

WALL STREET'S BIG OPPORTUNITY

*Opportunity Zones are a corporate tax break
masquerading as community development*



JUNE 2020

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Acknowledgements: This report was researched and written by Oscar Valdés-Viera and Patrick Woodall of Americans for Financial Reform Education Fund.

WALL STREET'S BIG OPPORTUNITY

Opportunity Zones are a corporate tax break masquerading as community development

June 2020

Executive Summary

The Opportunity Zone (O-Zone) tax break was created by the 2017 Republican tax cut legislation. It was promoted as a way to incentivize investment in economically disadvantaged areas but it is marred by poor design and flawed implementation so that it will most likely provide tax breaks for investments in already booming cities and gentrifying neighborhoods. The program incentivizes investments that aim to maximize returns in lower-income areas where residents are vulnerable to economic displacement pressures. Problems and likely negative consequences of the program include:

- **Exacerbation of affordable housing crisis and displacement of residents of color and lower-income residents:** The bulk of investments are likely to flow into a subset of cities and O-Zones that are already economically transitioning. Studies have found that prior place-based development tax incentives contributed to higher housing prices and the dislocation of existing residents.
- **Poorly targeted to disadvantaged areas:** The designated O-Zones did not have less investment than eligible areas that were not included in the program and many gentrifying areas or neighborhoods near gentrifying areas were included in the

program. Nine percent of the designated O-Zones do not meet the tax breaks' own statutory poverty or income thresholds.

- **Failure to include performance standards or disclosure requirements:** There are no requirements that the investments benefit low- or moderate-income residents, and the lack of transparency and disclosure prevents evaluation of the social and economic impact of the program.
- **Tax break could become \$26 billion giveaway:** Treasury Secretary Stephen Mnuchin predicted \$100 billion could be invested under the program; if these investments are held for a decade, federal revenues could fall by over \$26 billion. Investors and real estate developers would pocket these billions as tax savings.
- **Wealthy, well-connected investors poised to reap substantial benefits:** Some of President Trump's inner circle have already formed investment vehicles to benefit from O-Zone program and several high-profile real estate developers lobbied to have projects or land covered by the program.

The O-Zone tax break benefits the real estate industry and wealthy investors – far more than the program benefits



Opportunity Zones cover most of Oakland, California. Credit: Sundry Photography

communities. The lost federal revenues would have been better spent on public investments that address the problems people face every day in economically struggling communities.

Opportunity Zone Basics

Included in the mountain of corporate tax breaks in the 2017 Trump tax law was a provision that allowed the wealthiest investors to escape taxation on investment profits.¹ The new O-Zone tax break is pitched as encouraging investment in lower-income communities but it poses substantial risks that it will primarily provide major tax benefits for shifting capital gains earnings into lucrative real estate investments in rapidly gentrifying neighborhoods, adding to the affordable housing crisis and accelerating the displacement of existing residents. Already, Wall Street figures and firms have assumed a leading role in channeling money into funds designed to exploit the additional riches that this tax giveaway offers for wealthy investors.

The tax breaks only benefit the wealthiest investors and could amount to more than \$26 billion in tax savings over ten years. *Forbes* magazine wrote that the program could become “one of the biggest tax giveaways in American history” and the *New York Times* called it a “once-in-a-generation bonanza for elite investors.”² If the goal is affordable housing and community development, resources should be directed to meeting those goals, not giving tax breaks to investors. Some Trump insiders — including Jared Kushner (who recently shed his holdings because of concerns of the appearance of conflict-of-interest), Chris Christie and Anthony Scaramucci (see page 14) — already have holdings in special investment funds designed to take advantage of the tax cuts.

The O-Zone program is in many ways a bigger but more generally ineffective reboot of the failed geography-based development tax incentives of the past.³ These tax incentives focus on providing benefits to investors and assume that ancillary gains will automatically flow to local residents. The similar Empowerment Zone and Enterprise

neighborhoods or residents the program purportedly serves. To make this lack of standards even worse, the definition and designation of O-Zone geographies has been overly broad and encompasses some of the hottest, up-and-coming neighborhoods in the country.

The list of qualified O-Zone areas did include many lower-income neighborhoods, communities of color, and economically disadvantaged rural areas. Many investors are likely to pay lip service to economic development and some will really be focused on outcomes that serve lower income community residents, but the rules and design of the program do not create incentives to do anything other than maximize returns and tax benefits. As a result, it is expected that very little money will go to other places.⁸ Many projects that were already underway in more prosperous O-Zones have begun to utilize the program to access tax-subsidized financing.⁹ Developers and investors are focused on already hot places included as qualified O-Zones; and nothing in the program design creates incentives to do anything else.

The O-Zone program could become a massive tax break for gentrification, the upscaling of neighborhoods that may bring new economic activity but also displaces long-standing residents, especially people of color and lower-income people. It is not just that most investors will likely bypass the lowest-income areas, but also that the developments that target more affluent or gentrifying O-Zones could contribute to harming existing residents who are being priced out and squeezed out of their neighborhoods. There is a grave danger that

Most of the money is likely to pour into Opportunity Zones in or near gentrifying neighborhoods that are already receiving ample investment, have an influx of prosperous residents, and will generate the highest profits.

these investments will exacerbate the already dangerous disappearance of affordable housing and displace households of color and lower-income households. In effect, the O-Zone program could reward developers for driving

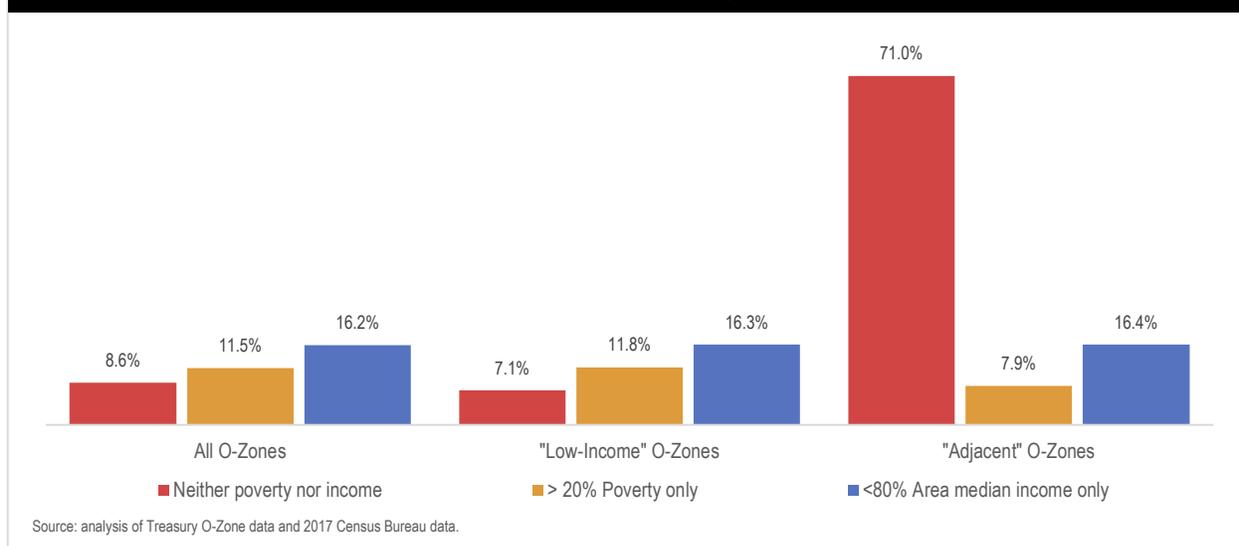
and profiting from displacement. All the while, the program's tax cuts erode federal revenues that could have actually been used to address the lack of affordable housing or otherwise serve lower-income communities.

Weak O-Zone Eligibility Standards Enable Gentrification Tax Breaks

Opportunity Zones provide generous tax breaks to incentivize investments into what the O-Zone statute and rules define as "low-income" areas. However, the loose definition of "low-income areas," the older demographic data the program relied on, and the choices made in winnowing the list of eligible census tracts allowed many higher-income and already-gentrifying areas to qualify for the program. The absence of performance rules and standards (see page 8) combined with investors' interest in maximizing returns, means that the bulk of the O-Zone investments are likely to flow to these neighborhoods. As a result, the program will likely fail to deliver investment to many low-income areas and communities of color while accelerating the dislocation from rising housing costs in areas that are already undergoing gentrification and demographic change.

The Treasury Department's application of a weak statutory standard for "low income" provided ample wiggle room to designate

Fig. 1: Share of O-Zone census tracts meeting poverty or income thresholds



more affluent areas as low-income Opportunity Zones. The definition of low-income for O-Zone designation included census tracts with poverty rates over 20 percent or median family incomes below 80 percent of the area median income.¹⁰ Under many federal definitions, by contrast, income between 50 and 80 percent of the area median is defined as “moderate-income,” areas below 50 percent of the area median income are considered “low-income” and areas below 30 percent of area median are “extremely low-income.”

It is also important to note that tracts with median incomes below 80 percent of the area median could still be quite prosperous in expensive cities (a census tract where half the families earned over \$97,000 in San Jose, over \$76,000 in Washington, DC or over \$75,000 in Seattle, for example would all meet that standard).¹¹ Census tracts where 20 percent of people live below the federal poverty line can also include substantial pockets of affluent or rapidly gentrifying areas.¹²

The Treasury Department further diluted these standards by using older demographic

data (from 2011 to 2015 instead of newer Census Bureau data) that included areas that had become more affluent since 2015 and excluded areas that might have suffered economic downturns.¹³ (Although Treasury allowed the use of newer data to include additional areas, it did not *exclude* areas that would not meet the low-income criteria with the latest data.¹⁴)

In addition, census tracts *adjacent* to low-income areas were also eligible for inclusion in the O-Zone program if the adjacent area incomes were not more than 25 percent higher than the neighboring “low-income” area.¹⁵ An adjacent neighborhood could qualify as an O-Zone with poverty rates below 20 percent and with family incomes above 80 percent of the area median, especially in higher-cost cities.

Treasury used these standards to identify every potentially eligible census tract and determined that more than half (56 percent) of *all* census tracts were eligible for the program; 23 percent of the eligible areas were adjacent tracts with lower poverty levels and higher incomes.¹⁶ States could nominate only 25 percent of the total census

tracts that qualified under the program (or 25 tracts if there were fewer than 100 eligible tracts statewide).¹⁷

Based on states' nominations, the Treasury Department certified 8,766 census tracts with around 35 million residents as qualified Opportunity Zones.¹⁸ Many of the

O-Zones do not meet either the poverty or income thresholds to be considered "low-income" using 2017 census data. About 9 percent (751 tracts or 8.6 percent) of the 8,766 qualified O-Zone tracts had 2017 family incomes above 80 percent of the area median income *and* poverty rates below 20 percent (see Figure 1).¹⁹ Nearly three-quarters (71.0 percent) of the adjacent O-Zone census tracts had higher incomes and lower poverty rates than the thresholds. More than 100 qualified O-Zones had incomes over 160 percent of the area median incomes – or double the income cutoff – and even if those areas had poverty rates over 20 percent, this data suggests these were areas with substantial wealthy populations and wide income disparities. All of these neighborhoods will remain qualified Opportunity Zones until the end of 2028²⁰ – even if they become (still) more affluent over the coming years.

Nor did the program successfully focus on areas with less investment. The Urban Institute found that there was only "minimal targeting" of the program to the communities that most need investment.²¹ It determined that qualified O-Zone areas did not have substantially lower levels of investment than undesignated areas and that one-third of the O-Zones census tracts were already receiving the highest levels of

Several prominent, wealthy and politically connected real estate developers appear to have successfully lobbied to have the census tracts where they owned properties included in the O-Zone program – in some cases, even though the area did not qualify as "low-income."

investment.²² Many neighborhoods qualified without being economically disadvantaged. For example, the Brookings Institution found that many states designated qualified O-Zones in college towns, where incomes might be low because of the non-working student population,

but which are not necessarily areas that have lacked investment.²³

The list of qualified O-Zones included a large portion of gentrifying neighborhoods across the country. The National Community Reinvestment Coalition (NCRC) estimated that 70 percent of gentrified neighborhoods are within or next to an Opportunity Zone.²⁴ The Urban Institute found that areas experiencing the most socioeconomic change were overrepresented in the designated O-Zones compared to areas that were eligible but not included in the program.²⁵

Wealthy developers successfully lobby to get projects covered by O-Zone tax break

Several prominent, wealthy and politically connected real estate developers appear to have successfully lobbied to have the census tracts where they owned properties included in the O-Zone program — in some cases, even though the area did not qualify as "low-income." *Pro-Publica* reported that "the Trump tax law gave governors the authority to distribute valuable tax breaks, and they have wielded it to benefit the politically connected."²⁶ A close friend of Trump, Richard LeFrak, successfully lobbied Florida



Rybozich Superyacht Marina, West Palm Beach. Credit: Airwaves1 CC-BY- 2.0

to get the property where his North Miami luxury Solé Mia project was under development included in the list of qualified Opportunity Zone census tract — which could increase the returns on the development by \$100 million.²⁷ Florida Governor Rick Scott (now Senator) also approved an O-Zone in West Palm Beach with a superyacht marina where the owner was planning a luxury apartment development and another in Tampa where the owner of the Tampa Bay Lightning hockey team planned a high-end residential and hotel project.²⁸ The founder of Quicken Loans and owner of the Cleveland Cavaliers with connections to the Trump family secured O-Zone status for several parcels in Detroit where he had substantial real estate holdings after pressing the state government and a fortuitous intervention that benefited him by the Treasury Department.²⁹

Some developers were able to get their projects covered by Opportunity Zones even though they did not quite qualify for the program. In Baltimore, billionaire CEO of Under Armour, Kevin Plank, successfully got the land under his Port Covington development aimed at wealthy millennials

considered an O-Zone even though it was initially rejected for being too wealthy. A lobbying campaign got it included in the Maryland governor's list, in part because of a mapping error, which ended up bumping an area with a much higher poverty rate off the O-Zone list.³⁰ New Hampshire Governor Chris Sununu designated one large, rural census tract as an O-Zone that contained a ski resort owned by his family, although many other undesignated areas had higher poverty rates or lower family incomes.³¹ Treasury Secretary Mnuchin personally intervened to get 700 acres in Nevada owned by his friend and convicted financial fraudster Michael Milken (later pardoned by Trump) counted as an Opportunity Zone even though Treasury had previously rejected its eligibility because it was too wealthy.³²

In early 2020, the Treasury Department's independent auditor Inspector General announced an investigation into whether the design or implementation of the O-Zone tax break had been distorted to create tax break bonanzas to wealthy or politically connected investors.³³

Lack of Performance Standards Mean Low-Income Communities and Residents Unlikely to Benefit from Investments

The O-Zone tax break has no requirements that the investments actually deliver economic benefits for the low-income communities and residents it purports to serve. There are no outcome-based targets or disclosure requirements to qualify for the generous tax breaks the investors receive. There are also no requirements that investments be spread across all the O-Zones, allowing the funding to flow to a small proportion of more prosperous or gentrifying areas. And there are no protections to maintain or expand affordable housing, meaning O-Zone investments are likely to add to the displacement of lower-income households and families of color from their homes and neighborhoods. Nor is there any mandated evaluation of the program. As the private fund industry publication *Pitchbook* noted, these investments “may produce healthy financial returns for investors but may lack in their contribution to the economic development of a region—the intended purpose of the legislation.”³⁴

The enacted O-Zone statute was derived from the bipartisan “Investing in Opportunity Act,” first introduced in 2015.³⁵ However, the tax cut statute did not include that bill’s modest accountability provisions. The O-Zone legislation omitted the earlier proposal’s required annual reports (after the program had operated for 5 years) that would have disclosed O-Zone investments at the national and state level; the number and value of Opportunity Funds; the percentage of O-Zones that received investments; and, importantly, an assessment of the impact O-Zone investments had on job creation, poverty



alleviation, and business creation.³⁶ Neither the earlier legislation nor the tax break law as passed included any evaluation or reporting of the potential negative impacts on communities such as displacement of residents of color and low-income residents or the elimination of existing local businesses.

The Trump administration implementation of O-Zones has not addressed the total absence of accountability standards, failure to set goals on impacts, or assessments of how or whether there are benefits to the low-income areas where investments will be made (for workers, residents, local businesses, housing costs, consumer prices, etc.). Nearly two years after the tax cut was enacted, Treasury has still not considered rules to evaluate the impacts, although it did solicit input on what data it might collect in May 2019.³⁷ As a result, it will be very difficult to comprehensively assess where O-

Zone investments have gone, whether they have been concentrated in thriving regions or struggling neighborhoods, or whether the investments have benefited or harmed residents or communities.

The O-Zone statute did require Treasury to issue regulations to “prevent abuse” of the program.³⁸ In April 2019, the IRS issued a second set of proposed rules to regulate Opportunity Fund investments, but they primarily related to determining what constituted allowable investments in O-Zone businesses, and did not establish any evaluation of the O-Zone investment outcomes for communities or residents.³⁹ The anti-abuse provisions were vague and unenforceable and required the IRS to determine whether O-Zone investments received tax benefits that were “inconsistent with the purposes” of the statute.⁴⁰

There were no requirements that the investments benefit residents or communities in Opportunity Zones. In a press conference following the release of the second set of proposed rules, Secretary Mnuchin said that reporting requirements were not an immediate priority and that Treasury did not want “oodles of reporting.”⁴¹ Although Treasury solicited input on what kind of data should be collected in 2019, it appeared to be a modest collection of investment information by the O-Funds, not the comprehensive data necessary to evaluate benefits or harms.⁴² While there have been no rule proposals to create meaningful accountability around O-Zones, the final tax rules still further reduced the targeting of the tax break by lowering investment requirements from 90 percent within O-Zones to only 40 percent,⁴³ allowing tax-subsidized dollars to leak out of the designated O-Zones altogether, likely flowing into still wealthier areas.



Washington, DC Opportunity Zone Buzzard Point, Credit: Kim Girton girtoncreative.com

Investments Most Likely to Flow to Subset of More Prosperous, Economically Transitioning O-Zones

The inclusion of many higher-income O-Zones and the lack of performance standards or requirements will encourage investors to receive tax benefits for spending that is concentrated in more affluent and already gentrifying neighborhoods in the most booming metropolitan areas where the profit opportunities are the greatest. Urban Institute Senior Fellow Brett Theodos said that the investors will pursue areas that are rapidly appreciating; “Where is that happening? It’s in the zones approaching gentrification. It could be that the lion’s share of the investment goes to a minority of the zones.”⁴⁴

Some of the O-Zones include rapidly developing areas. Washington D.C.’s O-Zones include the neighborhood with a new \$400 million soccer stadium as well as areas near the Navy Yard, Columbia Heights and

Shaw, and Capitol Hill East neighborhoods, where real estate projects have been popping and affordable housing options have been rapidly shrinking or disappearing.⁴⁵ More than half of NFL stadiums are located in O-Zones, including the \$1.8 billion stadium under construction for the Las Vegas Raiders.⁴⁶

The Long Island City neighborhood in Queens, New York was also designated an Opportunity Zone, even though it was the top neighborhood in the country for new apartment units from 2010 to 2016 and was targeted for the proposed Amazon

headquarters project (though the company said it would not have used the program for its since-abandoned development).⁴⁷ In Los Angeles, O-Zones cover parts of downtown, the tony Arts District, Hollywood and rapidly developing Koreatown, where an already started Hyatt hotel may benefit from the tax break.⁴⁸

Much of downtown Portland, Oregon including the Pearl District is covered by O-Zones, even though since 2016 developers had already planned to invest \$1.5 billion in this area, including a \$206 million luxury apartment tower.⁴⁹

Wall Street targeting already hot neighborhoods – ignoring stated goal of investing in “distressed communities”

Opportunity Funds are already focused on investing in the most profitable O-Zones — those with rising incomes, growing

populations, and appreciating property values. The investment industry, real estate business consultants and other market analysts have promoted the O-Zone tax break as an opportunity to reap tax benefits from strategic investing. The goal, according to the Treasury Department, is to encourage investment in “distressed areas,”⁵⁰ but the funds are aiming at the most affluent and avoiding those with the highest poverty levels.

Opportunity Funds and real estate advisors are promoting data-driven evaluation of O-Zone tracts based on investment

“attractiveness” scores, such as population size, economic growth, foot traffic and prior successful investments.⁵¹ Some are explicitly encouraging investors to target low-poverty or higher-income O-Zone areas – the very opposite of what the tax break was purportedly intended to promote.⁵² The real estate consultants

Cushman & Wakefield encouraged O-Zone investors to look for neighborhoods where “a process of economic improvement has already begun that can be further accelerated through the addition of new investment capital.”⁵³

The result is that the Opportunity Funds and consultants are promoting hot real estate – big cities and rapidly transitioning neighborhoods. Fundrise has highlighted major metropolitan areas, including Seattle, Los Angeles, Brooklyn and Manhattan, San Jose, and Portland as the best targets for O-



Crown Heights Brooklyn near multiple Opportunity Zones. Credit: Colin D. Young

Zone investments.⁵⁴ Develop Advisors LLC's Opportunity Zone index included San Jose, Salt Lake City, Honolulu, Denver, Washington D.C., and San Francisco-Oakland in their top ten O-Zone Cities.⁵⁵ Another ranking put downtown Seattle, Portland, and Oakland as well as Center City Philadelphia and Baltimore's Inner Harbor as the top five smart growth neighborhoods for O-Zone investments.⁵⁶

Since there are no requirements that O-Zone investments provide or expand affordable housing, Opportunity Funds are developing high-priced commercial real estate projects such as hotels, condominiums and apartment buildings in these areas. The tax rules provide greater benefits to longer-term projects that were launched earlier, so real estate projects that were underway or ready to proceed were quick to solicit Opportunity Fund financing. The *New York Times* reported that projects underway in 2019 included luxury apartment building in

Miami, a posh apartment tower in Houston, a New Orleans hotel, and a combination hotel-condominium project in Portland, Oregon.⁵⁷ None of these projects needed special tax benefits to spur investment, they were already planned or underway.

O-Zone Investments Threaten to Displace Low-Income Residents of Color

The O-Zone tax break will likely drive more investment into the already high-cost, economically transitioning, and gentrifying areas, which in turn threatens to raise housing costs and consumer prices, pushing lower-income families out of increasingly unaffordable neighborhoods. Average real estate prices are already rising in the designated O-Zones, paralleling how past geographically targeted tax incentive programs raised housing costs and contributed to displacement. According to

Pitchbook, the arrival of O-Zone investments could be “a harbinger of inflated cost of living.”⁵⁸

The fact that earlier tax incentives to promote economic development in disadvantaged areas ended up raising housing costs and displacing residents underlines this danger. The Federal Reserve Bank of San Francisco documented that prior community

development tax incentives consistently increased housing prices in the designated areas.⁵⁹ According to a 2019 *Wisconsin Law Review* article, “there is strong evidence that property values increase[d] in Enterprise Zones” that led to higher housing costs that “may price out the poorest members of the community.”⁶⁰ The Government Accountability Office reported that the federal Empowerment Zone program contributed to demographic changes, “as low-income residents were displaced by increases in property values and rental costs” and were replaced by higher-income people moving into the areas.⁶¹

In O-Zones, the investor-driven real estate boom has already increased real estate and housing costs. Real estate prices in the areas Treasury selected began rising as soon as the final O-Zone census tracts were announced. Real estate firm Zillow reported that home prices surged by more than 20 percent overall in the O-Zone neighborhoods since the designations, even before the rules of the program were finalized and investments begun.⁶² Investors poured over 60 percent more into purchasing development sites in

The O-Zone tax break will drive more investment into already high-cost, economically transitioning, and gentrifying areas, which threatens to raise housing costs, pushing lower-income families out of increasingly unaffordable neighborhoods. Earlier tax incentives to promote economic development in disadvantaged areas ended up raising housing costs and displacing residents, underlining this danger.

O-Zones after they were announced than in the prior year.⁶³ According to a 2019 study, development property and vacant land prices inside O-Zones rose 14 percent and 21 percent, respectively, after the final neighborhoods were selected.⁶⁴

The anticipated additional influx of speculative real estate investment is likely to drive up housing costs and accelerate

gentrification and the displacement of existing residents. A 2019 University of California, Berkeley study found that a 30 percent increase in typical neighborhood rents was associated with a 28 percent decline in low-income households of color in the San Francisco Bay region.⁶⁵ A 2019 NCRC study found that gentrification—especially prevalent in the bigger cities predicted to receive the bulk of the O-Zone investments—has already sharply increased property values and rental costs, diminishing the supply of affordable housing and displacing local residents, often African American and Latinx families.⁶⁶

The displacement impact could be the highest in the most expensive housing markets in the country where the O-Funds are targeting their investments, exacerbating the already serious problem of increasingly unaffordable housing for long-time low-income residents and residents of color. The SP Group found that high housing costs are already a problem in many Opportunity Zones, with 41 percent of O-Zone census tracts having typical rents that would

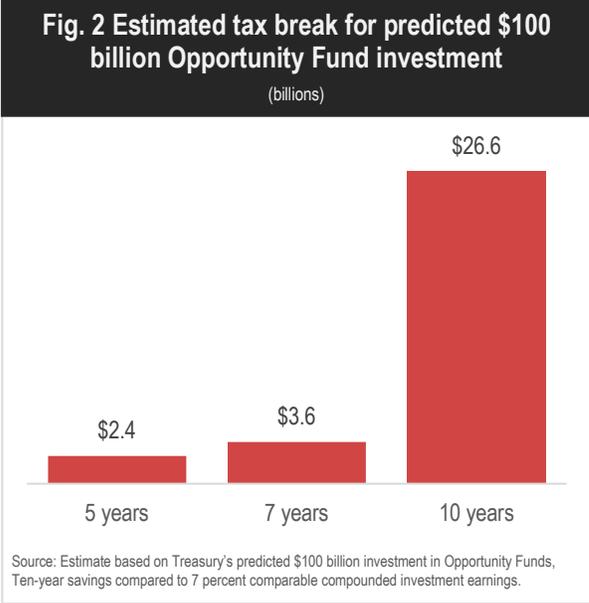
consume more than 30 percent of typical household incomes.⁶⁷

The O-Funds are likely to focus their investments in the O-Zones in economically vibrant cities or gentrifying areas that could raise housing costs and exacerbate displacement. For example, one O-Zone ranking put San Jose, California as the most attractive metro area for O-Zone investments.⁶⁸ But San Jose already has the second highest rents and most expensive homes in the country.⁶⁹ The ongoing gentrification in some of the regions with large numbers of O-Zones like New York City, Los Angeles, the San Francisco Bay Area, Portland and Houston has already spurred some of the highest levels of African American and Latinx displacement in the country.⁷⁰ As these O-Zones create hotter neighborhoods for investments, the long-time lower-income residents that qualified these areas for inclusion in the tax break program are the most vulnerable to dislocation due to higher housing costs.

O-Zones are a Major Tax Break

The O-Zone legislation created substantial tax breaks for transferring profits from investments into Opportunity Funds that pool these profits and then invest directly in qualified O-Zones. In theory, this should encourage private capital to flow into lower-income communities but that theory is undermined by the inclusion of so many economically transitioning or already prosperous neighborhoods in the program, along with the lack of standards or targets to focus on benefits to lower-income residents.

The tax “savings” for investors represent real losses to the public coffers. The Treasury Department and the Joint Committee on Taxation estimate that the O-Zone tax cuts would cost between \$13.3 billion and \$16.9 billion between 2019 and



2023.⁷¹ The federal revenue losses could be significantly larger further into the future when the largest tax cut provisions kick in after 10 years. In addition, states could face considerable tax revenue losses because many states mirror federal capital gains policies, so the Opportunity Zone tax breaks effectively undercut state capital gains tax revenues by millions of dollars every year.⁷²

The tax break is set up to encourage investors to move some of the \$6 trillion in unrealized capital gains (the unrealized profits from appreciated investments that have yet to be sold) into the O-Zones. The U.S. Treasury Secretary, Steven Mnuchin, estimated that \$100 billion of these parked capital gains could be shifted to Opportunity Funds.⁷³ For every \$100 billion invested in O-Zone vehicles for a decade, the federal government would lose (and investors would gain) an estimated \$26.6 billion in tax revenues (or in tax breaks).

The O-Zone statute provides three kinds of valuable tax breaks:

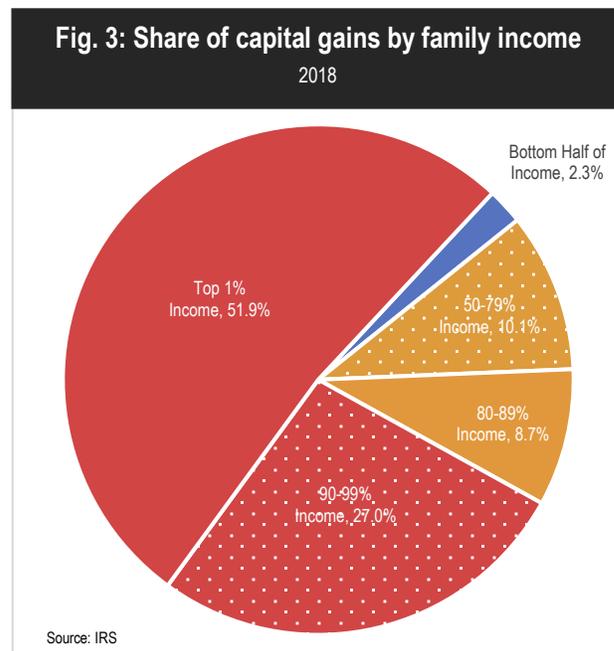
Deferred capital gains taxes: Investors can postpone paying taxes on realized

capital gains that are re-invested into an Opportunity Fund within six months.⁷⁴ The tax owed on the capital gains proceeds would be deferred until the Opportunity Fund stake is either sold or exchanged, or when this tax provision expires at the end of 2026.⁷⁵ The *Philadelphia Inquirer* referred to this portion of the program as a “juicy tax deferral opportunity.”⁷⁶ The capital gains deferral means investors can plow more initial money into Opportunity Funds, increasing the profit potential over the long-term.⁷⁷

Reduced capital gains tax owed:

Investors can reduce the tax they owe on capital gains that are moved and held in an Opportunity Fund. The tax break exempts 10 percent of the capital gains proceeds from taxes after 5 years and exempts another 5 percent after 7 years (for a total exemption of 15 percent of the original capital gain).⁷⁸ To receive the full seven-year capital gain tax reduction, investors would have to transfer earnings into Opportunity Funds by the end of 2019.⁷⁹ The savings from this deferred and reduced capital gains tax would be substantial. The projected \$100 billion investment in Opportunity Funds would receive a \$2.4 billion tax break after 5 years or a \$3.6 billion tax break after 7 years (see Fig. 2).⁸⁰

Total capital gains-tax exemption: Any capital gains earnings from Opportunity Fund investments that were held for at least 10 years would be totally exempt from capital gains taxes.⁸¹ *Pitchbook* called this provision “the most staggering tax benefit.”⁸² An investor could reap double the after tax earnings over a decade by investing capital gains in an Opportunity Fund instead of the stock market, according to one opportunity fund.⁸³ If investors shifted the predicted \$100 billion to Opportunity Funds and held the



investments for a decade, the total tax savings (including the deferred and reduced taxes plus the ten-year exemption) could amount to \$26.6 billion (Fig. 2).⁸⁴

Tax cut designed for the super-rich (including Trump cronies)

The O-Zone tax break will primarily benefit the very wealthy — those companies and individuals that have large, unrealized capital gains profits. The tax breaks are *only* available for reinvested profits from recently sold investments into Opportunity Funds.⁸⁵ Savings or principal from prior investments are not eligible to invest in Opportunity Funds. When a Treasury official pitched O-Fund investments to a crowd at the Harvard Club in New York City, he admitted that “the audience for opportunity zones is inherently fairly small because its limited to capital-gains income.”⁸⁶

The overwhelming majority of capital gains are earned and held by the highest-income families. Only 7 percent of taxpayers have any capital gains earnings.⁸⁷ Of those taxpayers that had capital gains earnings,

Table 1: Selected Opportunity Funds with over \$500 million investment target

Fund	Investments	Fund Size	Minimum Investment
Arkansas Opportunity Zone Fund (USA BioEnergy LLC)	Business, Real Estate	\$5,000,000,000	\$1,000,000
CIM Opportunity Zone Fund	Real Estate	\$5,000,000,000	
Belpointe Opportunity Zone REIT	Real Estate	\$3,000,000,000	\$10,000
SkyBridge Opportunity Zone REIT	Real Estate	\$3,000,000,000	\$100,000
Bridge Opportunity Zone Fund	Real Estate	\$1,000,000,000	\$250,000
Sikari Luxe Miami Opportunity Fund	Real Estate	\$750,000,000	\$50,000
Opportunity Development Group Fund I	Real Estate	\$650,000,000	
Arctaris Opportunity Zone Fund	Businesses	\$500,000,000	
Caliber Tax Advantaged Opportunity Zone Fund	Real Estate	\$500,000,000	\$250,000
Community Outcome Fund	Business, Real Estate	\$500,000,000	
Cresset-Diversified QOZ Fund	Business, Real Estate	\$500,000,000	\$1,000,000
Detroit Ozone Investment Fund	Real Estate	\$500,000,000	\$50,000
EJF OpZone Fund I	Real Estate	\$500,000,000	
EquiAlt Qualified Opportunity Zone Fund	Real Estate	\$500,000,000	\$25,000
EquityMultiple Opportunity Fund	Real Estate	\$500,000,000	
Fortuitous Partners Opportunity Fund	Business, Real Estate	\$500,000,000	
Galena Opportunity Fund	Real Estate	\$500,000,000	
Maxus Opportunity Fund	Real Estate	\$500,000,000	
OPZ Bernstein Opportunity Zone Fund	Real Estate	\$500,000,000	
RXR Realty Opportunity Zone Fund	Real Estate	\$500,000,000	
Somera Road Opportunity Zone Fund	Real Estate	\$500,000,000	
Starwood Opportunity Zone Fund	Real Estate	\$500,000,000	
Zone Opportunity Fund	Real Estate	\$500,000,000	\$50,000

Source: The Opportunity Zones Database. Available at: <https://opportunitydb.com/funds/>, accessed October 2019; minimum investment where available.

half of all of capital gains earnings were reported by just the top 1 percent of families with the highest income in 2018. The highest earning top 10 percent of families received over three-quarters of all capital gains earnings (see figure 3).⁸⁸ The lowest earning half of families reported only 2.3 percent of all capital gains earnings. In 2018 alone, the highest income 1 percent of families reported \$1.4 trillion in capital gains earnings.⁸⁹

But that is just the annual earnings. The Opportunity Zone program was described

as designed to encourage investors to sell parked investments with substantial unrealized capital gains. A Federal Reserve Board study found that the richest 10 percent of families held 93 percent of unrealized capital gains⁹⁰— the kinds of holdings the O-Zone policy was designed to attract.

The Opportunity Funds are really only options for the richest investors. Most of the qualified opportunity funds require very high initial investments—many require at least \$50,000, one SkyBridge fund has a

\$100,000 minimum investment, and the Pearl Fund has a \$250,000 minimum.⁹¹ In 2018, only the top 1 percent of highest income families had more than \$100,000 in capital gains on average — even the rest of the top 10 percent only took home an average \$47,000 in capital gains, which is not enough to take a stake in many Opportunity Funds. The bottom 80 percent of earners only received an average of \$3,600 in capital gains.

Private equity firms, hedge funds, and real estate developers are among those racing to take advantage of the Opportunity Zones tax breaks by establishing the largest Opportunity Funds. By April 2020, about 600 funds aimed to raise some \$70 billion (see Table 1, listing funds targeting at least \$500 million).⁹²

Notably, some of the funds would benefit Trump insiders, including former White House communications director Anthony Scaramucci (SkyBridge Opportunity Zone Real Estate Investment Trust⁹³), Trump ally and former New Jersey Governor Chris Christie (Hampshire Christie Qualified Opportunity Fund LLC⁹⁴), and former Trump Organization real estate employee Daniel Lebensohn (BH3 Debt Opportunity Fund⁹⁵). Presidential son-in-law Jared Kushner, whose wife, Ivanka Trump, pushed for the O-Zone tax break while Kushner owned a stake in the Cadre real estate investment firm he co-founded (which subsequently launched an Opportunity Fund).⁹⁶ In early 2019, Kushner sold his stake in Cadre after the firm raised concerns that his involvement raised the appearance of conflict-of-interest that was deterring other investors; the value of Kushner's Cadre investments quintupled from \$5 million to \$25 million over the prior three years.⁹⁷

Several private equity funds that have become corporate landlords by buying up thousands of single-family homes (often raising rents and compromising housing affordability) also already have started O-Funds. For example, Starwood Capital has a \$500 million Opportunity Fund but also owns 77,000 single-family homes; Related Companies has a \$250 million O-Fund and already owns 59,000 homes.⁹⁸

What can be done about O-Zones?

Opportunity Zones are a substantial tax giveaway to investors that will let Wall Street release an avalanche of money that is likely to be largely concentrated in a handful of cities and neighborhoods. The lack of standards and poor targeting make it highly likely that the program will fail to deliver substantial economic benefits to low-income neighborhoods or residents. In fact, the projects threaten to do harm. As the Urban-Brookings Tax Policy Center Senior Fellow Steve Rosenthal wrote, “there is serious risk that Opportunity Zones will foster a lot of investor interest, without substantially benefitting communities.”⁹⁹

Evidence points to a result where investors will extract much more value in tax savings than they provide in economic benefit to low-income areas or people. The total lack of disclosure or reporting standards means that the public will not know who is receiving the generous tax breaks, where funds are invested, and whether these investments provide tangible economic benefits to low-income areas or whether the investments accelerate displacement in low-income communities and communities of color.

Opportunity Zone tax break must be repealed: The Congress should repeal the Opportunity Zone break. The program does not make sense as

an approach to addressing the needs and goals of low- and moderate-income communities or individuals. Congress should instead devote resources to strategies that directly address these needs and goals (like building or refurbishing affordable housing units or improving key infrastructure like dangerous water systems) and that are accountable to local community priorities. Until the tax break is repealed, Congress should immediately undertake rigorous oversight of the program, while investments are being made.

Oversight should include demanding information about the investments taking advantage of Opportunity Zone tax breaks (which funds, which tracts, what kind of investments, how much funding, etc.) and about the impacts (including negative impacts like rising housing prices and displacement of residents and businesses). It should include Congress holding the executive branch agencies (IRS, Treasury, etc.) accountable to strengthen regulations and information collection and to impose performance goals as a condition of receiving tax breaks. Congress must prevent the Treasury Department and the IRS from further diluting tax rules governing O-Zone investments by permitting tax breaks for investments substantially outside the designated zones.

State and local measures to hold O-Zone investors accountable: States and localities should join the call for the tax break to be repealed, and for funds to be devoted to addressing community development priorities in low-income areas, including urgently needed affordable housing. But until the federal program is repealed, there are actions states and localities can take to limit the harm and increase the possibility of benefit, even though the rules of the program are set at the federal level. They can establish the performance criteria, disclosure requirements and other transparency and accountability measures Congress and the Trump administration failed to include in the program. A handful of places have begun the process of implementing O-Zone performance

measures, while others are moving to pile on additional O-Zone tax incentives without requirements that tie investor benefits to community benefits (see Appendix).

Appendix: States and Localities Should Establish O-Zone Accountability Policies

State and some local governments have already been involved in the program by nominating census tracts to become certified O-Zones. Since then, many state and local governments have created investment portfolios and inventories of available O-Zone projects. Forty-one states either do not tax capital gains or align state capital gains taxes with the federal tax code; only 5 states have their own capital gains tax provisions that do not confer the Opportunity Zone tax break for state taxes.¹⁰⁰

Eighteen states and Puerto Rico proposed enhanced or additional tax incentives in 2019 to lure investment to their O-Zones, creating a tax cut bidding war to entice investors that will ultimately further erode states' tax revenues (see Table 3). These state legislative efforts are illustrative of the kinds of supplementary incentives that are likely to be proposed in the coming years.

The city of Boulder, Colorado imposed a moratorium on building permits, demolition, and other applications for developments in the city's O-Zone tract until the city changes zoning and land use regulations to ensure the O-Zone investments would not displace people from an affordable neighborhood and that they would be aligned with a community development plan approved in 2017.¹⁰¹ In a much more limited move, Maryland has offered conditional access to additional tax credits to Opportunity Funds that report more information to the state Commerce Department.¹⁰² The additional tax benefits are tied to accountability requirements that include residents on O-Zone businesses' governing and advisory boards or through a community-Opportunity Fund agreement that specifies the benefits the fund agrees to provide to the community.

These examples point to the fact that states and localities can establish their own regulations to prioritize investments that further community goals and prevent O-Zone investments from

disruptively gentrifying neighborhoods and displacing residents. Possibilities include:

Preserve affordable housing and protect residents vulnerable to displacement: The O-Zone program appears likely to exacerbate the lack of affordable housing options in wealthier metropolitan areas and already gentrifying neighborhoods. The impending arrival of substantial investments into higher-priced housing makes it more urgent for states and localities to protect tenants from spiking rents and abusive landlords. Inclusionary zoning policies, rights of first refusal to purchase units and buildings, "just cause" eviction rules, new or strengthened rent control regulations, and the development of community land trusts would all help protect residents against displacement and excessive rent increases.¹⁰³

Supporting single-family homeownership in disinvested communities is another key way to prevent displacement and promote greater equity. Foreclosed homes in cities can frequently be rehabbed into affordable single-family homes to sell to families, and state and local governments can work with nonprofit developers and land banks to assemble packages of homes ripe for O-Zone investors interested in truly facilitating affordable housing and committed to affordability and accountability standards. State and federal governments can also address the common challenge of value gaps – which happen in neighborhoods where single-family property values are too low to support necessary rehabilitation – by providing grants and tax credits.

Impose accountability and transparency standards on Opportunity Fund investments:

States can establish their own accountability frameworks to increase the extent to which investments deliver economic benefits to communities and residents, and advance community-desired outcomes. States could require investors to enter into community agreements driven by resident-stakeholders with

Table 2: State Proposals to Supplement Federal O-Zone Program, 2019

State	Status	Tax or Policy Change
Alabama ¹⁰⁴	Enacted June 2019	\$50 million in annual tax credits to O-Funds if investments don't achieve 5-year expected returns
California	Pending May 2020 ¹⁰⁵	Streamline environmental reviews of O-Zone projects
	Did not pass ¹⁰⁶	\$200 million affordable housing tax credits in O-Zones, \$100 million tax credit to preserve affordable rental housing after O-Zone investments are sold.
Connecticut	Enacted June 2019 ¹⁰⁷	Facilitate O-Zone investments, study incentives, expedite permitting of O-Zone projects
	Pending May 2020 ¹⁰⁸	Exempt O-Zone projects from some historic preservation requirements in certain cities
Florida ¹⁰⁹	Did not pass	Revive state enterprise zone incentives, use O-Zone definitions for business investment
Kentucky ¹¹⁰	Did not pass	\$35 million in tax credits in rural counties and O-Zones targeting small businesses
Louisiana	Enacted June 2019 ¹¹¹	Additional tax breaks for structures under Restoration Tax Abatement
	Did not pass ¹¹²	Additional pilot tax credits for Louisiana-based manufacturers in O-Zones
Maryland	Enacted April 2019 ¹¹³	Apply 6 existing tax credits for O-Zone investments that provide increased disclosure
	Did not pass ¹¹⁴	State tax credit for O-Zone housing projects
	Did not pass ¹¹⁵	Certain financial assistance to O-Zone projects
	Did not pass ¹¹⁶	Applies business tax credit for expanding, locating in O-Zones
Massachusetts	Pending May 2020 ¹¹⁷	Priority technical assistance to promote O-Zones for midsize regional "Gateway Cities"
Michigan ¹¹⁸	Pending May 2020	R&D tax credits for auto industry in O-Zones
Nebraska ¹¹⁹	Enacted April 2019	Adds O-Zones to prioritized areas for Neb. housing/development/job training funds
Ohio ¹²⁰	Pending May 2020	Non-refundable 1% tax credit (up to 2% under some circumstances) for investments into Ohio O-Funds over \$250,000 that hold all their assets in Ohio O-Zones
Puerto Rico ¹²¹	Enacted May 2019	Territory-wide incentives, 25% tax credit, reduced income tax, 25% property/construction taxes.
Rhode Island	Did not pass ¹²²	10% tax credit for O-Zone investments in Pawtucket and Central Falls
	Did not pass ¹²³	20% tax credit for O-Zone investments statewide
South Carolina ¹²⁴	Pending May 2020	25% state tax credit capped at \$50,000 per taxpayer for O-Zone investments
Texas	Did not pass ¹²⁵	25% state tax credit for Businesses that rehabilitate buildings, purchase equipment in O-Zone; One-time tax refund of the lesser of 25% or \$50,000 for expenditures on labor, materials or equipment in O-Zone
	Did not pass ¹²⁶	25% tax credit for Texas approved O-Funds that meet job creation/retention standards
	Did not pass ¹²⁷	Up to \$35 million in insurance tax credits for certain O-Zone investments
Vermont ¹²⁸	Proposed 2019	Projects in O-Zones can receive annual village center/downtown tax credits
Virginia ¹²⁹	Did not pass	Solar tax credit on non-residential buildings in O-Zones
Washington ¹³⁰	O-Zone provisions removed	Tax credit against state insurance premiums for O-Funds that invest in rural areas
West Virginia ¹³¹	Enacted June 2019	Exemption from income tax for qualified O-Zone businesses from 2019 to 2025

strong, binding accountability standards in order to participate in the program. These requirements could include construction contributions to affordable housing, poverty alleviation, job creation, business start-ups, and other metrics.

Require that Opportunity Zone projects create good jobs for communities: States and communities could establish responsible employer standards in the permitting process to prevent companies that have a history of violating wage and hour rules, labor laws, workplace safety, or tax rules from constructing O-Zone projects. Developers and construction firms should use project labor agreements, pay prevailing wages, and establish uniform work rule on benefits, pay, and dispute resolution. Construction firms should recruit and train

workers from the O-Zone community where the project is being built.

Consider partnering with foundations and non-profits forming Opportunity Funds to invest in community-oriented projects:

States could attempt to attract positive investment by partnering with organizations that aim to maximize the positive community impact of O-Zone investments, including on affordable housing and long-term jobs. Some foundations and organizations promoting socially responsible investing have begun developing policy tools or offering parallel financial incentives (like loan guarantees) to encourage Opportunity Funds to improve transparency, accountability and community impact.¹³²

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2019), Hawaii (Hawaii Legislature. 30th Legislature. SB1130/SD1/HD1. Hawaii Governor David Ige. Gov. Msg. No. 1170. June 7, 2019), and Minnesota (Minnesota Legislature. 91st Legislature 2019 1st Special Session. HF5. Office of Governor Tim Walz. [Press release]. “Governor Walz signs budget bills into law.” May 31, 2019.). Puerto Rico also brought its capital gains taxes into conformity with federal rules (Puerto Rico Legislature. 2019 Session. SB 1147).

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