Addressing the Proposed Legislation of Qualified Rural Opportunity Zones: Are They Just Another Tax Break for the Wealthy or Can They Be Fixed?

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I. INTRODUCTION

Socioeconomic and economic disparity has a long history in the United States.1 Beginning in the 1800s, the gap between the wealthiest Americans and the rest of the nation began to widen.2 What started as the top 1% of the wealthiest Americans owning 25% of the nation’s wealth in 1810 has now increased to a total of 31% today.3 Further, the top 10% of the wealthiest Americans owned almost 60% of the nation’s wealth in 1810 and now own approximately 70%.4 Over the last forty years, through the Energy Crisis Recession in the early 1980s, the Great Recession of the late 2000s, and most recently, the COVID-19 pandemic, the top 1% has seen their annual average wages double, while the bottom 90% has seen their annual wage increase by a mere 29%.5 Throughout its history, the United States has been host to an increasing stratification between the uber-wealthy and the middle and lower-classes.6


2. Williamson & Lindert, supra note 1; see also The evolution of wealth inequalities over the last two centuries, CADTM (Apr. 1, 2021), https://www.cadtm.org/The-evolution-of-wealth-inequalities-over-the-last-two-centuries#nb (describing wealth inequalities in the United States and Europe from 1810 until 2010).


4. Wealth distribution in the United States in the third quarter of 2023, supra note 3; The evolution of wealth inequalities over the last two centuries, supra note 2.


The wealth gap has left the lower-income class with few job opportunities and significant barriers to education and healthcare. The government has addressed these socioeconomic disparities by encouraging direct investments from the private sector via tax incentives. The most recent tax initiative was the creation of Qualified Opportunity Zones (“QOZs”) as part of the Tax Cut and Jobs Act (“TCJA”) under the Trump Administration. The Opportunity Zone Program was the latest attempt to address economically distressed communities through a place-based incentive with the potential to shift some of the wealth out from the top 10% and back into the hands of the masses.

The government has encouraged private investment through people-based and place-based tax incentives to address the hardships faced by distressed communities and their residents who have been left behind. People-based incentives mobilize residents out of a distressed community to achieve a higher socioeconomic status. For example, the Low-Income Housing Tax Credit subsidizes low-income housing in higher-income neighborhoods. However, people-based incentives fail to improve communities as a whole and fail to address the underlying issues of why a community is economically distressed. Place-based incentives, on the other hand, aim to build up the economic conditions in long-suffering areas so that all residents can enjoy the benefits of plentiful resources and a healthy and safe life. This is important

8. See, e.g., Michelle D. Layser, How Place-Based Tax Incentives Can Reduce Geographic Inequality, 74 Tax L. Rev. 1, 8 (2020) [hereinafter Layser, Place-Based Tax Incentives].
11. Layser, Place-Based Tax Incentives, supra note 8, at 2–4.
12. Id. at 8–9.
13. Id. at 3.
14. Id.
because the place where one lives and the resources one can access impact people’s quality of life and overall health.15

The QOZ program is the first place-based incentive to mobilize significantly large amounts of capital and pool together resources to make investments that can have a real impact in distressed communities.16 The ease with which investments and improvements can be made via QOZ projects are virtually unrestricted due to their relatively lax requirements and regulations.17 In the first few years of its enactment, the QOZ project raised $75 billion dollars in private capital, while its closest predecessor, New Market Tax Credits (“NMTC”), mobilized roughly $63 billion dollars over twenty years.18 While the QOZ program has effectively mobilized capital,19 it has largely failed in its noble purpose while giving a significant tax break to the wealthy and arguably leaving the distressed community residents worse-off.20

Despite these failures, interest in a place-based tax incentive like the QOZ program remains, as evidenced by a recent proposal for a rural QOZ program that claims to fix past QOZ program failures and help underserved communities in a way previously not done.21 This Comment addresses the efficacy and failures of the original QOZ program to achieve its goal of incentivizing distressed community investment and analyzes how the proposed rural QOZ program fails to successfully address those pitfalls. Part II reviews the history of QOZ type programs and why the QOZ program has the potential to be extremely effective.


17. See Bender, supra note 16, at 12.


20. See discussion infra Part III.B.

Part III examines how the QOZ program works and the reasons for the program’s failures. Part IV discusses the differences and reasoning behind the changes in the proposed rural QOZ program. Then, Part V explains why the new rural QOZ program will not work as intended and will fail to address the same shortcomings seen in the initial QOZ program. Finally, Part VI will propose legislation and other solutions that allow the QOZ program to work as intended.

II. THE EMERGENCE OF QUALIFIED OPPORTUNITY ZONES

A. Prior Place-Based Incentives

The U.S. federal and state governments have tried multiple times to create effective place-based tax incentives such as empowerment zones, enterprise communities, renewal communities, and new market tax credits. These methods have mostly failed. Previous attempts to revitalize low-income and economically-distressed communities have largely led to gentrification, displacement of residents, and greater income disparity between the wealthy and the impoverished. Additionally, these place-based incentives did not go far enough to enable real change. Many of these incentives were structured as direct tax credits to the people who engaged in the incentivized business activity. For instance, the empowerment zones are one particular incentive that allows businesses located in government-designated and economically distressed census tracts to take advantage of different tax credits for

22. Coyne & Johnson, supra note 10, at 3.
engaging in business in that zone.\textsuperscript{26} The businesses can receive tax credits for certain activities like hiring and retaining employees who also live in that zone.\textsuperscript{27} Empowerment zones exist in both rural and urban areas; however, larger companies are the primary businesses that take advantage of these credits—not local business owners.\textsuperscript{28} The lack of success in empowerment zones represents just one instance of many place-based incentive failures.

Congress attempted to broaden and increase investment in low-income community projects with the NMTC.\textsuperscript{29} “[T]he NMTC is most structurally analogous to the Opportunity Zones incentive” compared to other existing tax incentives used to promote economic development because it allows some pooling of resources.\textsuperscript{30} Unlike QOZs, the NMTC gives tax credits to \textit{intermediaries}, Community Development Entities (“CDEs”), who sell their tax credit to investors so the intermediaries can pool money together.\textsuperscript{31} The CDEs use the investors’ money to fund projects in severely distressed census tracts through either loans or equity.\textsuperscript{32} Typically, these investments operate via debt.\textsuperscript{33} Additionally, CDEs have to apply to receive the tax credits every year.\textsuperscript{34} These rules, however, have financially limited NMTC projects—almost one-third of NMTC projects were under $500,000 with only 10% of projects reaching over $25,000,000.\textsuperscript{35} The actual impact was not significant to the community’s residents in the corresponding distressed census tracts

\textsuperscript{27} \textit{Id.}
\textsuperscript{29} See Griffith & Michel, \textit{supra} note 25, at 3.
\textsuperscript{31} See \textit{id.} at 175–76.
\textsuperscript{32} \textit{Id.} at 175–77.
\textsuperscript{33} \textit{Id.} at 176.
\textsuperscript{34} \textit{Id.} at 175; see also Guidance for Certification of Community Development Entities, New Markets Tax Credit Program, 66 Fed. Reg. 65806, 65810 (Dec. 20, 2001).
\textsuperscript{35} Bender, \textit{supra} note 16, at 4.
due to the lack of restrictions on projects the NMTC can fund, the inability to pool equity resources, and the relatively small size of the projects.36

B. Qualified Opportunity Zones

The QOZ program, on the other hand, pools a significant amount of funding together and be capital driven instead of debt driven.37 Rather than reducing the cost of employment or investment in a certain area, taxpayers are encouraged to bring their money together to make large scale investments.38 The concept of opportunity zones can be traced back to Silicon Valley billionaires who helped create the Economic Innovation Group, a think tank, which aims at “forging a more dynamic and inclusive American economy.”39 This think tank produced a report by two economists that addressed renewed attention towards economically distressed communities and geographically focused policy in the fallout of the Great Recession.40 The think tank specifically highlighted the uneven recovery between cities after the Great Recession, where some cities experienced extremely high unemployment rates, other cities beat, or came close to their pre-Great Recession employment numbers like Idaho Falls, Idaho with a 3.1% unemployment rate or Denver, Colorado with a 3.9% unemployment in December 2014.41 Examples of cities which failed to recover from the

36. Id.
37. Layser, Subsidizing Gentrification, supra note 30, at 177–78.
38. Coyne & Johnson, supra note 10, at 1–3.
39. About Us, ECON. INNOVATION GRP., https://eig.org/about-us/ (last visited Nov. 26, 2023); David Schleicher, Why We Can’t Have Nice Place-Based Policies: A Review of David Wessel’s Only the Rich Can Play, 31 J. AFFORDABLE HOUS. & CMTY. DEV. L. 19, 19–20 (2022) (book review); Timothy Weaver, The False Promise of Opportunity Zones, Bos. Rev. (April 13, 2023), https://www.bostonreview.net/articles/the-false-promise-of-opportunity-zones/; see Bender, supra note 16, at 4–5 (explaining that there were calls for a “new tax program” that could produce larger investments than previous place-based programs, which was answered by the QOZ program).
40. JARED BERNSTEIN & KEVIN A. HASSETT, ECON. INNOVATION GRP., UNLOCKING PRIVATE CAPITAL TO FACILITATE ECONOMIC GROWTH IN DISTRESSED AREAS 1–2 (2015).
Great Recession include El Centro, California with a 23.1% unemployment rate in December 2014 and Yuma, Arizona with a 25.6% unemployment rate at the end of 2014. The economists were especially concerned with the social effects of job loss on individuals and on the U.S. economy as a whole.

Looking at the issues with the prior place-based incentives along with the importance of geographic investment, these economists recognized a growing, untapped source of potential funds in unrealized gains held by venture capital investors, company founders, and other wealthy individuals. In 2015, economists estimated that the total unrealized gains held by U.S. investors were roughly $2.26 trillion. Naturally, in recent years, these enormous figures of unrealized gains have been eyed by members of Congress and the President Biden as a potential new base to levy taxes since they are currently untaxable.

42. Bernstein & Hassett, supra note 40, at 2.
43. Id. at 2–3 (noting that growing up in a poorer neighborhood leads to a lifetime earnings gap and higher rates of divorce; longer spans of unemployment make reemployment less likely; and unemployment leads to increased death rates, suicide, and illness).
44. Unrealized gains are the increased value of an asset that the owner has yet to sell. Alicia Tuovila, Unrealized Gain Definition, INVESTOPEDIA (Dec. 11, 2022) https://www.investopedia.com/terms/u/unrealizedgain.asp#:~:text=The/term/unrealized/gain/refers,has/yet/to/be/realized. Before a sale of an asset that has appreciated in value, the unrealized gain remains untaxed. Id. Once the owner chooses to sell the asset, those unrealized gains become realized and are typically subjected to a capital gains tax. Id. Unrealized gains exist solely on ‘paper,’ and they may increase or decrease depending on the value of the asset that day. Id.
46. Id. at 16.
Making efficient use of these funds is particularly appealing, considering that these unrealized gains sit idle in the pockets of millionaires and billionaires who do not want, nor need, to sell their assets and pay taxes.\textsuperscript{48} To pay bills or make investments, wealthy individuals can leverage other means, such as taking out loans instead of liquidating their investments in the market.\textsuperscript{49} This allows their investments to remain in the market, accruing even further unrealized gains. Previous tax proposals targeting these unrealized gains have failed and future proposals are unlikely to gain traction in the future.\textsuperscript{50}

Instead of letting the vast repository of unrealized gains go unused and untaxed, the Economic Innovation Group proposed mobilizing them as investments in economically distressed communities.\textsuperscript{51} Furthermore, if the gains were invested long enough, the investors could get their money back tax-free.\textsuperscript{52} This would encourage people to move their money and help fill in the gaps where the government could not, while also giving distressed economies a boost of resources, far out-reaching the programs of the past.\textsuperscript{53} After going through considerable changes throughout the bureaucratic process, this proposal became law

\begin{footnotes}
\textsuperscript{48} For instance, if an investor bought 132 shares of Facebook (now Meta) stock in 2012 when the company had its Initial Public Offering, it would have cost a total of $5,016. Brian Withers, \textit{If You Invested $5,000 in Facebook’s IPO, This Is How Much Money You’d Have Now}, MOTLEY FOOL (Nov. 17, 2019, 9:02 AM), https://www.fool.com/investing/2019/11/17/if-you-invested-5000-facebook-ipo-how-much-have.aspx. If the investor never sold the 132 shares, they would be worth almost $25,212 today, equating to an almost $20,000 in unrealized gain. \textit{Id.} Company founders often have a majority, if not all, of their stock with a basis close to zero dollars, such as $.0001/share, meaning that any appreciation at all is essentially unrealized gain waiting to be realized whenever it is sold. Matthew Bartus, \textit{There Is No Such Thing as “Founder Stock” (legally speaking)}, COOLEY GO (Jan. 23, 2022), https://www.cooleygo.com/thing-founder-stock-legally-speaking/.


\textsuperscript{50} Schwartz & Wilkie, \textit{supra} note 47; York, \textit{supra} note 47; Iacurci, \textit{supra} note 47.

\textsuperscript{51} \textit{BERNSTEIN & HASSETT, supra} note 40, at 16–20.

\textsuperscript{52} \textit{See id.} at 18.

\textsuperscript{53} \textit{Id.} at 18–19; \textit{see discussion supra} Part II.A.
\end{footnotes}
under the Trump Administration’s TCJA. While earlier incentives took a more interdependent approach, requiring extensive coordination among different actors, the QOZ program is the first of its kind to leave multi-step coordination requirements behind and pool enough money together to enable real change.

III. Efficacy and Failures of Qualified Opportunity Zones

A. How Qualified Opportunity Zones Operate

Opportunity zones are designated census tracts that meet certain criteria categorizing an area as economically distressed. Under the TCJA, these zones are the same as the NMTC areas; however, state governors can only elect up to 25% of their eligible zones.56

An eligible tract must have a poverty rate of at least 20%, or the median family income in the tract must not surpass 80% of median family incomes in the greater metropolitan area.57 For tracts in nonmetropolitan areas, the median family income cannot surpass 80% of the statewide median family income.58 Contiguous tracts to an eligible zone are also eligible if their median family income does not exceed that of the contiguous low-income community by 125%.59 In sum, the average income of tracts in urban areas cannot exceed the average income of 80% of their greater urban area, while tracts in rural areas cannot have an average income greater than 80% of that state.60 Likewise, tracts that are adjacent to urban and rural low-income tracts may also qualify to be a QOZ if the average income in the adjacent tract is only 25% more than its low-income tract neighbor.61

55. BERNSTEIN & HASSETT, supra note 40, at 17.
56. § 1400Z-1(d). If a State has less than 100 low-income communities, then the State may designate up to 25 zones. Id.
57. § 1400Z-1(c); § 45D(e).
58. § 45D(e).
59. § 1400Z-1(e).
60. § 45D(e).
61. § 1400Z-1(e).
Once a QOZ is selected and approved, a QOZ fund pools together resources from investors and uses it to hold QOZ property or QOZ business stock.\textsuperscript{62} To receive preferential treatment, QOZ funds must hold 90\% of QOZ property in relation to their total assets.\textsuperscript{63} If a fund holds QOZ property, the fund must substantially improve the property within thirty months of acquisition.\textsuperscript{64} Congress stipulated that “substantially improved” requires capital expenditures for a property to be equal to its adjusted basis on the day of acquisition.\textsuperscript{65} This encourages QOZs to move quickly to improve an area while discouraging investments from being spent on buildings already in good shape.\textsuperscript{66} If a QOZ fund purchases a more updated, nicer building, it will have to spend, essentially, an equal amount to the purchase price making improvements to that building which will be a difficult and costly task, versus purchasing a dilapidated building where it is easy to spend money improving it and is likely cheaper overall. Instead of a QOZ fund purchasing one expensive, updated property in an area, it can purchase multiple, neglected properties, refurbish them and significantly increase the funds value by doing so.

For QOZ business stock, a business must have at least 50\% of its income derived from doing business in its respective zone, and the business must have less than 5\% of the average adjusted bases of its assets attributable to nonqualified financial property.\textsuperscript{67} Nonqualified financial property includes financial vehicles such as debt, stock, partnership interests, options, warrants, futures contracts, and other similar properties.\textsuperscript{68} Nonqualified financial property excludes working capital held for no longer than thirty-one months and accounts receivable balances acquired in the ordinary course of business.\textsuperscript{69} These exclusions streamline investments, allowing for the substantial improvement of property,

\begin{itemize}
  \item \textsuperscript{62} § 1400Z-2(d)(1).
  \item \textsuperscript{63} \textit{Id.}
  \item \textsuperscript{64} § 1400Z-2(d)(2)(D)(ii).
  \item \textsuperscript{65} \textit{Id.}
  \item \textsuperscript{66} See Trivedi, \textit{supra} note 26, at 780–81 (discussing the intent behind the “substantial improvement” provision and the need to discourage investors from “simply acquiring and holding on to existing property indefinitely.”).
  \item \textsuperscript{67} § 1397C(b); U.S. DEP’T TREASURY, \textsc{Instructions for Form 8996: Qualified Opportunity Fund 3} (2022).
  \item \textsuperscript{68} U.S. DEP’T TREASURY, \textsc{Instructions for Form 8996: Qualified Opportunity Fund 3} (2022).
  \item \textsuperscript{69} \textit{Id.}
\end{itemize}
trades, and businesses within a reasonable time frame, without strict
time limits on large projects.\textsuperscript{70} The working capital must also be used
to develop the trade or business in a QOZ or to acquire or substantially
improve property in a QOZ.\textsuperscript{71}

Opportunity zones are funded by realized capital gains from inves-
tors.\textsuperscript{72} Using capital gains incentivizes investors to sell their stock, free-
ing up unrealized gains which can now impact communities across the
U.S. Investors selling stock or other capital gain-eligible property have
180 days to take those now liquid gains and invest that money into a
QOZ fund.\textsuperscript{73} QOZs provide three major tax benefits to investors in
exchange for their investment into a distressed community.\textsuperscript{74} First, an
investor can enjoy a temporary deferment of capital gains tax.\textsuperscript{75}
Second, holding a QOZ investment for five years can result in a perma-
nent 10\% reduction in capital gains that are taxed; this increases to a
15\% reduction if held for seven years.\textsuperscript{76} And third, an investor can ob-
tain a 100\% exclusion of capital gains tax on their investment if it is
held in a QOZ for ten years.\textsuperscript{77}

To illustrate, consider the following example: an investor purchases
$25,000 in stock in year zero. By year six, the stock is now worth
$125,000. The gain on the initial investment is $100,000 ($125,000 in
proceeds less the $25,000 of “basis”\textsuperscript{78} in the initial investment).\textsuperscript{79}
Assuming the investor is taxed at the maximum long-term capital gains

\textsuperscript{70}. Victoria Lee, Opportunity without Reach: The Problems with the Oppor-
tunity Zone Program and the Need for Clarification, Oversight, and Regulation, 47
\textsuperscript{71}. U.S. DEP’T TREASURY, INSTRUCTIONS FOR FORM 8996: QUALIFIED
OPPORTUNITY FUND 3 (2022).
\textsuperscript{72}. See § 1400Z-2.
\textsuperscript{73}. § 1400Z-2(a)(1)(A).
\textsuperscript{74}. H.R. REP. NO. 118-128, at 29 (2023).
\textsuperscript{75}. § 1400Z-2; H.R. REP. NO. 118-128, at 29.
\textsuperscript{76}. § 1400Z-2; H.R. REP. NO. 118-128, at 29. In other words, the overall tax
bill would be reduced from 20\% of capital gains to 18\%.
\textsuperscript{77}. § 1400Z-2; H. REP. NO. 118-128, at 29.
\textsuperscript{78}. Basis is the cost of an investment. Julia Kagan, Basis: Definition and
Examples in Finance, INVESTOPEDIA (Oct. 6, 2021), https://www.investopedia.com/
terms/b/basis.asp#. When an asset is sold, the basis is subtracted from gross proceeds
and is not taxed in the sale. \textit{Id}.
\textsuperscript{79}. § 1001(a); \textit{see infra} Figure 1.
rate of 20%, selling the stock in year six would subject the investor to $20,000 in taxes ($100,000 multiplied by 20% capital gains rate).\textsuperscript{80} However, if the investor elects to put the entire $125,000 of proceeds from the sale of stock into a QOZ within 180 days of the sale, the $20,000 tax bill on the $100,000 of capital gains is eligible to be deferred, minimized, or permanently excluded.\textsuperscript{81}

Suppose the investor takes the $100,000 out of the QOZ after five years; she will have deferred her capital gains tax for five years and excluded 10% of the gain from taxation.\textsuperscript{82} The investor would increase her basis by 10% of the $100,000, amounting to $10,000. Consequently, the tax at the 20% long-term capital gains rate would be assessed on $90,000, resulting in an $18,000 tax bill.\textsuperscript{83} After seven years, the basis would be increased to 15% which is $15,000.\textsuperscript{84} Thus, the new amount that capital gains tax is assessed on decreases to $85,000, resulting in a $17,000 tax bill.\textsuperscript{85} Now suppose the investment is left for ten years; the basis becomes 100% of whatever is withdrawn from the fund after year ten, and there would be no federal tax bill even if the investor’s original investment appreciates over $125,000.\textsuperscript{86}

In summary, an investor can change a $20,000 tax bill due year zero and make it an $18,000 bill due in year five, a $17,000 bill due in year seven, or a $0 bill due in year ten. Additionally, the final tax bill does not consider the time value of money saved by not paying taxes on those gains while they act as an investment the QOZ.\textsuperscript{87}
B. Qualified Opportunity Zones and Their Failures

Initially, QOZ programs posed great potential and the original idea proposed by the Economic Innovation Group could have worked.\(^{88}\) However, as the tax proposal made its way through the bureaucratic system, it was manipulated and changed, depriving the targeted communities of its intended benefits.\(^{89}\) Many studies, scholars, and analysts have revealed contradictory or insignificant findings, and many articles have found stories of success and stories of corruption relating to the operations of these QOZs.\(^{90}\) This Comment examines five general reasons QOZs have not worked.

\(^{88}\) See infra Part VI.A.

\(^{89}\) Schleicher, supra note 39, at 20–22.

\(^{90}\) Coyne & Johnson, supra note 10, at 2 (listing studies that found no evidence to suggest the QOZ program affected startup investment, commercial investment, business or business growth, nor did the program positively impact poverty rates, but some studies did find evidence of an increase in real estate prices in QOZ tracts); see also Weaver, supra note 39 (discussing different examples of corruption, such as the Ritz-Carlton in downtown Portland that was built using tax-free gains, and different examples of ‘positive cases’ such as the affordable housing in Brookville, Indiana).
1. The Definition of Eligible Census Tracts Was Too Broad

First, the broad definition of eligible census tracts for opportunity zones led to the qualification of many neighborhoods, cities, and towns that were not economically depressed and when looking at the spirit of the program, should not have been eligible. For example, the entirety of downtown Portland is an opportunity zone, 60% of National Football League stadiums are in eligible QOZs, and QOZ funding is being used to build a luxury hotel and casino less than a mile from the Las Vegas Strip and Allegiant Stadium, home of the Las Vegas Raiders football team. By allowing governors to designate census tracts with minimal base requirements, the program opened the doors for corruption and lobbying. Local governments are motivated to select the tracts that draw in the most money for investors. Further, local governments directly influence what projects will be worked on within the QOZ. For instance, local governments have the authority to approve and deny permits, specifically permits that govern “building height variances, promotion of certain goals about population density, [and] mixed-income housing units.”

91. See Bender, supra note 16, at 12–13; Schleicher supra note 39, at 20.
94. Donald J. Marples, Cong. Rsch. Serv., R45152, Tax Incentives for Opportunity Zones 9–10 (2022). It is easy to see how investing in a large casino hotel near the Las Vegas Strip would yield more gain and attraction overall than investing in the rural town of Wells, Nevada where 43.3% of its 1,057 residents live below the poverty line and its main draw is a “set up shop for day trips.” Census Data for Wells, Nevada, Census Rep., https://censusreporter.org/profiles/16000US3283000-wells-nv/ (last visited Feb. 22, 2024); Wells, Travel Nev., https://travelnevada.com/cities/wells/ (last visited Feb. 22, 2022).
96. Id.
power, local politicians are susceptible to lobbying and manipulation, which leads to corruption.97

Due to these issues inherent to the designation and operation of QOZs, there are quite a few ‘bad apple’ stories that have surfaced since the program’s enactment in 2018. For example, Maryland’s governor revised his QOZ nomination after extensive lobbying efforts.98 Another story from Florida revealed that the governor amended his QOZ nomination to include a tract that one of his donors had planned to develop into a superyacht arena.99 Further, Oregon’s governor designated Portland’s entire business sector for QOZ benefits which was used to construct a Ritz-Carlton luxury hotel.100 To attract the most investment to their respective states, governors were incentivized to pick zones most appealing for returns on investment and ripe for appreciation.101 The areas most ripe for appreciation were not severely economically distressed communities but areas that were gentrifying, which side-stepped the entire aim of the QOZ program.

However, there have been some “good apple” stories. For example, the SoLa impact project helped build affordable housing in Los Angeles; the Chicago Cook Workforce Partnership helped build housing where rent is equal to property tax; and the Agricultural Technology Campus in Hampton County, South Carolina helped create jobs and bring localized agriculture to that State.102 Nevertheless, because investing in these “good” projects do not yield as much return on

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97. See Weaver, supra note 39 (discussing QOZ redesignations suggesting governors’ ulterior motives, such as making donors happy or receiving a personal benefit); see also MARPLES, supra note 94, at 9–10 (explaining that “[a]bsent further congressional legislation, subnational government will likely play a larger role in types of individual projects and activities that will be supported by OZ investment” allowing local government to exercise discretion and choose the most attractive projects, which opens the door to choosing projects that help the official stay in power or that personally benefit the official).

98. Weaver, supra note 39.

99. Id.

100. Id.; see generally Schleicher, supra note 39, at 22.


investment as luxury real estate-type projects do, the projects that have a positive impact on the community are not as common in QOZs.\textsuperscript{103}

2. The QOZ Program Led to Gentrification

The second reason that QOZs have failed is because the innate structure of the program and each state governor’s incentive to attract the most investment to their own state has led to a mass designation of eligible zones that were already being gentrified.\textsuperscript{104} These tracts previously indicated evidence of gentrification before 2018, and their designation as QOZs only amplified these trends.\textsuperscript{105} These areas had the highest potential for return and, consequently, received the bulk of the designations and the bulk of the investment.\textsuperscript{106} Based on tax data, the designated OZs that were economically better off than other designated OZs received more funding because they had a higher return on investment; the better-off OZs also had “higher educational attainment, median household income and housing values.”\textsuperscript{107} For example, of all QOZs designated,\textsuperscript{108} 2\% were contiguous zones already being gentrified and on their way out of economic distress, and yet this 2\% received 6\% of the actual amount invested in QOZs in 2019 and 5\% in 2020.\textsuperscript{109}

\begin{enumerate}
\item \textsuperscript{103} See Layser, Place-Based Tax Incentives, \textit{supra} note 8, at 54–55.
\item \textsuperscript{104} See H.R. REP. NO. 118-128, at 34 (2023) (“The Committee believes that the existing opportunity zone program too often neglects areas with persistent poverty in favor of those that are rapidly gentrifying.”).
\item \textsuperscript{105} See, e.g., Haydar Kurban et al., Gentrification and Opportunity Zones: A Study of 100 Most Populous Cities with D.C. as a Case Study, 24 \textit{CITYSCAPE: J. POL’Y DEV. \& RSCH.} 149, 162–64, 173 (2022); Coyne & Johnson, \textit{supra} note 10, at 11 (noting that many tracts ultimately designated as QOZs were already developing economically and the influx of capital from the QOZ program helped some of those tract’s economies increase at a much faster rate than other OZ eligible tracts not receiving investment).
\item \textsuperscript{106} See Coyne & Johnson, \textit{supra} note 10, at 11.
\item \textsuperscript{107} \textit{Id.}
\item \textsuperscript{108} \textit{Id.} at 7–8 (listing statistics gathered from tax returns forms 8996 and 8997 for QOZs and emphasizing form 8996 reports on total assets and breaks out QOZ investment by type and by QOZ number, which identifies the census tract.) Form 8997 reports on capital gains deferred and tracks those gains in the subsequent years).\textit{Id.; see generally Opportunity Zones Frequently Asked Questions, IRS, https://www.irs.gov/credits-deductions/opportunity-zones-frequently-asked-questions (last visited Nov. 26, 2023).}
\item \textsuperscript{109} Coyne & Johnson, \textit{supra} note 10, at 10, 21.
\end{enumerate}
The urban QOZs, representing 86% of total zones, received 96% and 95% of actual investment in 2019 and 2020, respectively. This equates to urban QOZs receiving 12% more investment than their relative OZ designation and contiguous tracts receiving 300% more than their relative OZ designation. Further, only 5% of zones received 78% of all OZ investments, with just 1% of zones receiving almost 50%. In short, this data shows that a disproportionate share of investment went to contiguous zones already on their way out of economic distress, violating the goals of the QOZ incentive.

Furthermore, studies measuring the differences between designated OZs and OZs that were eligible for designation revealed that designated OZs were already trending toward employment growth and other metrics for economic prosperity before being picked. Overall, studies show little to no impact on unemployment, poverty rates, business activity, or business creation. Even in nonmetropolitan areas, there was no increase in employment or business establishments. Additionally, a case study of the opportunity zones in D.C. found that 68% of the designated zones “were either gentrifying or adjacent to two or more gentrifying tracts.” On the whole, there are contradictory findings on the effects of OZs, but most studies have found little to no positive impact on employment, income, business investment, or poverty. What positive impacts did occur were outweighed by the cost to the government of foregoing capital gains taxes.

110. Id.
111. Weaver, supra note 39. For instance, California and New York had $4.8 billion and $3.93 billion in QOZ property invested in their state, respectively, while Iowa and New Hampshire had $30 million and $40 million, respectively. Coyne & Johnson, supra note 10, at 22.
112. See, e.g., Kurban et al., supra note 105, at 152, 162–69 (examining D.C. and the effects of QOZ designation on key economic metrics and gentrification there before and after the program).
113. Coyne & Johnson, supra note 10, at 2–3 (examining studies that considered job posting data, venture capital investment data, credit card data, and loan data).
114. Id. at 2 (noting, however, that many if not all of these studies rely on data from the first few years of the program and that it may take much longer before the true effects of QOZs can be measured).
115. Kurban et al., supra note 105, at 173.
117. See U.S. GOV’T ACCOUNTABILITY OFF., GAO-21-30, OPPORTUNITY ZONES: IMPROVED OVERSIGHT NEEDED TO EVALUATE TAX EXPENDITURE
3. There Is a Lack of Adequate Reporting Metrics

Third, there is a lack of reporting on metrics required for QOZs. Many criticisms are aimed at the legislation’s inadequate disclosure requirements and the deprivation of readily available data points for analysts to thoroughly analyze.\textsuperscript{118} Despite amendments to the QOZs reporting requirements, there is still a scarcity of data to determine beneficial investments or to pinpoint the investments actually improving their census tract both in quantitative and qualitative means, etc.\textsuperscript{119} Moreover, economists and analysts speculate that it is still too early to tell whether these zones “work.”\textsuperscript{120} While the investment is easily made within a year or so, the tangible impact on the community may take much longer to realize.\textsuperscript{121}

4. The Tax Benefit Structure Does Not Incentivize the Proper Behavior

Fourth, the QOZ structure incentivizes the wrong type of behavior. The QOZ program is highly profit-motivated and lacks safeguards and regulatory oversight.\textsuperscript{122} Consequently, QOZs have only magnified the gentrification effect created in part by NMTCs.\textsuperscript{123} These kinds of zones were picked in already up-and-coming areas in order to attract the most investors and compete with other QOZs.\textsuperscript{124} As a result, many of the QOZ projects were only those that would yield the highest return to investors, and, in turn, real estate projects, specifically luxury real estate, are among

\textsuperscript{118} Eastman, supra note 93, at 7.

\textsuperscript{119} Hartt, supra note 16; Opportunity Zones: Improved Oversight Needed to Evaluate Tax Expenditure Performance, supra note 117, at 19.


\textsuperscript{121} Id.

\textsuperscript{122} Layser, Subsidizing Gentrification, supra note 30, at 218.

\textsuperscript{123} Id. At 172.

\textsuperscript{124} Michelle D. Layser, The Pro-Gentrification Origins of Place-Based Investment Tax Incentives and a Path Toward Community Oriented Reform, 2019 Wis. L. Rev. 745, 766 (2019).
the largest portion of investments.\textsuperscript{125} Real estate is another common investment—it is easy to guarantee compliance with applicable regulations and property values tend to appreciate,\textsuperscript{126} especially in gentrifying areas.\textsuperscript{127} There was no incentive structure to encourage investment in things such as infrastructure, affordable housing, or socially and environmentally responsible development projects which might benefit the community but offer little in return to the investors.\textsuperscript{128}

5. The QOZ Program Has Not Helped the Wealth Gap

Fifth, these zones have effectively shifted economic opportunity instead of creating it, while providing significant benefits to the wealthy.\textsuperscript{129} Because the QOZ is only funded by capital gains, only those with access to capital gains may participate. Further qualifications, such as being an accredited investor, also act as a barrier to those who may invest in a QOZ.\textsuperscript{130} This has essentially directed the benefits of QOZs toward high net-worth individuals who are accredited investors and have capital gains to invest, effectively making the rich richer.\textsuperscript{131} Some have argued that capital gains themselves are one of the many culprits in the economic divide this country faces.\textsuperscript{132} Tax returns with over $1,000,000

\begin{footnotes}
\footnote{125. Coyne & Johnson, \textit{supra} note 10, at 9. Of assets held by QOZ funds in 2019 and 2020, roughly 60\% were in real estate. \textit{Id.}}
\footnote{126. \textit{Id.}}
\footnote{127. See Alina S. Schnake-Mahl et al., \textit{Gentrification, Neighborhood Change, and Population Health: a Systematic Review}, J. URB. HEALTH 1, 1–2 (2020).}
\footnote{128. See Bender, \textit{supra} note 16, at 12 (explaining that there are no social impact requirements in the QOZ program, so profit-motivated Wall Street fund managers can take hold and ignore social goals while maximizing return for investors).}
\footnote{129. Hartt, \textit{supra} note 16; Marples, \textit{supra} note 94, at 8.}
\footnote{131. Bender, \textit{supra} note 16, at 15.}
\footnote{132. See, e.g., Joe Hughes, \textit{Limiting Tax Breaks for Capital Gains Would Mitigate the Racial Wealth Gap}, INST. ON TAX’N & ECON. POL’Y (Oct. 14, 2021),}
in Adjusted Gross Income ("AGI") were estimated to be responsible for over half of capital gains reported in 2012; in 2020, tax returns with over $1,000,000 AGI were estimated to be responsible for over 67% of capital assets reported on tax returns, despite making up less than 0.5% of total returns filed. In 2020, the median AGI of a QOZ investor was $750,000, and the average investment in a QOZ was $1,000,000.

Overall, the QOZ program has been running into the same issues as its place-based incentive predecessors. Early data has shown intensified gentrification which often displaces a community’s residents. The QOZs are also not shown to have increased any employment opportunities or to have ‘lifted residents out of poverty.’ Additionally, the QOZs were not structured correctly to incentivize the right kind of behavior. The rules were too lax and broad, and allowed the wealthy to take advantage of a tax break without actually benefitting the communities the QOZ program was intended to help.

In the wake of heavy criticism of the opportunity zones and their trends thus far, some Congress members have tried to fix the zones through additional regulations; but those attempts have failed and likely would not have worked anyway. Moreover, making any fixes to the current QOZ program have become moot and will not be effective this far into the program’s existence; the QOZ incentive is set to expire on December 31, 2026. However, new legislation is making its way to


133 Layser, Subsidizing Gentrification, supra note 30, at 219.
134 Hodge, supra note 23.
135 Haydar Kurban et al., supra note 105, at 162–64, 169 (examining the positive relationship between QOZ designation and gentrification in D.C. as a case study before and after the QOZ program).
136 Coyne & Johnson, supra note 10, at 2; Weaver, supra note 39.
137 See Bender, supra note 16, at 15–16.
138 Id. At 12.
139 Prior proposals only sought to increase reporting requirements rather than change the actual structure of the QOZ program or address any other issues at the core of the program. Marie Sapirie, Will Congress Finally Reform Opportunity Zones, FORBES (Apr. 25, 2022, 9:56AM), https://www.forbes.com/sites/taxnotes/2022/04/25/will-congress-finally-reform-opportunity-zones/?sh=1e585a775c4b.
the House floor. The Ways and Means Committee passed a proposal for a new kind of QOZ to address the failures of the original opportunity zones. This Comment’s next section examines these proposals.

IV. PROPOSED CHANGES AND RURAL OPPORTUNITY ZONES

The proposed law appears very similar to the existing QOZ program but features a few exceptions. The proposed rural opportunity zone program still offers the same incentive structure for capital gain tax deferral. It also still requires the same asset structuring and operation requisites for the QOZ funds and QOZ business. For example, QOZs still must hold 90% of their assets in QOZ property. But the new proposal adds rural QOZs, expands reporting requirements for the funds, and requires public reporting from the U.S. Department of the Treasury (“The Treasury”). While the House Committee believes these changes will improve and address the failures of the existing QOZs, its beliefs are misplaced.

The proposal would eliminate urban QOZs altogether. Instead of QOZs, the program would only include Qualified Rural Opportunity Zones (“QROZs”) and cover tracts in rural counties. For purposes of a QROZs, rural counties are those that are made up of more than 50% rural census blocks. The proposal would also auto-designate census tracts that are in persistent poverty, rather than give State leaders the discretion to choose their tracts, thus eliminating some of the potential

142. Id. at 1.
143. See discussion infra Part IV.
144. H.R. REP. No. 118-128, at 35.
145. Id. at 80–84.
146. Id. at 81.
148. H.R. REP. No. 118-128, at 34.
149. See id. at 34–35.
150. Id.
151. Id. at 35.
for governmental corruption seen in the original QOZ projects. As determined in May, 2023, this is roughly 341 counties and 6.1% of the U.S. population. To determine whether people are in high poverty, the U.S. Census Bureau compares annual income varied by family size, number of children, and age of the householder. More importantly, it excludes students living in college dormitories and people living in institutional group quarters, like nursing homes.

Another proposed addition to the QROZ program is an increase in reporting requirements. The proposal goes beyond what is required in the current law while also imposing harsher penalties for non-compliance. New reporting requirements of the QROZ program include: (1) the tract information; (2) the number of residential units held, if any; (3) the average monthly number of full-time employees of a QOZ/QROZ business or partnership; (4) whether property held by a QOZ/QROZ is owned or leased; and (5) the North American Industry

152. Tracts are designated as being in ‘persistent poverty’ according to the Bureau of the Census in their May 2023 report “Persistent Poverty in Counties and Census Tracts.” H.R. Rep. No. 118-128, at 35; see discussion supra Part III.B.1.

153. Craig Benson et al., U.S. Census Bureau, Persistent Poverty in Counties and Census Tracts 1 (2023).

154. Id. at 1.

155. Id. at 2.

156. Id. Student dormitories and nursing homes often house people that have very low incomes. When included in a poverty measurement, they significantly skew actual poverty levels in their areas to seem higher than it should be because they are not representative of the typical person in poverty living in an economically distressed area. See Coyne & Johnson, supra note 10, at 11.

157. Compare H.R. Rep. No. 118-128, at 38–39 (imposing penalties for non-compliance with reporting at $500 per day with a maximum penalty of $10,000 for one return which is increased to $50,000 for larger QOZ funds; a penalty of $2,500 per day for intentional disregard of reporting requirements with a maximum penalty of $50,000 for one return which is increased to $250,000 for larger QOZ funds; and a penalty for failing to provide certain disclosures to required parties at $250 for each disclosure up to a maximum penalty of $3,000,000), with Tax Cut and Jobs Act, Pub. L. No.115-97, 131 Stat. 2054, 2183–88 (codified at 26 U.S.C. §§ 1400Z-1–1400Z-2) (imposing penalties only for each month a QOZ fund does not have 90% of its assets invested in QOZ property).

158. Tract information includes the population census tract identification and the geographical area. H.R. Rep. No. 118-128, at 36.
Classification System ("NAICS") Code\textsuperscript{159} that applies to the trade or business.\textsuperscript{160} Failure to comply with the reporting requirements is subject to a maximum penalty of $50,000 or $250,000 for large funds.\textsuperscript{161}

Furthermore, the Treasury is required to issue an annual report to disclose: (1) the size and number of QOZ funds; (2) the total investment per census tract; (3) the total investment amount per NAICS code; (4) employment data; and (5) the number of residential housing units per census tract.\textsuperscript{162} In the sixth and eleventh year, both rural and the original QOZ funds must publish reports demonstrating their impact on various economic factors such as "job creation, poverty reduction, new business starts, and other metrics."\textsuperscript{163} These annual and quinquennial\textsuperscript{164} reports will increase transparency and accountability of QOZ programs and help ensure that it is working as intended.\textsuperscript{165} It will also allow the public to use the data to determine which investments have more of an effective impact.

The Committee also believes these changes will address the existing QOZ's bias towards areas that are rapidly becoming gentrified by focusing on largely neglected communities.\textsuperscript{166} By automatically designating rural census tracts that are in persistent poverty, the QROZ program both eliminates the discretion by State leaders which has been subject to abuse, and allows the areas that were typically not invested in, nor as attractive as the West Coast and East Coast QOZs, to benefit from the incentive.\textsuperscript{167} Additionally, by increasing reporting requirements, the


\textsuperscript{160} H.R. REP. NO. 118-128, at 36–37.

\textsuperscript{161} Large funds are those with over $10 million in assets. H.R. REP. NO. 118-128, at 38.

\textsuperscript{162} Id. at 39–40.

\textsuperscript{163} Id. at 40–41.


\textsuperscript{165} H.R. REP. NO. 118-128, at 34.

\textsuperscript{166} Id.

\textsuperscript{167} Id. at 35; See Coyne & Johnson, supra note 10, at 18.
impact of the QROZs will be much more easily observable and have the potential to uncover exactly what kind of investment works, if any.168 Nevertheless, these changes do not go far enough to fix the program, nor realize the full potential of a QOZ type program.169

V. RURAL OPPORTUNITY ZONES: A MISGUIDED SOLUTION

While some of the provisions of the new QROZ program will help make the existing program better, it will still likely not work as intended overall. This Comment proposes four reasons this new QROZ program will not work. First, the wealthy will continue to benefit the way they have without a fair trade-off to the communities the legislation is intended to benefit. Second, any structure to incentivize investments that have little to no return is non-existent. Third, the auto designating will not solve the issue the current committee believes it to. And fourth, the additional reporting measures do not remedy accountability nor allow effective analyzing.

A. There Is No Assurance that Communities Will Get the Investment They Need

First, the new proposal lacks any measures that ensure that distressed communities get the resources that will actually benefit them. These zones still have the same provision scheme that fails to dictate what kind of projects should be funded by investments.170 Simply restricting eligible zones solely to rural tracts does not by itself spur investment that benefits the community. In the QOZ incentive, the strong economic goal of any player that enters the market still exists—maximizing return on investment.171 The most attractive projects, those

168. See H.R. REP. NO. 118-128, at 34.
169. See infra Part V.
171. Investors’ main goal is to maximize their own profit; only recently has an interest in environmental, social, and governance issues impacted investing. However, it still looked at through the lens of superior performance. See, e.g., Francesco Cesarone et al., Does ESG Impact Really Enhance Portfolio Profitability?, 14 SUSTAINABILITY 2050 (2022). Even financial guru Warren Buffett stated that he is more inclined to prioritize returns over social causes based on shareholder needs. Simon Moore, Buffett Shares His Unconventional Views on ESG Investing, FORBES
easiest to finance, will be undertaken first, just as luxury hotels and apartments were for the original QOZ program.\textsuperscript{172} Without any limitations or more specific regulations on the types of projects to be invested in, the most attractive ones will always come first.\textsuperscript{173}

Additionally, QROZ projects require no input from actual community members. Every community is uniquely different and without hearing what the needs of a particular community are, any investment or large project undertaken can easily be less effective or even worse, unwanted.\textsuperscript{174} In the worst outcome, the project further gentrifies a community and displaces the residents, forcing them to rebuild their entire community in another city or town.\textsuperscript{175} This kind of disruptive outcome will not be adequately remedied by shifting opportunity zones to rural census tracts that are in persistent poverty. Building a hotel in an economically distressed community may bring some profit, temporary jobs, and tourism to the community, but if a distressed community needs a community center or better public infrastructure, the new hotel will not truly benefit the residents of that community.\textsuperscript{176} Lack of community involvement has been a long-standing criticism of a majority of the place-based tax incentives, yet proposals to fix the current QOZ program and the new QROZ program fail to address it.\textsuperscript{177}

\textsuperscript{172} Layser, \textit{Place-Based Tax Incentives}, supra note 8, at 54–55.

\textsuperscript{173} Fund managers additionally owe a legal duty to their investors to act in the best interest to their clients, which means maximizing profits, not maximizing social impact. Bender, \textit{supra} note 16, at 12.

\textsuperscript{174} \textit{Id.} at 11–12; Weaver, \textit{supra} note 39.

\textsuperscript{175} See, e.g., Layser, \textit{Subsidizing Gentrification}, \textit{supra} note 30, at 215–16.


\textsuperscript{177} See, e.g., BRETT THEODOS, URB. INST., \textit{A Tailored Opportunity Zone Incentive Could Bring Greater Benefits to Distressed Communities and Less Cost to the Federal Government: Can Opportunity Zones Address Concerns in the Small Business Economy?} 3–4 (2019) (arguing that without community input, there is no alignment with local goals and projects do not help the community; rather, they harm the community because residents are displaced, and small businesses are put out of business).
B. There Is No Incentive Structure

Second, the incentive to invest in projects that are proven to help these communities, or that are more tailored to address the needs of the residents, are absent in this new legislation. For example, some of these communities desperately need better infrastructure, such as public transportation, streetlights, or a cleaner water supply; however, the government is unable to deliver or is significantly behind schedule on providing these necessities. Additionally, there is an urgent need for affordable and habitable housing in these areas. Without an incentive structure that effectively promotes investments proven to help these communities, QROZ funds will continue to invest in projects that yield maximum returns, which generally does not align with the community’s best interest. Furthermore, only investing in rural communities will not fix the domination of investments in the high-return sectors, such as condominiums and hotels. In order to actually disperse the investments to business and infrastructure, something more must be done. Tax incentives typically come at a high cost, and the government would be throwing this money away if it does not properly incentivize investors to address the needs of these communities.


181. U.S. Gov’t Accountability Off., GAO-21-30, Opportunity Zones: Improved Oversight Needed to Evaluate Tax Expenditure Performance 10 (2020). When the government creates a tax incentive, its lost revenue becomes a significant part of the overall cost of the program; for instance, the QOZ program was estimated to cost the government $3.6 billion in lost revenue for 2020. Id.
C. Communities In Need Will Still Be Left Behind

Third, auto-designating rural counties in poverty will leave many economically distressed and high-poverty communities, both urban and rural, underserved. With the new QROZ program, the number of designated tracts is 1,926.182 Two-thirds of these new tracts were not designated as QOZs under the original program.183 While auto-designating effectively cuts out the extreme—and arguably the most—manipulated areas of the QOZ program, allowing zero discretion will still not adequately select the most disadvantaged communities for the program.184 It also excludes the urban population left out in the original QOZ program.185 Although rural communities were largely overlooked by the QOZ program at higher rates than deeply distressed urban QOZs,186 that does not mean these urban communities should be excluded. There are deeply distressed urban QOZs that were left impoverished and un-invested in, while their adjacent gentrified neighborhoods received an influx of investments.187

On the other hand, the use of a persistent poverty calculation over thirty years rather than using median incomes from a single five-year estimate will greatly help concentrate on communities that are distressed. The use of median income in the original QOZ program included college students as low-income and allowed lagged statistics to be the determining factor for QOZ eligibility, which failed to capture the gentrification of an area.188 This improperly characterized many tracts as eligible; but this is remedied by the persistent poverty calculation employed in QROZs. Further, narrowing QROZ eligibility to tract

183. Id.
184. Id.
185. Many distressed urban communities saw their better-off neighbors receive the QOZ investment, while they received no investment in their own communities. Drucker & Lipton, supra note 176.
186. See Coyne & Johnson, supra note 10, at 19 (showing that the share of designated tracts per state that are urban are almost all over 50% and many states are over 90%).
187. See Drucker & Lipton, supra note 176.
188. Lee, supra note 70, at 145–46.
level instead of county level allows for even more precise targeting. Before this report, legislation targeted poverty at the county level, yet over 74% of persistent poverty tracts were not located in counties experiencing persistent poverty. This difference shows that prior methods used to determine which areas received this designation for both the QOZ program and the NMTC program, excluded a significant number of communities and people. Additionally, the use of the persistent poverty calculation would help some of the most underprivileged areas in the U.S.—those with lower life expectancy rates, higher housing vacancy rates, and higher unemployment rates among those most able to work. Overall, the use of a persistent poverty calculation at the tract level is an improvement, but will ultimately cut out communities that also need benefits.

D. The Reporting Requirements Will Not Help Adequately Analyze QOZs Impact

Fourth, the reporting requirements laid out in the new proposal are not sufficiently tailored to ensure the QOZ program will work as intended. The new reporting requirements for the Treasury and QOZ funds do not collect all necessary data points to adequately determine what kind of investments work most effectively in opportunity zones. The QROZ reporting metrics will only determine the effectiveness of investments regarding economic factors, such as employment, rather than also focusing on the social issues that the program aims to improve. For instance, there are additional reporting requirements for the number of average monthly full-time equivalent employees and businesses in QOZs must report their NAICS code for their industry. Although these statistics can help determine whether more jobs are emerging and what sectors are most effectively adding jobs, for a QOZ whose original goal was to increase the health of the community, merely observing increased healthcare facilities in the area is not strong enough of an indicator to conclusively determine that the overall health of a

190. Craig Benson et al., supra note 153, at 1.
191. See generally Lettieri & Fikri, supra note 182.
192. See discussion supra Part IV.
community has actually improved. While these reporting requirements allow easier tracking of some economic factors and give important insight into how the QOZ program is helping combat poverty, without better reporting metrics, these economic statistics will likely become dominant in the narrative of a successful QOZ, ultimately ignoring other crucial social impacts.

In sum, the proposed changes are a good attempt to remedy the issues that haunt the QOZ program—especially the efforts to target communities that need the most investment and the new requirements for detailed reporting to better analyze the impact of QOZs. Nevertheless, there are too many areas where the new QROZs fall short, particularly when it comes to addressing the underlying issues of the original QOZ program. Even with clearer metrics to evaluate QROZs, the QROZ program’s structure remains inadequate to help economically distressed communities.

VI. RURAL OPPORTUNITY ZONES CAN BE FIXED

To address the issues in the QROZ and QOZ programs, the legislature should introduce new legislation to make the program more effective. This Comment proposes multiple solutions that address the multifaceted shortcomings of the QOZ program and other place-based tax incentives. These proposals can work in tandem or alone.

A. Adding an Tiered-Incentivize Structure to QOZs

To address the criticisms of the flood of investments into luxury real estate and real estate generally, the QOZ program should adopt something similar to the original proposal by the Economic Innovation Group. This original proposal included a tiered incentive structure for investors that brought more “generosity” to the community such as infrastructure—the higher the generosity, the higher the tax benefit to

193. See generally, e.g., Community Health Assessment & Health Improvement Planning: Assessment & Planning Models, Frameworks & Tools, CTRS. DISEASE CONTROL & PREVENTION, https://www.cdc.gov/publichealthgateway/cha/assessment.html (last visited Nov. 26, 2023) (examining the numerous methods and tools to evaluate the health of a community). This is just one example of the complexity of measuring the “success” of a sector.

194. See, e.g., Coyne & Johnson, supra note 10.
the investors would be. If a tiered incentive structure is adopted to give 100% excludable capital gain treatment to less attractive, but more impactful projects, such as public infrastructure, investments will begin to shift into those critical sectors. Other, more attractive projects like affordable housing could receive a max excludable capital gain treatment of roughly 80%, while even more attractive investments could receive a max excludable capital gain treatment of roughly 60%.

A tiered structure must still offer a strong enough incentive to encourage the wealthy to invest in these zones. The entire objective of the QOZs is to mobilize unrealized gains that millionaires and billionaires have sitting in their investment accounts, untouched and untaxed. If these wealthy individuals leave their investment accounts alone until they pass away, the accounts will likely be bequeathed to their heirs. Upon bequeathment, the heirs receive a step-up in the property’s basis to its fair market value on the date of the original investor’s death. This means that if a child inherits stock from a parent, the child could sell it the next day with little to no tax consequences. This is because the basis would be almost the same as the price at which the stock is sold. This is a great alternative to the QOZs for passing tax-free wealth to the next generation—accordingly, to stay attractive, the QOZ program must offer a strong enough incentive for investors.

Furthermore, the only limitation guarding against the step-up in basis on bequeathed property is the lifetime estate tax. Typically, when someone dies, their estate, or net worth, is valued to determine their taxable estate, or how much of their money and assets can be taxed, accordingly, to stay attractive, the QOZ program must offer a strong enough incentive for investors.

195. Bernstein & Hassett, supra note 40, at 18. For instance, an investor who funds a QOZ project that provides clean water to a community could receive 100% taxable gain exclusion while an investor who funds a new hotel could receive less than 100%.

196. See discussion supra Part II.B.

197. See Mary Whitfill Roeloffs, New Billionaires Inherited More Than They Earned Last Year, UBS Report Says, FORBES (Nov. 30, 2023, 12:08PM), https://www.forbes.com/sites/maryroeloffs/2023/11/30/new-billionaires-inherited-more-than-they-earned-last-year-ubs-report-says/?sh=75a71e013d68 (discussing surveys that show many people who inherit wealth are more likely to keep it as intergenerational wealth rather than giving it away).

198. I.R.C. §§ 1014(a)–(b).

199. This assumes the stock price of the stock remained relatively stable from day to day.
for State and federal income tax returns purposes. Under current regulations, an individual is able pass almost $14 million tax-free to their heirs; if an estate exceeds $14 million, the excess is generally taxed at the maximum rate of 40%. Additionally, individuals may take advantage of this exemption while they are alive through various estate planning methods. For example, by giving gifts during their lifetime, an individual can use the exemption applicable in the year the gift is made. Take an individual who wants to take advantage of the $14 million lifetime exclusion, if she waits to gift her $10 million house on her death to her son, she runs the risk that the value of their home will be over the maximum exemption amount on her death. Instead, she can gift the house to her son today and elect to have the $10 million house be counted against the $14 million exemption. This allows a significant amount of wealth to pass directly to the heirs of wealthy individuals with minor tax consequences. Therefore, to compete with these tax-free wealth transfer methods, the QOZ incentive structure must offer an enticing tax benefit for affluent investors to encourage participation in this program. The 100% excludable gain offered by the QOZ program is an effective incentive to do so; however, without clear guidelines dictating how money should be spent within the QOZ program, there is no benefit to anyone but the wealthy investors.

B. Expanding Access to QOZs

Additionally, by expanding access to include investors beyond accredited investors or the uber-wealthy, more capital can be infused into the QOZ program, thus enabling middle-income families to bridge their own wealth gap. Rather than solely benefitting the wealthy, the

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203. Id.
new rural QOZ program could democratize this complex investment structure, allowing the middle-class to partake in gains typically reserved for the ultra-wealthy. Since middle-class families lack the abundant capital gains of their wealthier counterparts, they could receive preferential tax treatment akin to a Roth Individual Retirement Account. Their contribution will be invested in a QOZ, yielding tax-free appreciation exclusive to middle-class families below a specified AGI; however, there should be a phase out based on AGI up to the cap. This AGI cap would be set at the top of the middle-income range of $156,000 and adjusted annually for inflation, which ensures larger tax breaks for lower-income investors, thus allowing them to save more compared to wealthier investors.

Alternatively, middle and low-income families could benefit from a direct, one-time charitable deduction against their AGI for an investment in a QOZ. This would be subject to a similar phase-out scheme for families with an AGI below $156,000, guaranteeing broader eligibility. Unlike current provisions, the deduction would not be limited to those who itemize on their individual income tax returns. Furthermore, these deductions would be claimable up to the date the income tax returns are filed, rather than year-end. While this approach might

204. BERNSTEIN & HASSETT, supra note 40, at 18. A Roth Individual Retirement Account allows individuals to contribute post-tax dollars into a retirement account, and after they reach the age of 59½, they can withdraw money tax-free, including the appreciation. I.R.C. § 408A.


206. Individuals can only take itemized deductions such as charitable contributions, medical expenses, property tax, and mortgage interest, against their income if those deductions, subject to certain limitations, are greater than the standard deduction, which for married persons, in 2022, is $25,900. U.S. DEP’T TREASURY, INSTRUCTIONS FOR FORM 1040 (AND 1040-SR) 6, 31 (2022); U.S. DEP’T TREASURY, INSTRUCTIONS FOR SCHEDULE A (2022). Typically, itemizing deductions is reserved for the wealthy—only 11.4% of individual income tax returns claimed itemized deductions in 2018. SOI Tax Stats—Tax Stats-at-a-Glance, IRS, https://www.irs.gov/statistics/soi-tax-stats-tax-stats-at-a-glance (last visited Nov. 26, 2023).

207. Using an April 15th funding deadline versus the applicable year-end, similar to a Roth Individual Retirement Account, will allow families who are unaware of the tax benefit to be able to participate. This will help low-income families who do not engage in, nor can afford to do, year-end planning.
generate a smaller amount of capital investment, it enables middle and low-income families to access the benefits of the QOZ program.

Additionally, there should be a restriction against QOZ funds requiring accredited investor status to help expand access to a broader range of investors not currently participating in the QOZ program. Banning this pseudo-requirement, will enable more people to be able to invest in the QOZ program who otherwise are unable to.

C. Allowing Certain QOZ Funds to be Feeder Funds

As introduced in a different legislative attempt to expand QOZs, allowing certain QOZ funds to be feeder funds will help fund more projects and expand access to preferential tax treatment. A feeder fund, or a fund of funds, is a partnership that pools together smaller investments to invest in a much larger, master fund. This structure allows investors to participate in QOZ funds indirectly through a feeder fund, which invests in larger QOZ funds. This arrangement may reduce transaction and operational costs for smaller QOZ funds, enabling a wider range of investors to participate without needing to commit significant capital.

Feeder funds have been subject to abuse; and, accordingly, there should be strict limitations on these funds. In line with a previous QOZ proposal, these funds should be required to hold 95% of assets in QOZs and operate as a domestic partnership. Going further, the legislation should cap feeder funds to total assets below the average QOZ fund size of $6 million and limit management fees to approximately 0.5% of total

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208. S. 4065, 117th Cong. § 302(b) (2022); H.R. 7467, 117th Cong. § 302(b) (2022).
210. Id.
211. The most famous example of feeder fund abuse is Bernie Madoff’s pyramid scheme that used feeder funds to fraud investors while paying Bernie millions of dollars in management fees. See Felicia Smith, Madoff Ponzi Scheme Exposes “The Myth of the Sophisticated Investor”, 40 U. BALTIMORE L. REV. 217, 237 (2010).
212. S. 4065; H.R. 7467. Domestic partnerships are those that are registered in the U.S and must comply with federal and state law and filing requirements. I.R.C. § 7701(a)(4).
Without these limitations, fund managers, who are typically paid a percentage of the total commitments that investors promise to invest in the fund, will be incentivized to create unnecessary feeder funds.

D. Requiring Community Involvement in QOZs

Incorporating community involvement in QOZ projects is essential. This has been a longstanding criticism of place-based incentives, yet new programs have not mandated it on any level. Without a more tailored approach, QOZ investments may fail to benefit their communities. While there are many logistical and bureaucratic challenges to gathering community input, the community’s local elected officials, who are familiar with a community’s unique needs, could represent its interests, helping to streamline the process. This can facilitate collecting community input from various members. Since community needs vary greatly—from clean water to healthcare access—involving elected representatives in QOZ projects could ensure that these diverse needs are addressed and prevent a one-size-fits-all approach to community development. Connecting the elected representatives to the QOZ project process can help remedy this issue. For instance, the community official could be required to sign-off on all QOZ projects within his community. With this paper trail, the community official would be held accountable by his constituents for the approved projects.

Nonetheless, concerns of manipulation by elected officials loom, as demonstrated previously by state governors’ exploitation of QOZ programs. To help deter this bad behavior, elected officials should be required to create a list of community needs before funds receive investments. Each QOZ fund must also disclose how it will meet those specific needs. However, the legislation must avoid overly-stringent standards or high penalties for noncompliance, as these might diminish the attractiveness of and discourage investing in the QOZ programs. Making the QOZ program too hard to comply with would make the

213. Typically, fund managers are paid anywhere up to 2% of the total commitments by the investors to the fund or the total value of the assets they are managing. James Chen, What Is a Management Fee? Definition, Average Cost, and Example, INVESTOPEDIA (Sept. 23, 2023), https://www.investopedia.com/terms/m/managementfee.asp.

214. See discussion supra Part III.B.
investment riskier, especially if rural tracts are the only eligible zones. Rural areas in particular are naturally less attractive for investments than urban zones, adding excessive restrictions could further dampen interest in QROZs, thereby hindering the program’s effectiveness in driving real change. 215

E. Increasing Reporting Requirements of QOZs

The current proposal is a reasonable attempt to hold QOZs accountable and increase transparency into what investments are being made; however, as noted in Part V, the reporting requirements should extend beyond purely economic aspects to include social issues. But levying stricter, more detailed reporting requirements onto the QOZ program is a balancing act. On the one hand, data needs to be collected so that it may be analyzed to determine exactly what kind of investments are most impactful and can inform the government and other entities on how to maximize the efficiency of money going forward. This is extremely beneficial to helping these kinds of communities. Yet, increasing reporting requirements raises the management costs of these projects in order to comply, likely diminishing their returns on investment. With less overall returns, this makes investors more likely to invest money elsewhere.

Instead of adding various factors and miscellaneous statistics to track, QOZs should be required to disclose the goal of their projects in their annual tax returns. This goal could even be categorized using a system similar to NAICS codes. Pre-determined categories would include goals such as affordable housing, education, or pollution-control. These categories would facilitate a clearer assessment of the degree of impact a specific QOZ project is having on its community. The Treasury could also easily include this data in their annual reports, and the private and public sectors could more easily research and evaluate the impact of QOZs in their intended area.

215. Rural zones are less attractive than urban zones because of the missed profit and potential for appreciation that is so prevalent in urban areas. Consider the Las Vegas example discussed in note 94, supra. Investing in a hotel casino in a central location near the Las Vegas Strip will bring in much more income and potential gains than investing in affordable housing in the city of Wells, Nevada whose town is more of a truck stop than a destination.
CONCLUSION

Almost thirty-eight million Americans live in poverty, while just six of the richest people in America are worth more than thirteen of the U.S.’s poorest states combined. It is difficult to see why the government has not encouraged more wealth to shift effectively to help economically distressed people and communities. Place-based incentives are a powerful tool which, if used correctly, can help elevate an entire community. They can improve health outcomes, enhance productivity, and catalyze financial autonomy within a community. This approach underscores the importance of targeted, effective policies in addressing socioeconomic disparities.

Despite the flaws in the current QOZ program and the proposed QROZ program, with appropriate adjustments, these initiatives can effectively support distressed communities. Legislators need to structure the program with firm regulations and safeguards to ensure that it will serve its intended purpose. The new program must include intentionally-structured incentives and precise reporting requirements to prevent the abuses observed in the original QOZ program. Without a well-considered structure, investors might exploit the program for personal gain, while simultaneously ignoring the needs of the communities meant to benefit from the program. Without robust regulations, the new version of the program will continue to fail and the drastic inequality gap between the uber-wealthy and the poor will only widen.

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218. See discussion supra Part III.B.

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