Missed Opportunity: The West Baltimore Opportunity Zones Story

Michael Snidal
Columbia University, Graduate School of Architecture, Planning, and Preservation

Sandra Newman
Johns Hopkins University Bloomberg School of Public Health

Abstract

This paper presents a qualitative evaluation of how Opportunity Zones (OZs) have attracted capital and economic development to highly distressed neighborhoods in West Baltimore. Based on 76 interviews with community and government officials, program managers, developers, businesses, and fund managers, we assess the strengths and weaknesses of OZs in West Baltimore and Baltimore City. We find that OZs are stimulating new investment conversations and building local economic development capacity. However, we also find OZs fail at oversight and community engagement, do not spur new development, and are a missed opportunity to incentivize actors and institutions critical to revitalizing distressed neighborhoods. To spur development in distressed neighborhoods, OZs require reporting standards, the removal of non-distressed census tracts, dollars for education and infrastructure, the incorporation of Community Development Financial Institutions, and incentives for non-capital gains holding investors.

Introduction

The stated goal of Opportunity Zones (OZs) is to bring economic development to distressed communities.[1] Broad selection criteria, flexible development guidelines, and lack of reporting requirements, however, have provoked concern that OZs may fail to spur investment in truly distressed neighborhoods (Gelfond and Looney, 2018; Theodos, Meixell, and Hedman, 2018).

This report presents the findings from 76 interviews with community and government officials, program managers, developers, businesses, and fund managers regarding OZ investments in the West Baltimore OZ Cluster, a grouping of 11 highly disadvantaged census tracts representing over

[1] On the goal of Opportunity Zones, see the published transcript of "The Promise of Opportunity Zones," Senate Hearing 115-297 before the Joint Economic Committee.

40,000 residents. These interviews were used to assess how OZs are supporting specific real estate and business investment projects in distressed neighborhoods.

We find that OZs are a missed opportunity. OZs are stimulating investment conversations and local government capacity; however, they are failing at oversight and community engagement, and they are not changing development outcomes. Participant interviews reveal a locality doing its best with a tax policy poorly designed to stimulate development in distressed communities. OZs are failing West Baltimore because they are a weak incentive for capital gains investors who want market-rate returns, because they do not sufficiently support investors and developers already active in distressed neighborhoods, and because of several related design flaws.

In the next section, we review previous evaluations of tax preferences for place-based development. In the methodology, we discuss the case study area, the case study strategy, and the interview and data collection process. We then summarize Baltimore OZ investments and describe the major findings from our participant interviews. We end with seven recommendations to improve OZ policy for distressed neighborhoods.

Evaluations of Tax Preferences for Place-Based Development

This is one of the first evaluations of OZ outcomes.[2] Tax incentives to attract mobile capital to distressed communities, however, have been advanced by all levels of government for over half a century. By the 1980s, most states had implemented Enterprise Zones (EZs), offering tax incentives and employment credits for investment and job creation in distressed areas. In 1993, the federal government established the Empowerment Zones program: a combination of tax credits, grants, bonding authority, and other benefits eligible in distressed urban and rural communities. These programs are the direct predecessors to OZs. Assessments of their outcomes are inconsistent and inconclusive.

Econometric studies of these programs have generally found nominal net benefits of both state-level EZ programs and the federal Empowerment Zones program. For example, Boarnet and Bogart (1996) found that EZ designation had no significant effect on employment or property values in New Jersey; Engberg and Greenbaum (1999) found that EZ designation had no effect on housing prices across 22 states; and the Government Accountability Office (GAO) (1988) found that EZs had little or no effect on job creation in Maryland. In the most exhaustive study, Peters and Fisher (2002) found that EZs in 13 states had little effect on economic growth. Positive effects that are documented tend to be found in less distressed areas.

In contrast, Papke (1994) found that EZ designation in Indiana resulted in an 8-percent increase in company inventory value; Greenbaum and Engberg (2004) reported that EZ programs across six states led to increased business development; and O'Keefe (2004) concluded that California's EZ raised employment by 3 percent over 6 years. Rubin's (1990) analysis, the most prominent work supporting EZs, found that 30 percent of the 500 companies she surveyed said the New Jersey EZ had affected company location and expansion decisions.

[2] Early studies of OZ outcomes nationally include Atkins et al. (2021); Chen, Glaeser, and Wessel (2019); and Theodos et al. (2020).

Fewer studies have examined the federal Empowerment Zones program. The Government Accountability Office (GAO) conducted two studies in 2006 and 2010 but failed to reach a conclusion due to poor data collection. Oakley and Tsao (2006) found limited evidence of improvements in certain Empowerment Zones compared to counterfactual sites—for example, poverty reduction in Detroit—but overall, they determined that the zones had little impact. Busso, Gregory, and Kline (2013) found greater impacts. According to their study, neighborhoods receiving Empowerment Zone designation experienced a 12–21 percent increase in total employment and an 8–13 percent increase in weekly wages compared to matched zones, and these gains came with only modest deadweight losses. They found, however, that the program had a nominal effect on rents and vacancy rates. Krupka and Noonan (2009) found that the federal program had a statistically significant and substantially positive effect on housing prices but varying and less impact on indicators of neighborhood quality.

These studies represent a mixture of shift-share and regression analysis, including sophisticated quasi-experimental designs. All recommend early and periodic performance assessments and monitoring of zones to help improve understanding of outcomes. We take this recommendation by reporting our early assessment of OZ policy in West Baltimore. Our qualitative approach sets the context for applying OZs to distressed neighborhoods and provides nuance on how and why the policy is and isn't changing development outcomes.[3]

Methodology

Our case study area is the West Baltimore Opportunity Zones Cluster (WBOZC) which we provide descriptive statistics for in exhibit 1. We selected the WBOZC for four reasons. First, the WBOZC represents 15 highly distressed census tracts representing roughly 44,000 residents that serve as a "black swan" for analysis; if findings indicate OZ policy attracted substantial capital, this may indicate that OZ neighborhoods with less distress could also attract equity. On the other hand, if we find negligible effects, we can explore why OZs are not serving neighborhoods most in need of investment. Second, Michael Snidal has a deep network and detailed knowledge of economic and community development experts and projects in West Baltimore. Third, both the City of Baltimore and the State of Maryland, unlike most jurisdictions, established staff positions to work specifically on OZs. These staff members could help identify capital flows and economic development activity in lieu of federal reporting mandates. Finally, Baltimore's proximity to Washington, D.C., allowed the first author to meet with economic development experts knowledgeable about Baltimore and national OZ activity.

[3] A comprehensive analysis of all peer-reviewed studies of state enterprise zones and the federal Empowerment Zone program is available from the first author upon request.

Exhibit 1

West Baltimore OZs Cluster Descriptive Statistics

Geography (# of census tracts)	Med Income ($)	Med House Price ($)	Med Rent ($)	Poverty Rate (%)	Unemployed (%)	College Educated or Greater (%)	Average Investment Score (1–10)*
West Baltimore OZs Cluster (15)	24,549	87,000	955	38	18	12	3.2
Baltimore OZs Cluster (42)	32,785	110,200	943	33	16	17	4.4
Baltimore (183)	42,094	134,800	961	24	13	25	4.2
Maryland OZs Cluster(149)	46,856	173,400	1,063	21	10	24	5.4
Maryland (743)	74,551	290,400	1,156	10	7	37	5.5
USA OZs Cluster (8,763)	33,345	108,000	725	31	12	18	5.3
USA (67,148)	53,657	178,600	953	15	5.8	29	5.5

OZs = Opportunity Zones.

**The Investment Score is the average score assigned to each census tract by the Urban Institute (UI) to capture lending activity before the introduction of OZs. UI established this investment score by census tract, ranging from 1–10, through a composite index which incorporates commercial lending, multifamily lending, single family lending, and small business lending data from American Community Survey (ACS), CoreLogic, Home Mortgage Disclosure Act, and Community Reinvestment Act data. Their full methodology can be found online: https://www.urban.org/policy-centers/metropolitan-housing-and-communities-policy-center/projects/opportunity-zones-maximizing-return-public-investment.*

Note: The West Baltimore OZs Cluster contains approximately 44,000 residents, and the City of Baltimore OZs contain approximately 120,000 residents, roughly 7 percent and 19 percent of Baltimore's population, respectively.

Source: Housing, poverty, employment, and education statistics are derived from ACS 2011–15 data

At the inception of the research, the first author developed an original 35-person participant list based on his knowledge and network of economic development experts. He then held initial meetings with the city council members representing the WBOZC and the City of Baltimore's designated OZ coordinator. Both authors also systematically reviewed OZ documents including enabling legislation, congressional testimony, articles and press releases by government, think tanks, advocacy groups, and local and national media. We emphasized actors and institutions engaged in business or project development in and around the WBOZC. Interviewees included developers, project sponsors, fund managers, wealth managers, investors, philanthropies, nonprofit agencies, community development institutions, city and state-level officials, and businesses. The interview list was expanded to 76 people using a snowball sampling method, a non-probability method of convenience in which the interviewing author asked each interviewee for recommendations for, and connections to, other experts at the end of each interview. A typology of the study participants is provided in exhibit 2.

Exhibit 2

Participant Typology for West Baltimore OZs Evaluation

Participant Identification	Number of Interviews
Government Agency	7
Elected Official	6
Banking/Fund Manager/Business	18
Developer/Small Developer	16
Nonprofit/Community Developer	15
Think Tank/Consultant/Philanthropic	14
TOTAL	76

OZs = Opportunity Zones.
Source: Michael Snidal

Interviews were open-ended and semi-structured. The first author explained the purpose of the study and described the participant identification process at the opening of each meeting. He asked selected questions from a list created by the authors. Not all interviewees were asked all questions because questions were tailored in advance of each interview. Frequently, interviews moved away from a question-by-question format and into dialogue and conversation across questions or topics. The first author was intentional, however, in balancing depth spent on each question with breadth of questions during each interview. Interviews were not recorded, but the first author took extensive notes during and after each interview, including capturing direct quotes.

Interviews started in October 2019 and ended in December 2020. Most interviews were conducted in person through February 2020 at offices, restaurants, coffee shops, and other locations across Baltimore, New York City, and Washington, D.C. In response to the advent of the COVID-19 pandemic in March 2020, we paused the study from mid-March to August 2020. We then conducted interviews in an online format. To clarify unclear responses, we followed up with 29 participants by email, phone call, or meeting.[4] We also requested OZ documentation from some participants, such as project-level financial projections, if the documentation would assist our analysis.

Project development details and investment estimates come from participant interviews, media reporting, and the first author's knowledge of Baltimore development. In cases where we do not footnote public reporting, development information and project finance estimates come exclusively from participant interviews and not objective records. Each financing estimate was checked for accuracy with at least three participant sources. Despite our best efforts, we cannot guarantee the accuracy of these numbers or whether we captured all OZ activity. We likely missed investors, developers, and businesses who considered, but ultimately abandoned, OZ capital.

Results: OZ Investments

Three years after the Tax Cuts and Jobs Act of 2017 (TCJA) was signed into law, no OZ capital had been committed in the WBOZC. However, we documented six OZ investments across the City of Baltimore. We also documented three projects, two within the WBOZC, that are likely to secure OZ financing within the next year. Excluding a $154 million OZ investment made in a $5.5 billion mega-development project at Port Covington, these projects represent $78 million of OZ equity, supporting roughly $468 million in real estate and business development projects across the City of Baltimore.[5] Baltimore OZ investments are documented in exhibit 3.

[4] The first author met with nine participants more than once. This includes multiple meetings with the City of Baltimore's OZ Coordinator.

[5] In Maryland, the comparable numbers are roughly $192 million and $800 million, respectively. Novogradac, a national professional services organization that is tracking Qualified Opportunity Fund (QOF) development, estimates the comparable amount invested across the country (as of the third quarter of 2020) at roughly $12 billion. See Novogradac OZ fund list. The White House Council of Economic Advisors (CEA) contends that this has spurred roughly $75 billion in total development over the same period. However, CEA's estimate includes investments that would have taken place without OZs. See CEA (2020).

Exhibit 3

Baltimore OZ Investments

Project/ Business	Description	OZ Investment ($)	Total Investment ($)	Med Income ($)	Med House Price ($)	Med Rent ($)	Poverty Rate (%)	Unemployed (%)	College Educated or Greater (%)	Investment Score (1–10)*
Yards 56	Mixed use development	30 million	150 million	50,280	124,500	1,061	11	7	17	5
Prosper on Fayette	Workforce housing and hotel	15 million	55 million	55,277	254,000	1,445	27	4	79	9
Galen Robotics	Business expansion	1 million	7 million	46,250	167,500	1,341	27	15	42	7
Penn Station	Amtrak Station redevelopment	10 million	90 million	36,607	219,200	908	30	17	43	6
Outlook Studios	Business expansion	1 million	Unknown	28,109	182,600	906	49	20	12	2
Port Covington	Mixed use mega-development	154 million	5.5 billion	103,667	276,000	1,802	9	6	71	10
North Ave Commercial**	Affordable housing & local business	1.2 million	4.5 million	31,855	122,500	976	33	21	24	2
Madison Park North**	Mixed use development	10 million	100 million	39,470	252,600	959	35	16	34	1
Northwood Plaza**	Mixed use development	10 million	58 million	43,221	150,700	935	20	14	31	6

OZs = Opportunity Zones.

**See exhibit 1 for description and source of "Investment Score." This is the score of each census tract and not an average.*

***Project, in appendix B, is an expected not finalized OZ investment.*

Source: Housing, poverty, employment, and education statistics are derived from American Community Survey, 2011–15 data

Baltimore OZ investments are supporting economic development that benefits city residents at-large, including investments in transit-oriented development and a minority-owned business, the attraction of high-paying technology jobs, and the development of a grocery store and other retail amenities.[6]

Little OZ capital, however, is flowing into deeply distressed neighborhoods. Investments in distressed communities include an estimated $1 million investment for minority-owned business expansion, a $10 million investment in a $100 million mixed-use redevelopment project, and a $1.2 million investment in a $4.5 million affordable housing development. These projects meet the stated intention of OZ policy, but they represent less than 5 percent of total OZ equity deployed or expected to be deployed in Baltimore. In contrast, 65 percent of all OZ capital is flowing into Port Covington, a census tract with a household median income approaching $100 thousand and where a $5.5 billion project was already underway.

We find OZs provide a "gap" equity source that may speed up a project timeline or substitute for other capital sources, but that does not determine the fate of a project or stimulate entirely new development. Direct subsidy programs and federal New Markets Tax Credits (NMTC) are more critical sources of capital to spur development. We observed dedicated government staff, sophisticated developers, and a few mission-driven financiers working to leverage OZs for community development. They illustrate a locality doing its best with a federal tax preference that was poorly designed for distressed neighborhoods. Most importantly, we document how OZ policy is failing to support or incentivize community development entities, community developers, small businesses, nonprofits, and institutions already operating in and around distressed neighborhoods. This is the missed opportunity of OZs.

Results: OZ Strengths and Weaknesses

Based on investment and development activity in the WBOZC and Baltimore City at large, we draw the following conclusions about the strengths and weaknesses of OZs for distressed communities.

OZs are Stimulating a New Set of Investors and Development Conversations

The greatest benefit of OZs is their ability to stimulate new investment conversations and attract new investors. We documented over 50 funds that had connected with individual businesses and projects in Baltimore. OZ coordinators reported as many as 80 projects across the city that were potential candidates for OZ investment. Whereas most of these funds and projects had not deployed or received capital, we found consensus that OZs had led to a new development "ecosystem" with the potential to stimulate economic development. As the city's OZ coordinator summarized: "One of the most important outcomes has been OZ's ability to attract a diverse cadre of new investors to Baltimore city. …these relationships represent new doors for attracting capital and development to Baltimore city."[7] One developer confirmed: "Investors are looking at areas that were previously redlined to development because of their race or ethnicity."[8]

[6] A detailed profile for each project in exhibit 3 can be obtained in a longer format report of these interviews. See Snidal and Newman (2021).

[7] OZ coordinator interviews.

[8] Government agency interviews.

Over the study period, investors and developers toured Baltimore, met with elected officials, attended conferences, and inquired with city and state OZ coordinators and project sponsors. OZ events were local and national in scope. For example, in January 2019, the Jack Kemp Foundation hosted over 200 people in Baltimore to discuss OZ opportunities and challenges. In October 2019, several project sponsors offered tours of OZ sites as part of an annual Baltimore "homecoming" event where successful professionals with links to Baltimore were invited back to the city to discuss how they could invest in its future. In October 2020, the online database "OpportunityDb" hosted a three-part webinar with several Baltimore OZ project sponsors as discussants.[9] Project sponsors also created marketing material for OZ investors. For example, a mid-sized development firm working in the WBOZC presented the first author with a sophisticated offering sheet of the sale of a multimillion-dollar OZ incentivized real estate portfolio. However, participants described this new investor class as primarily interested in market-rate development opportunities. They did not expect this new ecosystem to make large investments in Baltimore's lower-income and African-American neighborhoods like West Baltimore. A housing developer in WBOZC noted, "Sure, there may be new groups of investors that drive through [these neighborhoods] as part of an OZ marketing event. But when push comes to shove, [OZs don't] change their bottom line…they are only going to consider the same five or six neighborhoods that outside investors have always looked at."[10] Likewise, the president of a major regional community development organization noted that "the moment one of these investors sees the [3–5 percent] returns we are offering, the OZ conversation halts…."[11] Three community developers indicated that these conversations were short-lived and created a false sense of hope. The head of a development nonprofit noted, "[We] approach OZ investor connections with caution" because they have "eaten up a lot of [our] time" but failed to materialize.[12]

Small developers working in West Baltimore were generally skeptical of any new ecosystem. A housing rehabilitation firm in the WBOZC suggested that this new ecosystem "works within the existing power structure of development. Our bottom-line concerns social outcomes; outside OZ investors are looking for large financial returns. So, the conversation start[s] and end[s] there."[13] Community Development Entities (CDEs) indicated that the work they were already doing in distressed communities, particularly around affordable housing, was fragmented from this new network. They noted that OZs were not compatible with Low Income Housing Tax Credits (LIHTC) and other debt-led development.[14] We also found that the philanthropic sector was largely uninvolved with OZ policy except for the Abell Foundation funding the City of Baltimore's OZ coordinator position. We discuss OZ's failure to incentivize capital already operating in undercapitalized markets in more detail in the following section.

[9] For webinar see Milbergs (2020).

[10] Developer interviews.

[11] Nonprofit/community developer interviews.

[12] Nonprofit/community developer interviews.

[13] Developer interviews.

[14] Study participants stressed two reasons for this: (1) LIHTC projects are typically debt financed while OZs are an equity incentive and (2) OZs are a 10-year exit (that is, the major benefit accrues at year 10) while LIHTC is a 15-year exit which makes it challenging to time OZ-LIHTC projects.

OZs Are Spurring New Local Government Development Capacity

Related to this new ecosystem, OZs have created a new organizing structure in which the city engages in development. This is primarily the result of city and state OZ coordinators tasked to work with existing local officials to promote development in these zones, connect investors to OZ projects, track OZ activity, and present on OZ opportunities and progress. It is critical to note that these positions were not mandated by the federal government. On the contrary, OZ legislation mandated no requirement or appropriations for local economic development planning. Consequently, this outcome is best understood as an indirect result of Baltimore and Maryland deliberately establishing new positions.

The Baltimore OZ coordinator describes himself as a "matchmaker." This matchmaking, and the database of projects that has flowed from it, is stimulating new and more coordinated conversations within local government about setting priorities, allocating limited local dollars, and identifying resources for projects. OZs, in tandem with a new neighborhood impact investment fund (NIIF), have stimulated "a set of monthly meetings where many of the city's major agency leaders…come together and…go through projects one by one in a way that wasn't as intentional before the incentive." According to leadership at the City of Baltimore's Department of Housing and Community Development (DHCD), "the city now has a point person to connect the dots on investment and development." Another DHCD staff member noted that "the rollout of OZs fit very nicely in the early adaptation of Baltimore's community development strategy."[15]

Increased local government capacity includes the creation of a "development prospectus," a marketing document that the OZ coordinator pitched to developers and investors to tout the city's opportunities, projects, and neighborhoods.[16] It includes an interactive website portal where OZ actors can locate projects, information, and contacts about the state's OZ activity.[17] It also encompasses state legislation that extended existing employment incentives to all businesses that locate or expand within Maryland's OZ footprint.[18] Developer and investor participants frequently mentioned these developments and this new capacity. One developer noted, "the great thing about [OZs] is now we have this reliable point of contact in the city to get this project to completion …." Another development executive said, "Before [OZs], we frequently held off on consulting with the city until we had our sources and uses better lined up. After [OZs], we may be inclined to check in with the city on other opportunities…."[19]

It is noteworthy that eight study participants suggested that OZs may be redirecting government capacity away from non-OZ opportunities and privileging an elite set of investors with access to capital gains dollars. At the same time, city government participants noted that a major challenge of OZs was dealing with inquiries from people without any development experience or plan, or who were not serious investors. A major developer noted, "OZ hype [comes with] a challenge.

[15] Government agency interviews.

[16] See Baltimore Development Corporation (2018).

[17] See Maryland Department of Housing and Community Development (2018).

[18] See Opportunity Zones Incentives, S.B. 581, Regular Session 2019. (2019).

[19] Developer interviews.

Now you also have a bunch of inexperienced people talking about projects without a lick of development expertise…."[20]

Five participants expressed cynicism of OZ policy altogether, describing it as a "distraction," "total waste of time," and even a "con." An executive of a regional community development nonprofit stated, "[OZs are not] the only economic development strategy that needs capacity…. We have other zones and programs… this energy would be better served developing a strategy to win NMTC through a captive CDE."[21] Similarly, two of these participants proposed that OZ efforts be redirected toward developing municipal banking because commercial banks lend a trivial amount of their overall loan percentages to African-American residents and in African-American neighborhoods.[22] A policy expert described OZs as "the latest in a series of steps to redirect local development capacity to outside and powerful holders of capital."[23] Likewise, a program manager at a housing nonprofit commented, "Once again, the government is telling us that the solution to the problem is to compete for the same capital that ignored us in the first place." Thirteen total participants expressed a general concern that OZ's primary purpose is tax relief for the wealthy. The director of a nonprofit described [OZs] as "…[a] new way to reduce taxes for a bunch of people who…already aren't paying their fair share."[24] Even so, most of these participants supported OZ policy with a "nothing to lose" explanation.

OZs Are Failing at Oversight, Community Engagement, and Education

Baltimore and the State of Maryland made good faith efforts to track OZ development. The city held multiple meetings and workshops with neighborhood leaders and community organizations. The OZ coordinator noted that the city was "very intentional with investors…about investing in distressed neighborhoods."[25] City officials selected low-income neighborhoods for OZs, and they were deliberate about trying to establish community benefits agreements and employment targets around the policy. They also guided investors to high-priority projects that would be beneficial for Baltimore's lower-income and minority communities.

Even so, OZs are opaque and undemocratic. It offers no planning mechanisms for communities to prevent harmful investment. Participants repeatedly noted that OZs provided no designated funding to introduce communities to the tax preference or to educate them on how they could identify and connect with investors. Commitments like these, which help build trust with communities, are necessary to stimulate positive development in distressed communities, especially those with long histories of race-based disinvestment and skepticism of outside investors.[26]

The city coordinator referred to OZs as a "marketplace" and not a "program." He acknowledged that "at the end of the day, these are private-sector investors, and we don't control their purse

[20] Developer interviews.

[21] Nonprofit/community developer interviews.

[22] See Vanatta (2019) for the Abell Foundation report on this topic which two study participants referred us to.

[23] Think tank/consultant/philanthropic interviews.

[24] Nonprofit/community developer interviews.

[25] Government agency interviews.

[26] Participant interviews.

strings."[27] A manager of an investment fund described local ability to steer OZ investment as "like being placed in a sea with a paddle. The federal tax code is a pretty blunt mechanism to just throw at localities for economic development," this participant added.[28] The four Baltimore city councilmembers, as well as the two state legislators interviewed for this study, stressed their frustration with the lack of policy oversight. The latter added that a critical motivator for Maryland's OZ enhancement legislation was to try to establish a mechanism for project oversight.[29]

Participants were conflicted about how much oversight was needed. Some developers, including those involved in OZ deals, admitted they did not know how the OZ certification process worked. Even the most "laissez-faire" participants believed the existing tracking mechanism, self-certification by Form 8996, was insufficient and undermining trust.

A developer with a history of working in West Baltimore noted, "In my experience, too much community oversight of private development can lead to misinformed actors that end up scuttling good development… but we have clearly moved too far to the [opposite] end here. [OZs] could… at least have some sort of interim reporting so residents know what the hell is going on and so developers have some guardrails."[30] Likewise, a fund manager commented, "[OZs have] laid bare just how far we have moved away from transparency in economic development …parasitic development is happening, and the feds should not be incentivizing that."[31] A CDE executive went so far as to describe the reporting requirements as "comically corrupt."[32]

Community Development Corporations (CDCs) and smaller developers were the most concerned with the program's lack of oversight, education, and engagement. A CEO of a CDC stated, "[the Empowerment Zones program] may not have succeeded, but at least the community knew how [it] worked. …why isn't there a grant program to educate the residents on how [OZs] work?"[33] The developer of a project in the WBOZC, which expects OZ financing, noted, "the potential for unintended consequences is massive. One, all the development may just be concentrated on areas that don't need it. [Or] two, it isn't… but [OZs lead] to development that causes displacement."[34] These participants and two others suggested that educational engagement around OZs would help counteract a general skepticism of community development initiatives in poor minority communities. They also suggested that it might encourage smaller developers to engage with the policy and seek out OZ investment opportunities and conversations.

Consistent with these views was the incomplete understanding of how OZs work by most community developers and elected officials who participated in our study. We did not find this to be the product of the city and state poorly communicating their OZ efforts. Rather, OZs are such a sufficiently complicated economic development tool that they require federal funding for education

[27] Government agency interviews.

[28] Banking/fund manager/business interviews.

[29] Elected official interviews.

[30] Developer interviews.

[31] Banking/fund manager/business interviews.

[32] Nonprofit/community developer interviews.

[33] Nonprofit/community developer interviews.

[34] Developer interviews.

and engagement. Even the office of a U.S. Senator from Maryland showed a tenuous grasp of how OZ policy worked.

OZs Are Not Changing Economic Development Outcomes in Distressed Neighborhoods

OZs are stimulating new conversations and interest about investment in Baltimore, but this interest has not materialized into new developments for distressed neighborhoods. We documented two projects in the WBOZC likely to receive OZ financing: a $10 million investment in a $100 million mixed-use redevelopment project, and a $1.2 million investment in a $4.5 million project focused on minority-owned business development, zero energy waste, and affordable housing. Study participants described these projects as excellent examples of community-oriented development in and around West Baltimore. While OZs offer each project an additional source of capital for development and may accelerate developer timelines to secure project financing, neither project depends on this financing. Several aspects of OZs explain their inability to attract economic development to truly distressed neighborhoods like West Baltimore.

OZ Investors Demand Market-Rate Returns

OZ investment funds typically seek double-digit internal rates of return (IRR) between 10 and 16 percent, whereas projects in Baltimore's distressed tracts are more likely to generate IRRs no higher than 3–6 percent while also being considered higher risk investments. Most OZ funds are seeking market-rate returns on the same types of investments that other funds are making, regardless of the OZ incentive. An established national developer reported that he was "disappointed at the number of national OZ funds that are expecting pre-tax, compounded IRRs of high teens or even 20 percent for a 10-year hold on 'easy stuff.'"[35] The lowest IRR sought by an OZ fund that we found, which was not based upon an existing relationship for a specific project, was about 8 percent.

Mission-driven funds willing to accept lower returns have either been unable to raise OZ equity or unable to deploy it in truly distressed census tracts. This is partially because low-income census tracts are not expected to appreciate and partially due to technical design flaws, which we discuss later in this section. According to a director at an impact investment firm who considered a fund to support projects in the WBOZC: "there are a lot of reasons, from market realities to specific technical issues, that [OZs are] not going to work for us. [We are] not unique… 95 percent of mission funds have not raised equity."[36] A manager at a development firm exploring locations for an OZ business in Baltimore said, "[OZs don't] offer the value proposition" to invest in distressed neighborhoods.[37] A project sponsor unable to secure OZ capital stated, "[OZs are] meant for market-rate investments, some as high as 18 percent. And this does not fit the race and income profile of [distressed] neighborhoods in Baltimore or elsewhere …. [Do not] expect these funds to [invest] in low-income Black and Brown neighborhoods."[38]

[35] Developer interviews.

[36] Banking/fund manager/business interviews.

[37] Developer interviews.

[38] Nonprofit/community developer interviews.

OZs Are a Weak Incentive That Does Not Spur “but for” Development

OZs are a weak incentive that does not change development outcomes on its own. The tax deferment and the year-5 and year-7 step-up basis benefits of OZs offered little value to investors. One developer described these as “worthless.” Another noted, “we basically don’t bother trying to model those into our proformas anymore.” Five participants suggested that these be substantially increased to have effects. Investors find the value of the tax preference to be the permanent exclusion of taxable income on new gains for investments held for 10 years or longer.[39]

Based on a review of four OZ development proformas and participant reporting, we estimate the overall value of the tax preference to be worth 150 to 400 basis points (1.5–4 percentage points on an IRR). Participants described this value as relatively meager. A developer in the WBOZC noted, “game-changing tax policy would need to incentivize way deeper than this.” Another development team sent us a proposal to layer OZs with a host of other incentives and strategic planning. The proposal reads: “Attracting OZ equity investment for important but challenging projects in highly distressed OZ neighborhoods is proving to be especially difficult.” A Baltimore developer with a long track record of community-oriented development responded by email: “…we quickly determined to stick with [NMTC] investments and avoid the headache.” A developer working in the WBOZC commented, “I think the development community sees [NMTC] as a [much] more effective program.” Consistent with this sentiment, the developer of an OZ project commented that “OZ…was not the ‘but for;’ if anything [NMTC] were the ‘but for.’”[40] A community banking expert added, “OZ doesn’t stop the car from running out of gas….”[41] Participants described OZs as being for “investment-grade” and “shovel-ready” projects. In addition to NMTC, they noted that state and federal subsidy programs, like Economic Development Administration grants, are more important to supporting development than OZs.[42]

OZs Fail to Incentivize Community Developers and Investors

Developers and institutions investing or interested in investing in West Baltimore do not have readily available access to capital gains dollars. A recurrent theme in participant interviews was that there was no shortage of capital in Baltimore and particularly the greater Baltimore-Washington region that could be incentivized to invest in West Baltimore and other distressed areas. OZ’s favoring of capital gains over alternate capital sources, however, means it fails to attract these actors. As one real estate developer put it bluntly, “private equity guys with marble floors from New York are not going to come down to do a deal in the ‘hood’ in West Baltimore, regardless of the incentive you offer them. But there is private wealth here, and there are plenty of people who say ‘[expletive], my grandparents are from Baltimore. I want to make an investment here.’” Another developer similarly stated, “There won’t be bigger community transformation without incentivizing … people involved in the development process.”[43]

[39] Participant interviews.

[40] Developer interviews.

[41] Banking/fund manager/business interviews.

[42] Participant interviews.

[43] Developer interviews.

We found eight examples of OZs failing to support existing development and developers in the WBOZC. These include an expert in African-American wealth-building who is redeveloping single-family housing, a nonprofit providing construction contracts and homeownership opportunities for women of color, and a warehouse in an old lumber yard that could be used for adaptive re-use. We also documented four small businesses that had considered OZ financing to locate in a distressed community but that had been unable to find a deal with OZ investors.

OZs also fail to incentivize institutional capital. Pension funds and endowments came up in over 10 interviews as under-tapped sources of private capital to invest in distressed neighborhoods. According to the CEO of a nonprofit, "[OZs are] focused on attracting Silicon Valley dollars, which is all fine and good. But what the local economic development community has been realizing…a lot of money [is] sitting smack here in the Baltimore region that need not go to Boston or leave the country altogether." Another nonprofit executive noted, "given all the thought cities have put into anchor institutions and homegrown investment, I was disappointed to learn [OZs are] still working under the failed idea of chasing corporations…."[44] Three participants mentioned HopkinsLocal, a 2015 Johns Hopkins University endowment-funded initiative focused on local hiring and minority-owned business development, as an example of an existing initiative that OZs should be incentivizing (Johns Hopkins University, 2015).

Participants also frequently mentioned the absence of Community Development Financial Institutions (CDFIs) and CDCs as actors that were "critical to development in distressed communities" but "left on the sidelines," as one CDFI executive described.[45] CDFIs typically engage in debt-driven development, whereas OZs incentivize equity. An OZ fund can be set up as a separate private investment to support nonprofit development. However, as OZ investors seek high double-digit IRRs, they are often not suited to investing in these lower IRR projects. CDFIs also do not have the resources or human capacity to set up new private OZ funds. Moreover, federal rules about timing requirements for the deployment of capital make it difficult and risky for mission-driven organizations to execute OZ deals.[46] Likewise, CDCs tend to have long planning and development periods, including using the 15-year duration LIHTC.

A few national nonprofits, including Enterprise Community Partners, reported successfully incorporating OZ capital in projects outside of Baltimore. Executives, however, described these models as "not replicable to scale."[47] Baltimore's one exclusive CDFI,[48] and the seven other CDFIs active in Baltimore, were not directly involved in any OZ projects. Six participants mentioned that OZs did not properly align OZs with existing affordable housing and public housing redevelopment efforts. Two national affordable housing experts said that OZs were providing a new source of capital for workforce housing but that it did not support the development or preservation

[44] Nonprofit/community developer interviews.

[45] Nonprofit/community developer interviews.

[46] See more on technical design challenges in next section.

[47] Nonprofit/community developer interviews.

[48] Baltimore's Neighborhood Impact Investment Fund (NIIF) was applying for CDFI status and may become a second Baltimore CDFI.

of deeply affordable housing.[49] As one of these experts summarized, "the [affordable housing] industry does not see OZ as a game changer, [only] as a bridge source for development."[50] We found public housing authorities (PHAs) largely unfamiliar with OZs altogether.[51] The Housing Authority of Baltimore City confirmed this observation: "OZ just doesn't work for deeply affordable housing… or schools or infrastructure—the needs which we are involved in." A city official reiterated, "housing authorities are being expected to engage with OZs, but OZs didn't engage with housing authorities. Frankly, [PHAs] left out is a shame because [they] are… deeply knowledgeable in the challenges facing distressed neighborhoods."[52]

OZs Were Poorly Designed to Benefit Distressed Neighborhoods

OZs suffer from design flaws that make investment in distressed neighborhoods unlikely. Although the City of Baltimore selected distressed neighborhoods in need of investment, federal selection criteria force distressed communities to compete for investment with non-distressed communities both locally and nationally. Nationally, OZ selections have been shown to be of higher or equivalent levels of distress when compared to areas eligible for OZ investment that were not selected. Gentrified neighborhoods, however, or neighborhoods already experiencing capital investment, were also selected (Gelfond and Looney, 2018; Theodos, Meixell, and Hedman, 2018). Across the United States, 56 percent of census tracts qualified for OZ designation. In Baltimore, the rate is 92 percent (Din, 2018). Selection criteria allowed some non-low-income tracts contiguous to low-income tracts to qualify. Some OZ selections were made using outdated data and where distress was not defined properly. [53] For example, numerous college campuses, including the University of Maryland, were eligible for selection because students are considered low-income (Gelfond and Looney, 2018). This limits the likelihood that capital will flow to distressed neighborhoods.[54]

Baltimore selected 41 census tracts based on a set of overlapping investment strategies.[55] OZ selection was also aligned with a NIIF and with a new community development framework (Baltimore City Department of Housing and Community Development, 2021; NIIF, 2020). The Governor of Maryland approved 38 of the 41 tracts proposed by the City of Baltimore and added four new census tracts. The resulting 42 tracts were approved by the U.S. Department of the Treasury. It is noteworthy that two of the four tracts added by the Governor were downtown and Port Covington and that the

[49] The first author has compiled a detailed list of findings on how OZs are and are not being used for affordable housing. These are available upon request.

[50] Nonprofit/community developer interviews.

[51] The first author presented this study to the Council of Large Public Housing Authorities at their annual meeting in October of 2019. PHAs were largely unfamiliar with how the tax preference worked.

[52] Government agency interviews.

[53] Opportunity Zones were selected using data from the American Community Survey from 2011–15. States had the option to use 2012–16 data, but this was not required even if the neighborhood conditions had changed. See Gelfond and Looney (2018) for more on this flexible selection criteria.

[54] Conceptually, it is easy to understand why poor federal criteria for targeting and defining distress leads to distressed areas receiving little investment. OZs put localities in competition with each other for a new class of investors with most of the direct costs of the incentive—capital gains tax collections—the federal government's responsibility. To compete with other states, governors are incentivized to propose higher income or gentrifying census tracts. These tracts offer greater levels of price appreciation and thus receive most OZ investments.

[55] For a review of these strategies see Seigel and Estores (2018).

latter was only deemed eligible because of a mapping error.[56] Downtown's area median income (AMI) was greater than any census tract that city officials had recommended. Port Covington's AMI was twice as large as any census tract city officials had recommended.[57]

Participants described Port Covington as a logical and smart choice for the Governor to compete for OZ investments. They expressed concern, however, regarding its inclusion. A developer active in the WBOZC noted, "now we have a situation where new investors…come in town and do their homework but end up focusing on [Port Covington… not…] places that actually need this outside [capital]."[58] Similarly, a banker described Port Covington as "a totally different beast than the other OZs."[59] They felt that the inclusion of downtown and Port Covington made it difficult for distressed neighborhoods to compete successfully for OZ capital.

Participants knowledgeable in national OZ activity described this as a federal design failure. One fund manager commented that this "is not a story about Port Covington" but rather a challenge with OZ's broad selection criteria. He added, "Unfortunately…a bunch of places that already weren't going to see development [have been] put on a stage against places with [existing] development [activity] and savvy developers. If the playing field is West Baltimore against gentrifying Brooklyn or [downtown] Portland, West Baltimore isn't happening."[60] An economic development expert confided, "I think it is totally possible we see 75 percent of [total] investment being made in just a few [non-distressed] neighborhoods." These participants suggested that OZs required a more accurate definition of distress, the removal of contiguous tracts, and/or a deeper incentive for truly distressed areas. A nonprofit focused on development in underinvested communities described OZ selection criteria as the "original sin" of the policy.[61]

It is noteworthy that most real estate developer participants believed there was also logic in adding less distressed tracts to qualify for OZs as a strategy to help spur investment in more distressed tracts. These real estate developers described Baltimore as requiring a "domino effect," "edge" neighborhood-led development, and/or "working from your strengths" strategy.[62] These developers believed that projects like the redevelopment of Amtrak's Penn Station and Northwood Commons, which are not located in deeply distressed tracts but still qualify as distressed under OZ's definition, may catalyze development in adjacent tracts that are deeply distressed. They did not believe, however, that Port Covington or other "contiguous" tracts served this purpose or meant the intention of the policy.

---

[56] Port Covington qualified as "contiguous" due to a computer program glitch. See Ernsthausen and Elliott (2019).

[57] Based on 2011–15 ACS data, Downtown and Port Covington had AMIs of $55,277 and $103,667, respectively. The census tract with the highest AMI recommended for OZ designation by city officials was $50,280.

[58] Developer interviews.

[59] Banking/fund manager/business interviews.

[60] Banking/fund manager/business interviews.

[61] Nonprofit/community developer interviews.

[62] Developer interviews. Note: "working from your strengths" was the development slogan and strategy of Baltimore Mayor Martin O'Malley. Baltimore City continues to maintain a strategic focus on "middle market" neighborhoods. See City of Baltimore Department of Planning (2020).

OZ's short selection period also did not allow time for planning processes to stimulate market-rate development.[63] This hindered investment in truly distressed neighborhoods. Baltimore's distressed neighborhoods require "development gestation periods" and "market making" in advance of a market-based incentive. These are processes in which public, philanthropic, and nonprofit actors strategically align resources, ideas, and proposals to assist neighborhoods to engage with the market. As one city agency executive summarized, "…distressed neighborhoods could be poised for development… [with]… long-term planning for future investment. But the… short [OZ selection] timeline didn't give the city the ability to be strategic like that." An executive at Baltimore's Department of Housing and Community Development (DHCD) indicated, "There is a lot of 'tilling of the soil' that needs to be done in some … neighborhoods…. [But] the quick designation means [we have to] focus on the short-term deals that you already knew were going to happen."[64] Investors and businesses also indicated that the fast, unorganized rollout of OZs, including Treasury Department guidelines, which were disseminated on a piecemeal basis, discouraged transformative and higher-risk investments.

If the federal government had better aligned OZ policy with direct investment programs, particularly targeting infrastructure and housing, and had they given localities more time to prepare and align their local tools and resources, additional development and investment might have been stimulated. As a developer contemplating an OZ deal stated, "If you really want to see a whole neighborhood improve, you need some sort of planning process…to connect this to the city's strategy around anchor institutions and innovation processes, [etc.]."[65] Five participants suggested that the federal government proactively align OZ policy with direct subsidies from federal agencies, including the Department of Housing and Urban Development (HUD), the Economic Development Administration (EDA), and the Department of Transportation (DOT).[66] A city councilmember representing the WBOZC described the OZ rollout as "putting the cart before the horse," suggesting federal agencies should have provided direct dollars for predevelopment in advance of [OZs]."[67]

OZ rules also make investment in distressed neighborhoods unlikely. Capital deployment regulations stipulate that investors deposit their capital into a fund within 6 months of the gain being realized. In turn, funds must invest their capital in an OZ property or business within 6 months. Meant to ensure that tax-deferred capital is invested into OZs, this process creates risks that are particularly challenging for mission-driven investors with low margins for error. A director at an impact investing firm summarized, "The overarching problem is technical… holding, calling, and deploying OZ capital flies in the face of how private equity often works." Another fund manager said, "You must be simultaneously raising and investing capital…. This is a real challenge and may be why many funds don't materialize and many businesses aren't funded." A third

[63] States had only 90 days to submit their selections to the Treasury although they could ask for a 30-day extension.

[64] Government agency interviews.

[65] Developer interviews.

[66] One year after the Tax Cuts and Jobs Act of 2017 (TCJA) was signed into law, The White House established the Opportunity and Revitalization Council to identify existing federal programs that could be targeted, prioritized, and enhanced in OZs and other distressed communities. See White House (2019). While this effort may reflect the spirit of Comprehensive Community Initiatives, study participants were either unaware of it and/or described it as reactive.

[67] Elected official interviews.

investment fund participant indicated that these deployment rules restricted OZ venture capital from investing in new startups like traditional venture capital. A mission-driven fund manager confirmed, "the challenge is timing, timing, timing. Developers are looking at options on property, [but OZs don't] give them enough time to do their due diligence."[68] A developer of a Baltimore OZ project said, "because you have to get money out the door quickly, time pressure may lead to missed opportunities but also dumb inexperienced investments."[69]

We documented design flaws beyond capital deployment rules. The CEO of a software startup company that sought but did not secure OZ financing responded by email, "the biggest issue was just uncertainty on how a software business could qualify without intangible assets… It was deemed to be too risky for the investors [given] the potential retroactive penalties and interest on taxes." An established company that also considered OZ investment said that OZ policy designers "didn't understand what 'substantial improvement' meant for a small business. Maybe they will figure it out… but we have moved on…. They should have consulted with fund managers about … business development before [putting this into] the tax code."[70] A consistent theme emerged from interviews with businesses: OZ designers failed to fully engage with venture capitalists and fund managers in policy design.

Finally, OZs were failing to address a historically racialized hurdle to development in distressed neighborhoods, the "appraisal gap." In Baltimore, historic banking practices, such as redlining, drove down land values in targeted neighborhoods for decades. Part of the legacy is that current bank regulations now prevent investments in these neighborhoods because the as-is built value of many proposed projects remains low. For example, one study participant was an officer at a national bank that was deploying OZ equity for projects that met Community Reinvestment Act compliance standards. The bank accepted preferred returns as low as 3 percent, thereby facilitating true mission-based development. The bank was hoping to deploy over $100 million in OZ equity in 2021. It had explored four different OZ projects in distressed Baltimore neighborhoods over the course of our study. The bank ultimately was unable to close on a project, however. The officer explained: "in low-income neighborhoods, the appraisal gap [remains] a significant challenge in having a developer find true equity… because we have to [reduce] the [amount of] debt and equity [that we can commit to the project] based on the appraisal."[71] Similarly, in a conversation about appraisal gaps, a nonprofit developer stated, "An OZ type program could be valuable if we… figure out how to value low-income Black and Brown communities."[72]In brief, some OZ proposals do not obtain sufficient capital because the appraisal industry assesses properties in minority neighborhoods at values lower than those projected by investors and developers.

Eight participants discussed how neighborhood value is tied to race and how development standards and criteria, which OZs rely upon, help maintain and replicate a system that denies wealth building in African-American communities. In addition to appraisal gaps, these participants

[68] Banking/fund manager/business interviews.

[69] Developer interviews.

[70] Banking/fund manager/business interviews.

[71] Banking/fund manager/business interviews.

[72] Nonprofit/community developer interviews.

noted that OZs failed to address the lack of sophisticated developers and desirable retail anchors in historically disinvested neighborhoods. These participants recommended direct government intervention in the form of subsidies or by the Treasury acting as a guarantor in historically redlined OZ tracts. We advance this recommendation in the next section.

Restructuring OZs

OZs require substantial restructuring to stimulate investment in distressed neighborhoods. We propose seven changes. Recommendations 1–2 include actions that Congress could take immediately. Recommendations 3–7 are illustrative only. They require additional analysis and the convening of development, policy, and legal experts.

1. **Institute a Reporting Requirement**

OZs are failing at oversight.[73] A federal reporting requirement is needed to fully understand OZ successes and failures and to protect against fraud and abuse. The absence of reporting sends a message that OZs may be a handout to the wealthy and not designed for the benefit of distressed communities.

As of this writing, legislation requiring detailed reporting requirements is pending. For example, Senate Bill 1344 and House Bill 2593 would require the U.S. Department of the Treasury to collect data on the number of funds created, their holdings, and their asset class.[74] They would also require data collection for census tracts receiving Qualified Opportunity Fund (QOF) investments, including measures of poverty reduction, job creation, and new business starts. States and federal agencies would report these data to Congress 5 years after the bill's enactment and every year thereafter. Another proposal, Senate Bill 2787, The "Opportunity Zone Reporting and Reform Act," requires that QOFs report on a host of information, including the identities of all investors, partnerships, and corporations in which the fund holds interest. This bill also creates penalties for taxpayers that fail to comply with reporting requirements. Finally, the bill directs the Government Accountability Office (GAO) to report on the effectiveness of the OZ legislation at years 5 and 10 (Novogradac, 2020). Several policy research and advocacy organizations have also proposed reasonable reporting standards.[75]

The original legislative proposal for OZs included reporting requirements, but they did not survive passage of the Tax Cuts and Jobs Act of 2017. Past federal initiatives offer more robust data collection standards than OZs. Data collection should be implemented immediately.

2. **Remove Non-Distressed Census Tracts from OZ Eligibility**

Giving localities, which compete for footloose investment, the authority to pick neighborhoods that may not meet the intention of investing in distressed neighborhoods has led to census tracts being designated for OZs that do not represent the ostensible objective of the legislation.[76] The continued

[73] See Results: OZ Strengths and Weaknesses #3

[74] H.R. 2593, 116th Congress. (2019). https://www.novoco.com/sites/default/files/atoms/files/hr_2593.pdf

[75] For example, see Theodos (2019).

[76] See Results: OZ Strengths and Weaknesses #4d

inclusion of non-distressed census tracts that are contiguous to distressed tracts may crowd out other private investment, result in large equity investments going to a few neighborhoods that did not need investment, and reduce the chances that OZs reach low-income neighborhoods. Removing contiguous tracts will not remove an important "edge neighborhood" development process described in the OZ strengths and weaknesses section of this report. In Baltimore, edge neighborhoods qualified for OZs because they met the definition of low-income.

Census tracts that no longer qualify for low-income status based on up-to-date data and those that were never intended to be eligible for OZ investment, such as college campuses, should be removed. The "Opportunity Zone Reporting and Reform Act," mentioned in the previous recommendation, provides one model to remove these tracts and replace them with more distressed tracts.[77]

3. Deepen the Tax Preference for Neighborhoods in High Distress

OZs are a weak incentive.[78] Flat rate benefits for a large and diverse set of census tracts means that most equity flows into a few neighborhoods that don't need investment while almost no equity flows into neighborhoods that most need investment. The 10 and 15 percent step-up basis advantages of the tax preference are poorly conceived and of marginal value to investors. However, our interviews and analysis of developer financials indicate that increasing these percentages would stimulate additional OZ investment.[79] Deeper incentives should only be considered for deeply distressed neighborhoods and must be tied to project eligibility and reporting requirements.

4. Funding for Education, Engagement, and Technical Assistance

OZ development in Baltimore has been heavily dependent on local support and capacity, most notably the creation of development coordinators who connect a new class of investors to developers and businesses. These positions were supported by local government and philanthropies, not federal policy. Even with local support, community stakeholders and small developers expressed insufficient education and engagement at the neighborhood level.[80] This is especially concerning because many OZ-designated census tracts have histories of parasitic and discriminatory investment. Moreover, OZ dollars are primarily available to highly experienced and sophisticated developers and businesses with deep contacts in private finance that truly distressed neighborhoods lack. To address this deficiency, the federal government should provide grant support for education, engagement, and technical assistance on OZs.[81]

[77] Gelfond and Looney (2018) also offer additional guidance.

[78] See Results: OZ Strengths and Weaknesses #4b

[79] Our analysis of developer financials suggests the step-up basis advantages would need to be increased to at least a 50 percent reduction on the original capital gains investment. However, analyzing the depth of the incentive required in different housing markets across the country is necessary before a precise change is advised.

[80] See Results: OZ Strengths and Weaknesses #3.

[81] Study participants indicated the minimum level of support should include allocations for states to develop OZ coordinator positions and development strategy documents. Based on a preliminary analysis, we think this support would cost less than $75 million over 5 years of the program. At a greater cost, Congress should also consider grant support for predevelopment loans, technical assistance for businesses, and business incubator and start up support.

5. Fund Infrastructure and Provide a Federal Guarantee for OZ Investments

The rollout of OZs was poorly aligned with direct federal investments.[82] Future OZ investment is more likely to be stimulated if the federal government aligns new direct investments with OZ policy in highly distressed neighborhoods, particularly investments in infrastructure, housing, and transportation. Public investments would increase opportunities for real estate appreciation and business growth.

A federal guarantee should be added to reduce the risk for developers to invest in deeply distressed neighborhoods.[83] Because many distressed neighborhoods were not designated for OZs, it is critical that this guarantee represent additional funding and not the reallocation of existing forms of government aid for community development. The justification for new appropriations could be based on cost savings created by removing contiguous tracts that are currently receiving unnecessary OZ subsidies (as discussed in recommendation 2).

6. Incentivize Community Development Financial Institutions (CDFIs)

OZs fail to incentivize community development.[84] CDFIs are trusted community partners that are willing to take on higher risks and lower returns than traditional private equity actors. They have a long history of investing in low-income communities. As debt-led actors, however, they were not incorporated into OZ policy, which incentivizes equity investments (Tansey and Swack, 2019). In Baltimore, CDFIs are only indirectly engaged in OZs.[85]

Most CDFIs don´t have the capital or capacity to develop QOFs. For CDFIs to make OZ investments, large grant capital would need to be made available to allow these institutions to develop the personnel and knowledge to make equity investments. There are also shorter-term approaches to incorporate CDFIs into OZ policy. First, new legislation could treat subordinated debt and royalty debt products, used by CDFI banks, as OZ investments. This would increase CDFI bank lending capacity in distressed neighborhoods. Another possibility is to allow or require QOFs to partner with CDFI loan funds, bringing OZs under CDFI purview and steering funds toward mission-driven projects. House Bill 7262 proposes to amend the Tax Code of 1986 to allow QOFs to invest in CDFIs and could result in greater CDFI involvement in OZs.[86]

---

[82] See Results: OZ Strengths and Weaknesses #4d.

[83] The exact guarantee and underwriting requirements would need to be determined by additional research and in consultation with finance experts. The amount of risk capital necessary to change project outcomes requires analysis across multiple states and housing markets. According to one estimate shared with us by a mission-driven investment firm, $95 million per state in guarantee capital, over a 5-year window (approximately $4.75 billion total) would generate significant activity in distressed OZ census tracts.

[84] See Results: OZ Strengths and Weaknesses #4c.

[85] For example, through the allocation of New Markets Tax Credits (NMTC) to projects that were also recipients of OZs.

[86] H.R. 7262, 116th Congress (2020). Community Development in Opportunity Zones Act of 2020. https://www.congress.gov/bill/116th-congress/house-bill/7262/all-info?r=1&s=1

7. **Democratize OZs to Non-Capital Gains Dollars**

In Baltimore, we identified capital that, if given tax preference, is more likely to be invested in distressed neighborhoods than capital gains dollars.[87] In addition to CDFIs, OZs are a missed opportunity to capitalize entrepreneurs, investors, and developers who are geographically and emotionally connected to wealth building in distressed neighborhoods. OZs also fail to engage institutional dollars like pension funds of universities that operate in and around distressed neighborhoods but often invest in primary or foreign capital markets.[88]

Capital gains investors already have diverse investment options, and they demand rates of return that are unlikely to be found in distressed markets. Moreover, few small businesses and developers have access to these investors. Thus, we recommend expanding OZs to incentivize certain non-capital gains equity investments made in deeply distressed census tracts. In brief, a permanent exclusion of taxable income produced through an investment could be applied to traditional equity investments for qualified project sponsors and projects. Alternatively, this incentive could be substituted for the current capital gains design. [89] If properly implemented, these changes could encourage development in distressed neighborhoods and prevent waste of future tax dollars for direct federal investment.

Acknowledgments

The authors gratefully acknowledge support for this project by the Johns Hopkins University 21st Century Cities initiative.

Authors

Michael Snidal is a doctoral candidate in urban planning at Columbia University's Graduate School of Architecture, Planning and Preservation and a real estate developer in Baltimore City. Sandra Newman, Ph.D., is Professor of Policy Studies and director of the Center on Housing, Neighborhoods and Communities at Johns Hopkins University Bloomberg School of Public Health.

References

Baltimore City Department of Housing and Community Development. 2021. *A New Era of Neighborhood Investment: A Framework for Community Development*. https://dhcd.baltimorecity.gov/sites/default/files/DHCD%20Framework%202021%20file%20update%20FINAL.pdf.

[87] See Results: OZ Strengths and Weaknesses #4d.

[88] For a discussion of the role pension funds can play in local investment see Baird et al. (2019).

[89] Such a change requires the convening of community development experts, anchor institutions, philanthropies, tax experts, and even communities themselves—to determine the mechanisms and institutions necessary to pool and manage this capital and determine how such tax preference would pass federal securities regulations.

Boarnet, Marlon G., and William T. Bogart. 1996. "Enterprise Zones and Employment: Evidence from New Jersey," *Journal of Urban Economics* 40 (2): 198–215.

Busso, Matias, Jesse Gregory, and Patrick Kline. 2013. "Assessing the Incidence and Efficiency of a Prominent Place Based Policy," *American Economic Review* 103 (2): 897–947.

Din, Alexander. 2018. "Intersecting Opportunity Zones with Vacant Business Addresses," *Cityscape* 20 (3): 277–280.

Engberg, John, and Robert Greenbaum. 1999. "State Enterprise Zones and Local Housing Markets," *Journal of Housing Research* 10 (2): 163–187.

Gelfond, Hilary, and Adam Looney. 2018. *Learning from Opportunity Zones: How to Improve Place-Based Policies.* Washington, D.C.: Brookings Institution.

General Accounting Office (GAO). 1988. *Enterprise Zones: Lessons from the Maryland Experience.* Washington, D.C.

Greenbaum, Robert T., and John B. Engberg. 2004. "The Impact of State Enterprise Zones on Urban Manufacturing Establishments," *Journal of Policy Analysis and Management* 23 (2): 315–339.

Johns Hopkins University. 2015. "HopkinsLocal." https://hopkinslocal.jhu.edu/.

Krupka, Douglas J., and Douglas S. Noonan. 2009. "Empowerment Zones, Neighborhood Change and Owner-Occupied Housing," *Regional Science and Urban Economics* 39 (4), 386–396.

Maryland Department of Housing and Community Development. 2018. *Maryland Opportunity Zones*. Maryland.gov. https://dhcd.maryland.gov/Pages/OZ/OpportunityZones.aspx.

Maryland State Legislature. 2019. "S.B. 581—Regular Session 2019: Economic, Housing, and Community Development—Opportunity Zone Incentives." March 30, 2019. https://legiscan.com/MD/text/SB581/2019.

Neighborhood Impact Investment Fund (NIIF). 2020. https://www.baltimoreniif.org/.

Novogradac. 2020. *Opportunity Zone Reporting and Reform Act Detailed Summary*. https://www.novoco.com/sites/default/files/atoms/files/oz_reporting_reform_act_summary_110619.pdf.

Oakley, Deirdre, and Hui-Shien Tsao. 2006. "A New Way of Revitalizing Distressed Urban Communities? Assessing the Impact of the Federal Empowerment Zone Program," *Journal of Urban Affairs* 28 (5): 443–471.

O'Keefe, Suzanne. 2004. "Job Creation in California's Enterprise Zones: A Comparison Using a Propensity Score Matching Model," *Journal of Urban Economics* 55 (1): 131–150.

Papke, Leslie E. 1994. "Tax Policy and Urban Development: Evidence from the Indiana Enterprise Zone Program," *Journal of Public Economics* 54 (1): 37–49.

Peters, A.H., and P.S. Fisher. (2002). *State Enterprise Zone Programs: Have They Worked?* W.E. Upjohn Institute.

Rubin, Marilyn. 1990. "Urban Enterprise Zones: Do They Work? Evidence from New Jersey," *Public Budgeting & Finance* 10 (4): 3–17.

Tansey, Charles and Michael Swack. 2019. "The Potential Role for CDFIs in the Opportunity Zones of the Investing in Opportunities Act (IIOA)," *The Carsey School of Public Policy at the Scholars' Repository* 362.

Theodos, Brett, Brady Meixell, and Carl Hedman. 2018. *Did States Maximize Their Opportunity Zone Selections?* Washington, D.C.: Brookings Institution, Metropolitan Housing and Communities Policy Center.

Additional Reading

Atkins, Rachel, Pablo Hernandez-Lagos, Cristian Jara-Figueroa, and Robert Seamans. 2021. "What is the Impact of Opportunity Zones on Employment Outcomes?" *NYU Stern School of Business.* http://dx.doi.org/10.2139/ssrn.3673986.

Baird, Ross, Bruce Katz, Jihae Lee, and Daniel Palmer. 2019. *Towards a New System of Community Wealth*. Drexel University's Nowak Metro Finance Lab. https://drexel.edu/~/media/Files/nowak-lab/Drexel_NMFL_CommunityWealth_Final.ashx.

Baltimore Development Corporation. 2018. *Baltimore Development Prospectus.* http://baltimoredevelopment.com/opportunity-zones.

Chen, Jiafen, Edward L. Glaeser, and David Wessel. 2019. The (Non-) Effect of Opportunity Zones on Housing Prices. NBER Working Paper No. 26587. National Bureau of Economic Research.

City of Baltimore Department of Planning. 2020. *Revitalization Strategies*. https://planning.baltimorecity.gov/planning-communities/revitalization.

Council of Economic Advisers (CEA). 2020. *The Impact of Opportunity Zones: An Initial Assessment*. https://www.novoco.com/sites/default/files/atoms/files/white_house_the_impact_of_opportunity_zones_an_initial_assessment_report_082220.pdf.

Ernsthausen, Jeff, and Justin Elliott. 2019. "One Trump Tax Cut Was Meant to Help the Poor. A Billionaire Ended Up Winning Big," ProPublica. https://www.propublica.org/article/trump-inc-podcast-one-trump-tax-cut-meant-to-help-the-poor-a-billionaire-ended-up-winning-big.

Government Accountability Office (GAO). 2010. *Revitalization Programs: Empowerment Zones, Enterprise Communities, and Renewal Communities.* Washington, D.C.

———. 2006. *Empowerment Zone and Enterprise Community Program: Improvements Occurred in Communities, but the Effect of the Program Is Unclear.* Washington, D.C.

Milbergs, Egils, "Transforming Baltimore's Opportunity Zones." YouTube video, 2:05:18, November 12, 2020. https://www.youtube.com/watch?v=UBMHYUCpuPo.

The Promise of Opportunity Zones, Senate Hearing 115-297 before the Joint Economic Committee. 115th Congress (2018). https://www.govinfo.gov/content/pkg/CHRG-115shrg30384/html/CHRG-115shrg30384.htm.

Seigel, Ben, and Franco Estores. 2018. "Opportunity Zones are Knocking: Will Baltimore be Prepared?" Baltimore, MD: 21st Century Cities Initiative. https://21cc.jhu.edu/wp-content/uploads/2018/06/21cc_baltoz_whitepaper.pdf.

Snidal, Michael and Sandra Newman. 2021. "Missed Opportunity: The West Baltimore Opportunity Zones Story." Presented at the Brookings Institution conference, "Opportunity Zones: The Early Evidence," https://www.brookings.edu/wp-content/uploads/2021/01/Snidal-Newman-Brookings-Draft-Feb-19-2021.pdf.

Theodos, Brett. 2019. "A Tailored Opportunity Zone Incentive Could Bring Greater Benefits to Distressed Communities and Less Cost to the Federal Government," Statement of Brett Theodos, Senior Fellow, Urban Institute, before the Subcommittee on Economic Growth, Tax, and Capital Access, Committee on Small Business, U.S. House of Representatives.

Theodos, Brett, Eric Hangen, Jorge González, and Brady Meixell. 2020. *An Early Assessment of Opportunity Zones for Equitable Development Projects*. Washington, D.C.: Urban Institute.

Vanatta, Sean H. 2019. "The Municipal Banking Movement: An Opportunity for Baltimore," *The Abell Report* 32 (6) 1–19.

White House. 2019. *Implementation Plan for the White House Opportunity and Revitalization Council*. Washington D.C.: White House Opportunity and Revitalization Council. https://www.hud.gov/sites/dfiles/Main/documents/WHORC-Implementation-Plan.pdf.