want to move on to Step 3.
- *STEP 3 – Tax Credit Guaranteed Returns.* The AIM Act creates a \$50 million pool of state “impact investment tax credits,” which can only be accessed through a project agreement with ADECA. Under those agreements, credits can only be claimed if an investment underperforms expectations – meaning that they make investing in high-need projects safer by insuring against downside risk. In exchange, the state gets regular reports on project-level impact and a share of the upside if a fund outperforms expectations. See “STEP 3” details below for additional information on the mechanics of this powerful incentive.

STEP 1 – Fund Approval and State Conformity. Anyone who has one or more potential OZ-based investment opportunities can form a federally designated Opportunity Fund, then apply to ADECA to become an “approved Opportunity Fund.”

To determine whether a fund gets “approved” – and is eligible for state law conformity and the incentives available under Steps 2 and 3 – ADECA has a three-part test.

- A. *Capacity.* Funds need to demonstrate, among other things: (1) ability to raise capital, (2) management experience, (3) strength of projects/pipeline, (4) anticipated returns, (5) a strategy for tracking and reporting social impact, and (6) strong community engagement (evidenced by partnerships with elected officials or nonprofit organizations like ours).

- B. *Impact.* Funds need to demonstrate how and why they will create as much community-oriented impact as possible, with specific priorities in (1) rural areas, (2) technology/advanced manufacturing, (3) living wage job creation, (4) workforce training, (5) affordable housing, (6) blight remediation / urban revitalization, and (7) projects with substantial social, environmental, or economic impact.
- C. *Alabama-Based.* At least 75% of the applicant's projects need to be located in Alabama (or headquartered here for OZ purposes).

If a fund passes these tests, its investors automatically get the same capital gains tax treatment at the state level as they do at the federal level. If you are unfamiliar with these federal tax benefits, please visit www.opportunityalabama.com/resources for more information.

The phrasing of these tests above make it seem like this incentive regime is only applicable to “fund managers” running large, multi-asset funds. However, it applies far more broadly than that. A strong developer using her own capital gain from a prior project to invest in her next deal would likely meet the capacity and Alabama-based criteria in (A) and (C), but she would still need to meet the impact criteria in (B) to get conformity (and access to the incentives below).

STEP 2 – Access to State Capital. In order to encourage more impact-aligned OZ investment, the AIM Act permits certain state-created funds to invest 3% or more of their corpus in impact-oriented Opportunity Funds. The ten funds specifically listed in the statute range from the Alabama Game and Fish Fund to the Public Road and Bridge Fund. Each of these funds are professionally managed and have certain investment guidelines and return expectations. As a result, they are not required to commit capital to ADECA-approved Opportunity Funds. All the legislation does is create a pathway for approved funds to start conversations about investment with the State.

However – as described above, any fund that wants access to impact investment tax credits *must* get at least a dollar of state investment. This means approved funds will be underwritten by at least one professional fund manager before they can even begin to negotiate a project agreement with ADECA to claim a tax credit guaranteed return – and that only the best funds (and projects) will get the biggest incentive.

STEP 3 – Tax Credit Guaranteed Returns. The first three to five years of any investment are almost always the riskiest. For real estate projects, all of the pre-development risk, construction risk, and lease-up risk happen in this short window. For operating businesses, most new ventures sink or swim within the first 36 months after receiving an investment. Those risks are only exacerbated when the project is located in an underperforming or low-income area in need of revitalization.

The AIM Act allows ADECA to enter into project agreements with approved Opportunity Fund sponsors to offset these risks. These project agreements allow ADECA to allocate a portion of a \$50 million pool of newly minted “impact investment tax credits” to (A) offset losses on projects that close and (B) guarantee returns (up to U.S. Treasury rates, which currently hover around 2%) on projects that underperform.

The law is intentionally vague on what those guarantees could look like on a project-to-project basis, so we have included some examples of how this was intended to work.

- *Example 1a:* A real estate fund wants to raise \$15 million to undertake three \$5 million projects – a build-to-suit manufacturing facility, a new workforce housing development, and a redevelopment of five buildings on a rural town square. The manufacturing and the redevelopment projects are hugely successful, producing substantial investor returns, but the projected demand is not there for the workforce housing. It never turns a profit, and the project is sold for \$1 million (a \$4 million loss). Under its project agreement with ADECA, the fund could receive up to \$4 million in tax credits in Year 5 (the first year credits can be allocated under the Act) to offset that loss, and another \$400,000 in tax credits to provide an annualized 2% return over the 4 years the project lost money.
- *Example 1b:* Same as above, but assume the fund has only asked ADECA to give it enough tax credits to offset half its losses and has not asked for any guaranteed return. In that case, ADECA would only allocate \$2 million to the fund manager, leaving more tax credits available to guarantee future deals. Because this is a competitive application process, ADECA may ultimately reward creative fund managers who propose structures like this that do more high impact projects with smaller tax credit allocations.

- *Example 2:* A seed-stage OZ venture fund wants to invest \$2.5 million in five biotech companies and locate them in a distressed neighborhood. The risk for an investor here is huge – it might be that none of the five biotech companies pan out, and that the entire \$2.5 million is lost. With impact investment tax credits, however, investors know that they will get enough in tax credits to offset losses and provide U.S. Treasury-level rates of return. So – even if each of the five companies goes out of business by Year 4, fund investors will receive tax credits of up to \$2,550,000 in Year 5. If only one company goes out of business, only a portion of the credits would be used – enough to cover losses, just as in the example above, and provide a 2% return on that single investment.

Have questions about how all of this works? [We can walk you through it.](#)

As noted above, while credits can be used to offset losses or guarantee returns during the first four years of a fund’s life cycle, they cannot be claimed by the fund until Year 5 or later.

ADECA can allocate the credits in whatever manner it sees fit. It could give out all \$50 million to a single fund or split that amount up across multiple funds. It could distribute them all in a single year or space them out over multiple years. This gives ADECA the flexibility to adapt in a broader Opportunity Zones landscape that changes every month as the national market takes shape.

From a public policy perspective, the structure of this incentive is more beneficial than the typical tax credit for two reasons.

- First, because the state will underwrite the funds that apply for these credits, ADECA should have sufficient information to award credits only the funds that have the greatest likelihood of success – and if those funds are successful, they will never use a single dollar of the credit they were allocated.
- Second, the project agreement negotiation process requires the fund to provide the state with some substantial (but undefined) portion of the upside if a fund overperforms expectations. By selecting the right fund managers and developers and negotiating strong project agreements, ADECA will make it far more likely that the state will see substantial returns on its investments in these approved funds.

Taken together, this means that the state could (theoretically) get a net *direct* positive revenue stream from this new incentive without even looking to all the indirect benefit of sales tax, income tax, and property tax growth typically used to justify tax credits.

Other AIM Act Incentives. In addition to these Opportunity Zone incentives, the AIM Act makes the State's incentives more accessible and more valuable to companies looking to locate in rural areas and technology companies looking to locate anywhere in the state. For example, the AIM Act:

- Eliminates state capital gains taxes entirely for owners of tech or STEM companies who relocate the company's HQ to Alabama, sell at least three years after relocating, and remain in Alabama at least five years after the sale;
- Reduces the number of jobs that must be created by STEM and technology companies to be eligible for Alabama's investment tax credits, property and sales tax abatements, and job creation/operating expense rebates; and
- Incentivizes investment and job creation in Alabama's rural communities by increasing the number of counties designated as rural for purposes of receiving incentives.

Next Steps. As a procedural matter, it may take time to put the infrastructure in place to make this program operational. From developing an application process to coordinating between state fund managers to develop an OZ pitch and underwriting procedure, a huge amount of work remains before this new incentive regime becomes operational. Stay tuned for additional updates from OPAL as this process develops.

In Closing. The AIM Act is a huge win for the State of Alabama – It provides us with an incentive to drive investment towards the best projects that need it the most in a way no other state can match. We have seen the incredible pipeline of high-impact, high-potential projects across the state that are the perfect candidates for this new tool, and we are excited to work with national and local investors to start getting great deals done.