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OPPORTUNITY KNOCKING? ARE OPPORTUNITY ZONES A MODEL FOR A SMARTER FEDERAL HOMEOWNER SUBSIDY?

Matthew J. Rossman

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OPPORTUNITY KNOCKING? ARE OPPORTUNITY ZONES A MODEL FOR A SMARTER FEDERAL HOMEOWNER SUBSIDY?

Matthew J. Rossman*

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INTRODUCTION

At the eleventh hour, Congress tacked a handful of provisions onto its comprehensive tax reform bill, the Tax Cuts and Jobs Act of 2017 ("TCJA"),[1] creating an ambitious new national economic development program called Opportunity Zones. This program allowed each state to designate up to 25% of its high-poverty census tracts as Opportunity Zones and provides lucrative federal tax breaks to those who, over the next several years, invest in businesses located within them.[2] Unlike past tax inducements used to attract business capital to poor, economically disinvested communities, this program places no limits on the number of investors or investments that qualify, has no pre-approval process for investments, and functions virtually unhindered by governmental decision-makers. Proponents of the program tout it as simple, targeted, scalable, and market-driven—and, thus, a smarter approach than its predecessors.[3] And as capitalism aimed at social good, it appeals to both sides of the political aisle.[4]

Notwithstanding the program's inconspicuous adoption, Opportunity Zones did not materialize from thin air. They are the brainchild of a think tank founded by Silicon Valley entrepreneurs, most prominently Napster and Facebook co-founder Sean Parker.[5] The Economic Innovation Group ("EIG") was borne of the belief that putting successful entrepreneurs, policy experts, academics, and investors around a table will yield new insight and innovative solutions to seemingly intractable

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[1] Tax Cuts and Jobs Act, Pub. L. No. 115-97, § 13823(a), 131 Stat. 2184 (2017) (codified at I.R.C. §§ 1400Z-1, 1400Z-2).

[2] I.R.C. § 1400Z-1(d) (2018).

[3] *The Promise of Opportunity Zones: Hearing Before the Joint Econ. Comm.*, 115th Cong. 7–8 (2018) [hereinafter *Hearing Before the Joint Econ. Comm.*] (statement of John W. Lettieri, Co-founder and President of EIG), https://www.jec.senate.gov/public/index.cfm/2018/5/the-promise-of-opportunity-zones.

[4] The original bill proposing Opportunity Zones had several Democratic and Republican co-sponsors. Jim Tankersley, *Tucked Into the Tax Bill, a Plan to Help Distressed America*, N.Y. TIMES (Jan. 29, 2018), http://www.nytimes.com/2018/01/29/business/tax-bill-economic-recovery-opportunity-zones.html. The co-authors of the principal white paper proposing the Opportunity Zones concept were Jared Bernstein, Vice President Joe Biden's former Chief of Staff, and Kevin Hassett, Chairman of President Trump's Council of Economic Advisors when Congress passed the TCJA. *See* Jared Bernstein & Kevin A. Hassett, *Unlocking Private Capital to Facilitate Economic Growth in Distressed Areas*, ECON. INNOVATION GROUP at 1–2 (Apr. 2015), https://eig.org/wp-content/uploads/2015/04/unlocking-private-capital-to-facilitate-growth.pdf.

[5] Andrea Chang, *Entrepreneurs Launch Economic Innovation Group, a D.C. Think Tank*, L.A. TIMES (Mar. 31, 2015), http://www.latimes.com/business/technology/la-fi-tn-economic-innovation-group-20150331-story.html#.

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economic problems.[6] In designing Opportunity Zones, EIG drew on erudite behavioral game theory developed by mathematician John Nash (known to most because of the movie "A Beautiful Mind"), arguing that some economically distressed communities are simply stuck in a "bad" Nash equilibrium.[7] In short, these communities have the capacity to successfully absorb business capital, but instead drive off potential investors, each of whom is individually concerned about being the only one who leaps in and, consequently, losing their wager.[8] Opportunity Zones offer individual federal tax subsidies designed to upend this equilibrium by enticing capital off of the sidelines and into Opportunity Zones, signaling to others a lucrative environment in which to invest.[9] The resulting infusion of capital will create jobs and raise incomes, dramatically transforming the economic prospects and living conditions of residents in economically disinvested places.[10]

Just as decisions by those with business capital about where to invest are instrumental in shaping communities, so are decisions by homeowners and prospective home buyers about where to invest in a home. As this Article will explain, a prospective home investor's calculus can be more complex. Homeowners and buyers typically assess the overall value proposition that will follow from investing and living in a home in a particular community, as opposed to simply considering the potential return on investment. Nevertheless, as with business investors, if other homeowners and home buyers are not investing in a particular community, a prospective home investor will take this as a signal not to do so. When compounded over time, individual decisions to withdraw from or avoid a particular housing market lead to decreased home values, vacant properties, physical deterioration, decimation of the local tax base, and a decrease in city services, each of which feeds the others. This type of a downward community spiral seriously undercuts the value proposition of homeownership in that market.

Housing market disinvestment is as pervasive as economic disinvestment, and perhaps even more stratified.[11] The differences between thriving housing markets and disinvested ones are stark and getting worse, as higher income households

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[6] *Id.*

[7] Bernstein & Hassett, *supra* note 4, at 4.

[8] *Id.*

[9] *Id.*

[10] *Id.* at 5.

[11] *See infra* Part II(A).

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increasingly seek out more exclusive and affluent communities.[12] The negative consequences on health, quality of life, schools, and personal wealth and attainment for those remaining in chronically disinvested housing markets are severe and well documented.[13] On the other hand, emerging research shows significant upticks in property values when the public and philanthropic sectors intervene selectively and strategically to improve the investment environment.[14]

With these similarities in mind, this Article considers whether Opportunity Zones would be a good model for how the federal tax code subsidizes individual homeowner decisions. In a previous article, I criticized the federal tax code's current approach to homeowner subsidies as doing nothing to prevent housing market disinvestment and, in fact, probably accelerating it.[15] As it stands, the tax code subsidizes homeowner decisions no matter where they occur, at least in concept; in reality, the tax subsidies disproportionately benefit those in the wealthiest housing markets.[16] Rewarding homeownership at large is counterproductive and stems from an overly simplistic presumption that only good things happen when someone decides to invest in a home. I argued that different types of homeowner decisions create varying amounts of positive and negative externalities (i.e., benefits to and costs for others).[17] Smarter homeowner subsidies would target those homeowner decisions that net the greatest societal benefit.

At first glimpse, the Opportunity Zones program includes several hallmarks of a smarter subsidy for combatting disinvestment. Ostensibly, it targets federal tax breaks at communities that possess the highest combination of opportunity and need, and, thus, where they would yield the most societal benefit. It is premised on assumptions about business investor behavior that appear to hold water and are also applicable to home investment decisions. Because the program dispenses with the usual bureaucracy associated with targeted subsidies, Opportunity Zones have the potential to spur place-based development at a scale not possible with past approaches that opted for greater governmental involvement and, thus, greater cost.

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[12] *See, e.g.*, David Albouy & Mike Zabek, *Housing Inequality* (Nat'l Bureau of Econ. Research, Working Paper No. 21916, 2016); *see also* Jim Tankersley & Ted Mellnik, *Exclusive Neighborhoods, Exclusive Recovery*, WASH. POST (May 4, 2016), https://www.washingtonpost.com/graphics/business/wonk/housing/charlotte/.

[13] *See infra* Part II(A).

[14] *See, e.g.*, *Rehab Impacts in Cleveland 2009–2015*, DYNAMO METRICS, http://www.rehabimpact.com/ (last visited Apr. 16, 2019).

[15] Matthew J. Rossman, *In Search of Smarter Homeowner Subsidies*, 40 U. HAW. L. REV. 203, 219 (2017).

[16] *Id.* at 213–17.

[17] *Id.* at 217–38.

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Moreover, the program spreads the cost of enticing investors into disinvested communities across the entire federal tax base rather than simply drawing from the already financially distressed local tax bases of those communities. If an analogue to the Opportunity Zone model could meaningfully induce investment by prospective and current homeowners in strategically chosen disinvested housing markets, the infusion of homeowner capital could have a transformative effect not just on those markets, but ultimately on those around them.

Of course, evaluating a model as a better way of subsidizing something as complex, varied, and consequential as homeowner decisions deserves more than just a casual look. It requires a deeper examination of the model, the problem that the model would be used to solve, and the track record of other governmental subsidies in addressing it. This Article undertakes this type of examination. Part I explores more fully the impetus and basic design of the Opportunity Zones program, and identifies emerging criticisms of it. Part II examines the problem of housing market disinvestment and the rationales for public sector intervention to contain it, revealing that these are very similar to the rationales underlying the Opportunity Zones program. Part II also explains how government currently uses tax breaks to subsidize individual homeowner decisions. In so doing, it draws a sharp distinction between the federal tax code's disregard for housing disinvestment and the primary focus local government tax abatement strategies give to it, and identifies significant advantages to addressing the problem through a federal subsidy.

Part III lays out what a federal homeowner analogue to the Opportunity Zones program might look like. To add context, it profiles a housing market that would be a likely candidate and uses it to explain the "disinvestment penalty" faced by homeowners in these types of markets. It then sketches a design for a homeowner subsidy, mimicking as closely as practical the Opportunity Zone model.

Finally, Part IV evaluates whether this type of federal homeowner subsidy would actually be a smarter way of subsidizing homeowner decisions. For this purpose, this Article draws on the qualities of "smart" homeowner subsidies that I proposed in my previous article.[18] Specifically, as this Article will explain, smart subsidies are tailored, limited, variable, and complementary. On the whole, they advance, or at the very least do not undermine, other federal government policies that seek to reduce negative housing externalities. They "pencil out" (i.e., demonstrate a net societal gain that exceeds their cost). Part IV also raises a few additional considerations to bear in mind.

[18] *Id.* at 253–54.

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Putting aside judgment on whether Opportunity Zones will be effective at combatting economic disinvestment, this Article concludes that a homeowner analogue to the Opportunity Zones model has potential as a model for a smarter federal homeowner subsidy, especially when compared to the current homeowner subsidies and subject to some important refinements. As this Article will argue, if it adopted a federal homeowner analogue, Congress should insist on a greater oversight role for the federal government in zone selection and ongoing program assessment and improvement, as well as a more deliberate zone selection process. It should also change certain design aspects of the subsidy, including making it a tax credit on local taxes for all homeowners within the selected housing markets. Congress should also leverage the desire of states and metropolitan governments to see that census tracts within their boundaries qualify for the analogue's tax benefits by insisting they plan in advance for how to address potential strains on housing affordability and other negative housing externalities that could follow from a housing market rebound in their selected census tracts. If carefully designed, these refinements should not dampen the market-driven spark that is central to the Opportunity Zones model. In contrast with the near total disregard for housing market disinvestment exhibited by the federal tax code's current individual homeowner subsidies, a well-crafted homeowner analogue to the Opportunity Zones model at least has the potential to meaningfully combat this pervasive problem.

I. OPPORTUNITY ZONES

A. Background

Intrinsic to the Opportunity Zones model is the recognition that the geography of economic recovery from last decade's Great Recession has been sharply uneven.[19] EIG, among others, demonstrated this through its "Distressed Communities Index."[20] This national map of economic well-being, broken down by zip codes, shows that one in six Americans (fifty-two million individuals) live in communities that are economically distressed.[21] These communities have median household incomes far below and poverty rates well above the national average.[22] Not surprisingly, they

[19] Bernstein & Hassett, *supra* note 4, at 1.

[20] *The 2017 Distressed Communities Index*, ECON. INNOVATION GROUP 1, 18, https://eig.org/wp-content/uploads/2017/09/2017-Distressed-Communities-Index.pdf.

[21] *Id.* at 9.

[22] Tankersley, *supra* note 4.

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also face chronically high unemployment rates and historically low rates of new investment in businesses.[23]

When persistent, these conditions exact severe economic and social costs on those who live in these communities. Long-term unemployment causes incomes to plummet, stalls career progressions, and makes reentry into the work force more difficult.[24] Studies have linked these circumstances to higher illness and suicide rates,[25] higher divorce rates,[26] exacerbated mental health conditions,[27] increased drug abuse,[28] and lower achievement outcomes for children of unemployed workers.[29]

The ripple effect of chronic economic distress extends well beyond the significant personal costs. Poorer communities have greater social service costs, and declining business activity and lower individual incomes reduce the local tax base from which these costs can be met.[30] An overburdened tax base also leads to a drop-off in public investment and infrastructure, making it even more difficult to attract private capital.[31] This causes a downward spiral in the physical and financial conditions of these communities—what the initiators of the Opportunity Zones concept refer to as "an equilibrium characterized by decay."[32]

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[23] Bernstein & Hassett, *supra* note 4, at 2.

[24] *Id.* at 2–3.

[25] *See, e.g.*, Daniel Sullivan & Till von Wachter, *Job Displacement and Mortality: An Analysis Using Administrative Data*, 124 Q.J. ECON. 1265, 1268 n.5 (2009).

[26] *See, e.g.*, Kerwin Kofi Charles & Melvin Stephens Jr., *Job Displacement, Disability, and Divorce* (Nat'l Bureau of Econ. Research, Working Paper No. 8578, 2001), http://www.nber.org/papers/w8578.pdf?new_window=1.

[27] *See, e.g.*, Arthur Goldsmith & Timothy Diette, *Exploring the Link Between Unemployment and Mental Health Outcomes*, AM. PSYCHOL. ASS'N (Apr. 2012), http://www.apa.org/pi/ses/resources/indicator/2012/04/unemployment.aspx.

[28] *See, e.g.*, Gera E. Nagelhout et al., *How Economic Recessions and Unemployment Affect Illegal Drug Use: A Systematic Realist Literature Review*, 44 INT'L J. DRUG POL'Y 69 (2017).

[29] *See, e.g.*, Ann Huff Stevens & Jessamyn Schaller, *Short-Run Effects of Parental Job Loss on Children's Academic Achievement* (Nat'l Bureau of Econ. Research, Working Paper No. 15480, 2009), http://www.nber.org/papers/w15480.pdf.

[30] *See generally* ALAN MALLACH & LAVEA BRACHMAN, REGENERATING AMERICA'S LEGACY CITIES (2013).

[31] Bernstein & Hassett, *supra* note 4, at 3.

[32] *Id.*

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Proponents of Opportunity Zones identify several justifications for intervening in economically distressed communities. Most compelling on a moral and emotive level is providing their residents pathways out of poverty and its host of related problems.[33] Large macroeconomic forces explain much of the economic disparity among communities in the United States and it is therefore hard to fault those who live in places that lost out for circumstances not of their own doing.[34] Accordingly, providing incentives to help these communities reposition themselves to compete on a very different playing field seems entirely fair and compassionate.

Proponents also offer what they characterize as "solid economic arguments" for subsidizing business development in distressed communities.[35] Governments, and thus taxpayers, bear very high costs in providing a social safety net to those living in poverty.[36] These costs could be significantly offset by economic recovery in these communities. Another argument focuses on the lower production of and consumption of goods produced elsewhere in the United States by those who live in distressed areas.[37] These act as drags on national gross domestic product and could be alleviated by reducing unemployment and raising incomes in these areas, making everyone better off.[38]

Then, there is the behavioral game theory known as the Nash equilibrium.[39] EIG contends that the hesitation of investors to fund businesses in many distressed areas stems from their observation that other investors are not doing so.[40] Over time, this resistance causes the community to become stuck in a "bad" Nash equilibrium, in which economically rational and socially efficient capital infusions that would

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[33] *See, e.g.*, Tim Scott, *New Tax Law Will Spur Opportunity in Distressed Communities*, USA TODAY (Feb. 14, 2018), https://www.usatoday.com/story/opinion/2018/02/14/new-tax-law-spur-opportunity-distressed-communities-every-state-tim-scott-column/334519002/.

[34] *See generally The Enduring Challenge of Concentrated Poverty in America: Case Studies from Communities Across the U.S.*, CMTY. AFF. OFFS. FED. RES. SYS. & METRO. POL'Y PROGRAM BROOKINGS INST. (2008), https://www.brookings.edu/wp-content/uploads/2016/06/1024_concentrated_poverty.pdf.

[35] Bernstein & Hassett, *supra* note 4, at 4.

[36] *Id.*

[37] *Id.*

[38] *Id.*

[39] *See, e.g.*, S.K., *What Is the Nash Equilibrium and Why Does It Matter?*, THE ECONOMIST (Sept. 7, 2016), https://www.economist.com/the-economist-explains/2016/09/06/what-is-the-nash-equilibrium-and-why-does-it-matter.

[40] Bernstein & Hassett, *supra* note 4, at 4–5.

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otherwise flow to the community stall because no one wants to be the first to invest.[41] Geographically targeted tax incentives that encourage private investment can upend this equilibrium by sending positive signals to other investors about the investment climate in these communities.[42]

B. Design

To accomplish its objectives, the Opportunity Zones program offers federal income tax breaks to taxpayers with capital gains who invest them in business activity in certain economically distressed communities.[43] A starting point for understanding the design of the program is recognizing that taxpayers in the United States are sitting on over $6 trillion in unrealized capital gains in their stock portfolios and other investments.[44] Generally speaking, the federal tax code taxes these gains at a rate of between 15% and 23.8% when investors realize them by selling their interests in the investments.[45] By taking the gains and investing them into an Opportunity Zone, an investor will, depending on the circumstances, be able to defer, reduce, or avoid the capital gains tax the investor would otherwise have had to pay.[46]

While simple in concept, several aspects of the program and the related tax benefits are more intricate. Congress did not address most of these details in the TCJA. Instead, it charged the United States Department of the Treasury ("Treasury Department") with issuing regulations to fill in the gaps.[47] The Treasury Department has issued proposed regulations and other administrative guidance in multiple waves

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[41] *Id.*

[42] *Id.* at 20.

[43] *Id.* at 4.

[44] *Opportunity Zones: Tapping into a $6 Trillion Market*, ECON. INNOVATION GROUP (Mar. 21, 2018), https://eig.org/news/opportunity-zones-tapping-6-trillion-market.

[45] Effective January 1, 2018, the tax rate on long-term net capital gains (those held for longer than a year) is 15% for individuals with annual income greater than $38,601 ($77,201 if married filing jointly) and less than $425,800, 20% for individuals with annual income greater than $425,801 ($479,001 if married filing jointly), and 21% for corporations. I.R.C. § 1(h) (2018). Many individuals with modified adjusted gross income greater than $200,000 ($250,000) will also pay a net investment tax of 3.8% on their capital gains. I.R.C. § 1411(a) (2018).

[46] *See infra* notes 76–81 and accompanying text.

[47] I.R.C. § 1400Z-2(e)(4).

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in late 2018 and throughout 2019,[48] to the consternation of many investors.[49] Fortunately, for purposes of this Article, a description of the broad parameters of the Opportunity Zones program is sufficient.

First, as with any federal tax credit or deduction, there is terminology to wade through that is critical to understanding exactly what qualifies for it. Investments that qualify for the Opportunity Zone tax benefits are realized capital gains that a taxpayer invests in a Qualified Opportunity Fund ("QOF").[50] A QOF is an investment vehicle organized as a legal entity primarily for the purpose of investing in Qualified Opportunity Zone ("QOZ") Property,[51] which essentially means that it provides capital for new business activity that takes place in an Opportunity Zone.

QOZ Property includes QOZ stock, partnership interests, and business property.[52] QOZ stock and partnership interests are ownership interests in QOZ Businesses that a QOF acquires, solely for cash, after December 31, 2017.[53] QOZ business property is tangible property, like real estate or equipment, acquired by a QOF primarily for use in a trade or business in a QOZ.[54] The tangible property must be new or substantially improved by the QOF,[55] acquired for cash, and acquired after December 31, 2017.[56] Many of these requirements follow from the objective that the

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[48] *See, e.g.*, Investing in Qualified Opportunity Funds; Hearing, 84 Fed. Reg. 1014 (proposed Feb. 14, 2019) (to be codified at 26 C.F.R. pt. 1); *Opportunity Zones Frequently Asked Questions*, IRS, https://www.irs.gov/newsroom/opportunity-zones-frequently-asked-questions (last updated Aug. 23, 2019); Investing in Qualified Opportunity Funds, 84 Fed. Reg. 18652 (proposed May 1, 2019) (to be codified at 26 C.F.R. pt. 1) [hereinafter Investing in Qualified Opportunity Funds 18652].

[49] *See, e.g.*, Michael Novogradac, *Clarity Provided by Second Tranche of Treasury Regulations to Incent More Investment in Opportunity Zones Businesses (Part I)*, NOVOGRADAC (Apr. 17, 2019), https://www.novoco.com/notes-from-novogradac/clarity-provided-second-tranche-treasury-regulations-incent-more-investment-opportunity-zones; Ethan Rothstein, *Multi-Asset Funds, Aggregating, Gentrification And Abuse: IRS Still Has A Lot On Its OZ Regs Plate*, BISNOW (July 10, 2019), https://www.bisnow.com/national/news/opportunity-zones/big-questions-still-linger-after-the-final-opportunity-zones-hearing-99792.

[50] I.R.C. § 1400Z-2(d)(1).

[51] *Id.*

[52] *Id.* § 1400Z-2(d)(2)(A)(i–iii).

[53] *Id.* § 1400Z-2(d)(2)(B)–(C).

[54] *Id.* § 1400Z-2(d)(2)(D)(i).

[55] *Id.* § 1400Z-2(d)(2)(D)(i)(II).

[56] *Id.* § 1400Z-2(d)(2)(D)(i)(I) (citing "purchase" as defined in I.R.C. § 179(d)(2)).

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program attract new capital to Opportunity Zones that represents long-term cash investments in these businesses, rather than loans.

A QOZ Business is an entity that meets several requirements. Most relevant for purposes here is that substantially all its tangible assets are used in a trade or business in a QOZ and that at least 50% of its total gross income is derived from the active conduct of the business in a QOZ.[57] There are a handful of specified business activities that disqualify an entity as a QOZ Business, including golf courses, country clubs, hot tub and suntan facilities, race tracks and other gambling venues, and liquor stores.[58] But these are relatively narrow restrictions; the intent of the program is to capitalize businesses engaged in a very broad range of goods and services within Opportunity Zones.

Last, but certainly not least, is the term Opportunity Zone itself. Generally speaking, an Opportunity Zone is a low-income population census tract that a state has nominated and the Treasury Department has certified qualifies for this status, making it a QOZ.[59] The TCJA took its definition of eligible census tracts directly from the definition of "low-income community" ("LIC") for the New Market Tax Credit ("NMTC"), another federal program that encourages investment in distressed areas.[60] A LIC is a census tract that has either (i) a poverty rate of at least 20% or (ii) a median family income that falls below 80% of the statewide or metropolitan area median family income, depending on its location.[61] However, a state could also nominate a census tract as a QOZ if it was contiguous with an LIC that it nominated as a QOZ and if the median family income of the tract did not exceed 125% of the median family income of the contiguous LIC QOZ.[62] The idea was to allow states to include some census tracts that fell below high-poverty thresholds, but still made

[57] *Id.* § 1400Z-2(d)(3)(A)(ii) (citing I.R.C. § 1397C(b)(2)).

[58] *Id.* § 1400Z-2(d)(3)(A)(iii).

[59] *Id.* § 1400Z-1.

[60] *Id.* § 1400Z-1(c)(1) (citing I.R.C. § 45D(e)).

[61] *Id. See* I.R.C. § 45D(e) (Low-income community "means any population census tract if—(A) the poverty rate for such tract is at least 20 percent, or (B)(i) in the case of a tract not located within a metropolitan area, the median family income for such tract does not exceed 80 percent of statewide median family income, or (ii) in the case of a tract located within a metropolitan area, the median family income for such tract does not exceed 80 percent of the greater of statewide median family income or the metropolitan area median family income."); *see also* Rev. Proc. 2018-16, 2018-9 I.R.B. 383.

[62] Rev. Proc. 2018-16, 2018-9 I.R.B. 383.

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strategic sense to target. No more than 5% of the tracts a state nominated could be non-LIC contiguous tracts.[63]

A particularly interesting feature of the Opportunity Zones program, especially for purposes of this Article, is that it limited the number of census tracts a state could nominate to 25% of the total number of LIC census tracts in that state.[64] The statute did not prescribe how a state should make its choices. But the intention clearly was to get states to prioritize tracts that they felt represented the best balance of need and opportunity.[65] Earlier versions of the Opportunity Zones legislation were more explicit in this regard, requiring states to

> provide particular consideration to areas that: (1) are currently the focus of mutually reinforcing state, local, or private economic development initiatives to attract investment and foster startup activity; (2) have demonstrated success in geographically targeted development programs such as promise zones, the new markets tax credit, empowerment zones, and renewal communities; and (3) have recently experienced significant layoffs due to business closures or relocations.[66]

The late omission of the more explicit selection language did not appear to represent any change in course in this regard. Rather, in the words of EIG's President, it reflected a recognition of the "federalist spirit of the new law," giving states even more leeway as they went about "identifying priorities, engaging stakeholders and incorporating additional selection criteria in ways that reflected their unique local characteristics."[67]

Ironically, given the care Congress wanted states to take in choosing census tracts, it only gave them ninety days from the enactment of the TCJA to nominate

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[63] I.R.C. § 1400Z-1(e)(2); *see also* Rev. Proc. 2018-16, 2018-9 I.R.B. 383.

[64] *Id.* § 400Z-1(d)(1). For a state where 25% of LIC produces a fractional quotient, the state may round up to the next whole number. And if a state has fewer than 100 LICs, it may designate a total of 25 tracts. Rev. Proc. 2018-16, 2018-9 I.R.B. 383-84.

[65] *See, e.g.*, *Opportunity Zones: A New Economic Development Tool for Low-Income Communities* (Guidance for Governors, February 2018), ECON. INNOVATION GROUP (2018), https://eig.org/wp-content/uploads/2018/02/Guidance-for-Governors-FINAL.pdf.

[66] *See Joint Explanatory Statement of the Committee of Conference*, 115th Cong. 399 (2017), https://docs.house.gov/billsthisweek/20171218/Joint%20Explanatory%20Statement.pdf (summarizing the text of the provisions proposed by the Senate in December 2017); *see also* Investing in Opportunity Act, S. 293, 115th Cong. (2017), https://www.congress.gov/bill/115th-congress/senate-bill/293/text.

[67] *See Hearing Before the Joint Econ. Comm.*, *supra* note 3, at 3.

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the tracts (although they could request a thirty-day extension).[68] In turn, the Treasury Department had only thirty days from receipt of the states' nominations to designate the nominated tracts as QOZs.[69] The end result was that by June 14, 2018, less than six months after passage of the TCJA and an even shorter time after many state officials had even heard of the program, the process of choosing Opportunity Zones was over.[70] A QOZ designation remains in effect for the length of the program (i.e., until December 31, 2028) and the TCJA provided no mechanism for a state to change its QOZs.[71]

As for the specific tax breaks a QOZ provides, the program's proponents designed them based on what they viewed as the links between the needs of economically distressed communities, the capacity of private market investors, and the types of incentives and the investment environment that could spur them to invest.[72] Economically distressed communities need large pools of immediately and broadly available business capital that is not looking to exit quickly and is not dependent on accompanying public sector investment.[73] Private investors are sitting on massive amounts of unrealized capital gains, as a result of post-recession stock market appreciation, and like all economic actors, they seek to minimize or at least defer the taxes they pay on gains.[74] Investors also tend to prefer investment vehicles that are nimble, administratively straightforward, and spread risk.[75]

Against this backdrop, several design aspects of the program can be better understood. For instance, the number and value of the tax breaks increase the longer the investment lasts.[76] The tax breaks are a combination of capital gain tax deferral, discounts, and exclusion that may be best explained with an example. Imagine an investor who realizes a $1 million capital gain from selling stock in 2018 and would

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[68] I.R.C. §§ 1400Z-1(b)(1)(A), 1400Z-1(c)(2)(A).

[69] *Id.* §§ 1400Z-1(b)(1)–(2), 1400Z-1(c)(2)(B).

[70] Treas. Notice 2018-48 (June 20, 2018) (listing population tracts officially designated as QOZs).

[71] I.R.C. § 1400Z-1(f) (more specifically, until the close of the 10th calendar year following the designation).

[72] *See* Bernstein & Hassett, *supra* note 4.

[73] *Id.* at 16.

[74] *Id.*

[75] *Id.* at 17.

[76] I.R.C. § 1400Z-2(b)–(c).

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otherwise have to pay federal tax of $238,000 on this gain, leaving her $762,000.[77] If she invests the $1 million dollars in a QOZ Fund, she will not have to pay this tax until the sooner of when she disposes of her QOZ Fund investment (or the QOZ Fund liquidates) or December 31, 2026, saving her money simply through tax deferral.[78] If she holds the investment for between five and seven years, she also will receive what amounts to a cancellation of 10% of the tax on the gain she invested in the QOF,[79] saving her an additional $23,800. This cancellation increases to 15% if she holds the investment for between seven and ten years,[80] netting her an additional $11,900. Finally, if she holds the investment longer than ten years, she also pays no capital gains tax on any gain resulting from her investment in the QOZ Fund.[81]

Because the tax benefits are contingent on the investor's investment in a QOZ Fund rather than her direct investment in a QOZ Business, the investment can be pooled with those of other investors, spreading out the risk any one investor faces. Furthermore, the QOZ Fund can move investments between various qualifying businesses and business assets in the QOZ, tying the investor's success to fund performance rather than necessarily to the performance of any one particular business. The statute contains no governmental pre-approval process or caps on investment, and a QOZ Fund will self-certify as to its compliance with the law.[82] This means that the program is nearly entirely free of any bureaucratic procedures or oversight. These features have led Opportunity Zone program proponents to proclaim that it is more "free market" oriented, more likely to attract investors, and more nimble than past federal and state programs aimed at spurring economic development in distressed communities.[83]

However, even at this early stage, the Opportunity Zones program is not without its critics. The speed at which the program moved from inclusion in the TCJA to implementation left government officials, fund managers and investors

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[77] Local Initiatives Support Coalition, *Opportunity Zones Fact Sheet*, OPPORTUNITY FIN. NETWORK, https://ofn.org/sites/default/files/resources/PDFs/Opportunity_Zone_fact_sheet.pdf (last visited May 9, 2019).

[78] I.R.C. § 1400Z-2(b)(1).

[79] *Id.* § 1400Z-1(b)(2)(B)(iii).

[80] *Id.* § 1400Z-2(b)(2)(B)(iv).

[81] *Id.* § 1400Z-2(c).

[82] Internal Revenue Service, *About Form 8996, Qualified Opportunity Fund*, https://www.irs.gov/forms-pubs/about-form-8996.

[83] Bernstein & Hassett, *supra* note 4, at 4.

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scrambling to figure out how it worked.[84] As noted above, the TCJA also left out many details.[85] While the Treasury Department continues to write and release regulations in "tranches" filling in these details, many investors have remained on the sidelines due to the uncertainty.[86] Meanwhile, more than eighteen months have already passed, lessening the value of certain tax benefits due to the program's statutorily prescribed end date.[87]

There are also early signs that the program will not produce the volume or types of investment its proponents touted due to certain design aspects. Some investors are balking at the "capital lockup" associated with the long periods necessary to realize the program's more lucrative tax benefits.[88] The complexities resulting from the hundreds of pages of interpretive regulations the Treasury Department has released is also causing distaste among investors about the professional and administrative fees they face in making investments in QOFs.[89] Meanwhile, early reports indicate that those QOF investments that are occurring are going mostly to higher end rental housing and hotels in already bustling neighborhoods, as the program's unfettered investing requirements allow capital to flow to opportunities that represent the lowest risk and highest return to investors.[90] Program proponents counter that the real estate

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[84] *See, e.g.*, Ruth Simon & Richard Rubin, *As States Pick 'Opportunity Zones' for Tax Breaks, a Debate Over Who Benefits*, WALL ST. J. (Mar. 20, 2018), https://www.wsj.com/articles/will-new-tax-incentives-for-poor-communities-work-some-are-skeptical-1521547201.

[85] *See supra* notes 47–49 and accompanying text.

[86] *See, e.g.*, Jon Banister, *Opportunity Zone Experts Voice Concerns Over Program's Rules, Suggest Fixes in IRS Hearing*, BISNOW (Feb. 14, 2019), https://www.bisnow.com/national/news/capital-markets/opportunity-zone-experts-voice-concerns-over-programs-rules-suggest-fixes-in-irs-hearing-97528.

[87] *See, e.g.*, Lynnley Browning, Bloomberg, *Opportunity Zones Knocking, But Few Answering the Call So Far*, BLOOMBERG (Apr. 10, 2019), https://www.bloomberg.com/news/articles/2019-04-10/opportunity-zones-knocking-but-few-answering-the-call-so-far.

[88] *See, e.g.*, Alicia McElhaney, *Is Anyone Actually Investing in Opportunity Zone Funds?*, INSTITUTIONAL INVESTOR (May 23, 2019), https://www.institutionalinvestor.com/article/b1fjptxryzv07y/Is-Anyone-Actually-Investing-in-Opportunity-Zone-Funds.

[89] *See, e.g.*, Ryan Ermey, *Opportunity Zone Investing: Is It for You?*, KIPLINGER (June 5, 2018), https://www.kiplinger.com/article/investing/T041-C000-S002-opportunity-zone-investing-is-it-for-you.html.

[90] *See, e.g.*, Jesse Drucker & Eric Lipton, *How a Trump Tax Break to Help Poor Communities Became a Windfall for the Rich*, N.Y. TIMES (Aug. 31, 2019), https://www.nytimes.com/2019/08/31/business/tax-opportunity-zones.html; *cf.* Brian Phillips, *What Investors Need To Know About The 'Three Waves' Of Opportunity Zones*, FORBES (June 11, 2019), https://www.forbes.com/sites/forbesnycouncil/2019/06/11/what-investors-need-to-know-about-the-three-waves-of-opportunity-zones/#446f71e14f4a.

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projects that have dominated the program's early wave are merely the lower-hanging fruit, and they preach patience for the venture capital for businesses that will grow quality local jobs that they assert the program will ultimately attract.[91]

Another commonly voiced concern is that the statute did not contemplate safeguards to address gentrification and affordability issues in communities where Opportunity Zone benefits prove successful in reigniting real estate markets.[92] In a similar vein, advocates for economically distressed communities wonder if the jobs created in Opportunity Zones will actually fit the skill sets of those who live in them and/or if the products and services the businesses offer match the needs of QOZ residents.[93]

Still others have voiced concerns about last minute deletions of transparency and reporting requirements included in the original bill that served as the basis for Opportunity Zones.[94] The original legislation required the Secretary of the Treasury to collect data and report five years from the beginning of the program and annually after that to Congress on a broad range of matters.[95] These reports would have included details on the use of the program incentives as well as the effect of Opportunity Zones investments on economic indicators like job creation, poverty reduction, and new business starts within the Zones.[96] A program as broad and flexible as this one necessarily invites concern as to whether it achieves its objectives

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[91] Phillips, *supra* note 90.

[92] Adam Looney, *Will Opportunity Zones Help Distressed Residents or Be a Tax Cut For Gentrification?*, BROOKINGS (Feb. 26, 2018), https://www.brookings.edu/blog/up-front/2018/02/26/will-opportunity-zones-help-distressed-residents-or-be-a-tax-cut-for-gentrification.

[93] *See, e.g.*, Dan Weil, *The Trump Administration Said These Tax Breaks Would Help Distressed Neighborhoods. Who's Actually Benefiting?*, WASH. POST (June 6, 2019), https://www.washingtonpost .com/realestate/opportunity-zones-are-loaded-with-tax-benefits-but-will-they-actually-help-residents/ 2019/06/05/0f80e1c6-7e68-11e9-8bb7-0fc796cf2ec0_story.html?noredirect=on&utm_term= .a4a8f66c96a8.

[94] Letter from Sen. Cory Booker, to The Honorable Steven T. Mnuchin, Sec'y of the Treasury 1 (June 8, 2018), https://www.novoco.com/sites/default/files/atoms/files/booker_letter_oz_060818.pdf; *see also Hearing Before the Joint Econ. Comm.*, *supra* note 3 (statement of Terri Ludwig, CEO of Enterprise Community Partners, recommending "Treasury prohibit abusive investments that result in the net elimination of affordable housing (housing that is affordable to residents earning up to 120 percent of Area Median Income) because housing affordability is vital to achieve the intent" of the OZ Program).

[95] Investing in Opportunity Act, S. 293, 115th Cong. § 2(c) (2017).

[96] *Id.*

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and whether it is being abused, and the absence of reporting requirements makes these concerns much more difficult to monitor.

II. HOUSING MARKET DISINVESTMENT AND HOMEOWNER SUBSIDIES

A. *Disparity and Disinvestment in Local Housing Markets*

Like economic well-being, housing market strength varies across the country and is perhaps even more stratified.[97] Even a brief look at home value analytics websites like Zillow or Core Logic reveals that the nation consists not of one housing market, but of thousands of localized markets and submarkets[98] that vary considerably in their strengths and weaknesses.[99] Disparity across and within housing markets only heightened during the onset and recovery from the foreclosure crisis and financial recession of the past decade.[100] Housing market measures, like home value fluctuations, sale activity, and housing stock conditions, can vary significantly not only between different regions of the country, but also city by city and even neighborhood by neighborhood.[101]

As with local economies, housing markets in some communities are highly distressed due to chronic disinvestment. Generally speaking, community disinvestment is a process by which residents, institutions, businesses, and other financially mobile economic actors extricate themselves from a community they perceive as deteriorating and too risky in which to invest, leading to further decline

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[97] *Compare The 2017 Distressed Communities Index*, *supra* note 20, *with* Ted Mellnik et al., *America's Great Housing Divide: Are You a Winner or Loser?*, WASH. POST (Apr. 28, 2016), https://www.washingtonpost.com/graphics/business/wonk/housing/overview/?noredirect=on.

[98] For simplicity's sake, this Article will often use "housing market" to mean metropolitan housing markets, as well as the myriad of smaller submarkets included within them. Other times, it will use "submarket" when it seems important to do so.

[99] *See generally* ZILLOW, https://www.zillow.com/ (last visited Apr. 6, 2019); *see also* CORELOGIC, https://www.corelogic.com/ (last visited Apr. 6, 2019).

[100] *See, e.g.*, Frank Ford, *Is the Cuyahoga County Foreclosure Crisis Over? It Depends on Where You Are Standing*, W. RESERVE LAND CONSERVANCY (Mar. 18, 2016), https://www.wrlandconservancy.org/articles/2016/03/18/is-the-cuyahoga-countyforeclosure-crisis-over; *see also* Matthew J. Rossman, *Counting Casualties in Communities Hit Hardest by the Foreclosure Crisis*, 2016 UTAH L. REV. 245, 253–61.

[101] *See* Rossman, *supra* note 100.

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and, in some cases, large-scale abandonment.[102] Less mobile actors (i.e., those who cannot afford to move) are typically the ones left behind.

Housing market disinvestment drives down home values to the point that they struggle to support private investment. Remaining homeowners hesitate to make improvements to their homes out of a concern they will not recoup these investments.[103] Developers, lenders, and prospective home buyers view purchasing and rehabbing existing homes and constructing new ones as too risky or cost prohibitive, so new sources of capital also dry up.[104] Meanwhile, a shrinking tax base, caused by the departure of more affluent residents, businesses, and institutions, falls far short of allowing local government to capably manage increasing stockpiles of orphaned and deteriorating homes.

It is important to note that the demographic patterns of millennials and empty nesters, and the fruition of long-standing urban revitalization efforts, are successfully turning around housing markets in many downtown areas and other amenity-rich urban neighborhoods once thought of as disinvested.[105] But a bird's eye view of the country's housing markets reveals other demographics that are quite troubling and indicate the great extent of disinvestment. Nationwide, 22.1% of census tracts have significantly depressed property values and predominantly low-income populations, which are hallmarks of disinvested housing markets.[106] So-called "middle neighborhoods" are another large category of communities, encompassing up to 50% of housing in some metropolitan areas.[107] Middle neighborhoods are less distressed

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[102] *See, e.g.*, Arthur J. Naparstek & Dennis Dooley, *Countering Urban Disinvestment Through Community-Building Initiatives*, 42 SOC. WORK 506 (1997).

[103] *See generally* Susie Chung, *The Geography of Home Improvement Activity: A Metropolitan-Level Analysis of Remodeling Expenditures During the 2000s*, JOINT CTR. FOR HOUS. STUD. (2011), http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/w11-6_chung.pdf.

[104] One example of this is known as the "appraisal gap." Due to a home appraisal that comes in at a price that is lower than what was agreed upon by a seller and buyer, a mortgage lender is unwilling to lend a sufficient amount to allow the transaction to move forward. *See, e.g.*, Brena Swanson, *Homeowner Expectations and Appraisal Values Divided as Gap Widens*, HOUSINGWIRE (Mar. 8, 2016), https://www.housingwire.com/articles/36481-homeowner-expectations-and-appraisalvalues-divided-as-gap-widens.

[105] *See, e.g.*, ALAN MALLACH, THE DIVIDED CITY: POVERTY AND PROSPERITY IN URBAN AMERICA 33–48 (2018).

[106] Neighborhood Homes Inv. Act Coal., Neighborhood Homes Tax Credit Presentation (July 20–21, 2017), https://www.dropbox.com/s/048w8v0mygpihmt/NHTC_Ohio_presentation_FINAL.pdf?dl=0.

[107] *See* Ira Goldstein et al., *Demographics and Characteristics of Middle Neighborhoods in Select Legacy Cities*, *in* ON THE EDGE: AMERICA'S MIDDLE NEIGHBORHOODS 21, 29 (Paul Brophy ed., 2016) (indicating

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for now but sit on the precipice of disinvestment based on a number of demographical and economic indicators.[108]

Housing market strength, like economic prosperity, is an indicator of other measures of community and personal well-being. Residents of robust housing markets, on the whole, do significantly better while residents of disinvesting housing markets do significantly worse in accumulating personal wealth, home value appreciation, and personal attainment for their children.[109] Disinvesting housing markets are also much worse off when it comes to schools, public infrastructure, crime, vacant properties, and other physical deterioration,[110] and their residents are considerably more likely to be exposed to environmental health hazards like lead paint, bad drinking water, and poor air quality.[111]

There is a strong, although not an absolute, correlation between a particular community's economic prosperity and its housing market strength.[112] Although robust local economies tend to drive up demand for homes and thus home values, other factors can play a role. Most notable (and troubling) is race. For instance, it has long been established that home value appreciation in predominantly African American communities lags considerably behind that of homes in predominantly white communities with comparable resident income levels.[113] Increasing levels of

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that between 37% and 51% of residents in sample legacy cities, like Baltimore, Detroit, Milwaukee and Philadelphia, live in middle neighborhoods).

[108] *See* Paul Brophy, *Middle Neighborhoods in America's Cities and Suburbs: Rediscovering a Precious Asset*, *in* ON THE EDGE: AMERICA'S MIDDLE NEIGHBORHOODS vii, viii (Paul Brophy ed., 2016).

[109] *See generally* Rossman, *supra* note 15, *infra* Part IV(A)–(B).

[110] *Exploring the Relationship Between Vacant and Distressed Properties and Community Health and Safety*, CTR. ON URB. POVERTY & CMTY. DEV. (June 5, 2017), http://povertycenter.case.edu/wpcontent/uploads/2017/06/vacant_distressed_props_comm_health_safety.pdf [hereinafter *Distressed Properties Study*]; *see also* Erica Raleigh & George Galster, *Neighborhood Disinvestment, Abandonment, and Crime Dynamics*, 37 J. URB. AFF. 367, 367 (2015).

[111] *See* Emily A. Benfer & Allyson E. Gold, *There's No Place Like Home: Reshaping Community Interventions and Policies to Eliminate Environmental Hazards and Improve Population Health for Low-Income and Minority Communities*, 11 HARV. L. & POL'Y REV. S1, S3, S4, S9 (2017).

[112] *Compare The 2017 Distressed Communities Index*, *supra* note 20, with Ted Mellnik et al., *supra* note 97.

[113] *See, e.g.*, Gregory D. Squires, *Demobilization of the Individualistic Bias: Housing Market Discrimination as a Contributor to Labor Market and Economic Inequality*, 609 ANNALS AM. ACAD. POL. & SOC. SCI. 200 (2007); *see also* DAVID RUSK, THE "SEGREGATION TAX": THE COST OF RACIAL SEGREGATION TO BLACK HOMEOWNERS (Brookings Inst. ed. 2001), https://www.brookings.edu/research/

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segregation of wealthy residents into wealthy neighborhoods and poor residents into poor neighborhoods is another way in which the economic prosperity of a metropolitan area is often not indicative of strength throughout that area's housing markets.[114]

B. Rationales for Intervention in Disinvested Housing Markets

As discussed in Part I, Section A, proponents of Opportunity Zones offer four principal rationales for subsidizing business investment decisions in economically distressed areas. One could offer the very same rationales for subsidizing homeownership decisions in disinvested housing markets.

First, there is a personal and moral obligation to ameliorate the highly distressing living conditions of those who live in disinvested housing markets. This type of disinvestment occurs as a result of many individual decisions by financially mobile residents and other economic actors to depart that, when taken together and spread over time, decimate a housing market and result in collateral damage to both the community and its residents.[115] Moreover, certain governmental policies have actually accelerated the pace of disinvestment in ways that have negatively and disproportionately impacted low-income and minority residents who remain in these markets.[116] It seems profoundly unfair to simply pin the costs resulting from these decisions on those left behind, many of whom lack the resources to leave.

A second rationale for intervening with subsidies is to reduce the vast cost to government at all levels of containing the dangers and risks associated with deteriorating housing markets, to say nothing of reducing the other costs governments currently incur in trying to engineer market turnarounds. Decaying and abandoned properties are the most visible sign of housing market disinvestment, and they impose substantial costs on local government through increased housing code

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the-segregation-tax-the-cost-of-racial-segregation-to-black-homeowners/. This disparity rises with increasing levels of segregation. *Id.*

[114] *See, e.g.*, Albouy & Zabek, *supra* note 12, at 10.

[115] George Galster, *The Case for Intervention in Middle Neighborhoods*, *in* ON THE EDGE: AMERICA'S MIDDLE NEIGHBORHOODS 9–20 (Paul Brophy ed., 2016).

[116] *See, e.g.*, Richard D. Kahlenberg & Kimberly Quick, *The Government Created Housing Segregation. Here's How the Government Can End It*, THE AMERICAN PROSPECT (July 2, 2019), https://prospect.org/article/government-created-housing-segregation-heres-how-government-can-end-it; *see also* RICHARD ROTHSTEIN, THE COLOR OF LAW: A FORGOTTEN HISTORY OF OUR GOVERNMENT SEGREGATED AMERICA (2017).

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enforcement staff, nuisance abatement, and, ultimately, demolition costs.[117] Local governments must also pay to deal with associated increases in crime and environmental health hazards, on top of "normal" city services, at the same time as their tax bases shrink due to the exodus of affluent residents, the decreased tax value of deteriorating buildings, and the negative spillover effect that distressed properties have on the property values of neighboring ones.[118] State and federal governments act as somewhat of a backstop by providing deteriorating communities with both conventional community development funding[119] and supplemental needs-based funding for other expenses like infrastructure, transportation, schools, and ameliorating health hazards. Due to the expense of and inconsistency of political will in aiding disinvested communities, however, much of this funding unfortunately takes the form of after-the-fact disaster relief rather than proactive investments to head off problems before they arise.[120] A critical missing ingredient in this scenario is adequate capital investment to reawaken a viable housing market, which could in turn interrupt the backlog of decaying properties, fund infrastructure, and alleviate quality of life concerns. It is certainly fair to contend that, if effective, subsidizing homeowner decisions that reduce disinvestment would significantly reduce overall government expenses.

[117] CMTY. RESEARCH PARTNERS & REBUILD OHIO, $60 MILLION AND COUNTING: THE COST OF VACANT AND ABANDONED PROPERTIES TO EIGHT OHIO CITIES (2008), https://www.issuelab.org/resources/3351/3351.pdf?download=true (studying eight Ohio cities, prior to the national foreclosure crisis that drastically increased property vacancy and deterioration in those cities, and estimating the annual costs of vacant and abandoned properties to those cities at $64 million—nearly $15 million in city service costs and over $49 million from lost tax revenues from demolitions and tax delinquencies).

[118] *See, e.g.*, DAN IMMERGLUCK, THE COST OF VACANT AND BLIGHTED PROPERTIES IN ATLANTA: A CONSERVATIVE ANALYSIS OF SERVICE AND SPILLOVER COSTS 23 (2015) (estimating "conservatively" the costs of vacant and blighted properties in Atlanta to city government at between $2.6 million and $5.7 million annually along with a one-time cost to single family property values of $153 million).

[119] *See, e.g.*, *Community Development Financial Flows*, URB. INST., https://apps.urban.org/features/community-development-financing/ (last visited Apr. 9, 2019) (detailing, through an interactive dashboard, investment data for ten federally supported community development programs at the county-level: HUD HOME awards, low-income housing tax credit allocations; HUD Choice Neighborhood awards; Capital Magnet Fund awards; Community Development Finance Institutions lending activity, Opportunity Finance Network data; New Markets Tax Credit Program investments project data; Community Reinvestment Act–reported small business lending data, Promise neighborhoods awards; Community Development Block Grant awards; and Section 108 lending awards).

[120] *See, e.g.*, Todd Spangler, *Congress Approves at Least $120M for Flint Water Fix*, USA TODAY (Dec. 10, 2016, 8:04 AM), http://www.freep.com/story/news/local/michigan/flint-water-crisis/2016/12/10/congress-flint-water-funding/95243816/.

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Third, numerous studies have drawn attention to the drag on regional economies and the national economy as a whole caused by the isolation of both poor and minority residents in disinvested housing markets. Economists have linked this type of residential segregation to impaired economic growth across United States metropolitan areas due to isolated residents' underperformance in the economy[121] and reduced per capita incomes and educational attainment.[122] It is also linked to inefficiencies in regional residential development caused by trying to stabilize pockets of distress and the sprawling residential development that ensues from those fleeing to avoid those pockets.[123] In these ways, the problem of disinvested housing markets is a problem for the entire economy.

As a counterpoint to these first three rationales, some contend that the better policy is to simply provide avenues for those who live in disinvested communities to move to places with better opportunities.[124] While the debate over whether to focus on the development of places versus people is vigorous and ongoing, relying entirely on either approach is unrealistic.[125] There are several critical realities that stand in the way of wholescale abandonment of disinvested communities in favor of thriving ones, including social structures that impair movement,[126] capacity and affordability constraints in thriving economic areas,[127] and the legacy and lost sunk costs associated with simply abandoning communities.

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[121] Huiping Li, Harrison Campbell & Steven Fernandez, *Residential Segregation, Spatial Mismatch and Economic Growth Across US Metropolitan Areas*, 50 URB. STUD. 13 (2013).

[122] *See* GREGORY ACS ET AL., THE COST OF SEGREGATION: NATIONAL TRENDS AND THE CASE OF CHICAGO, 1990–2010, at ix (2017).

[123] *See, e.g.*, David M. Cutler & Edward L. Glaeser, *Are Ghettoes Good or Bad?*, 112 Q.J. ECON. 827 (1997).

[124] *See, e.g.*, Louis Winnick, *Place Prosperity v. People Prosperity: Welfare Considerations in the Geographic Redistribution of Economic Activity*, Real Estate Research Program, UCLA, Essays in Urban Land Economics and Honor of the 65th Birthday of Leo Griebler 273–83; Edward Glaeser, *Can Buffalo Ever Come Back?*, N.Y. SUN (Oct. 19, 2007), https://www.nysun.com/opinion/can-buffalo-ever-come-back/64879/.

[125] *See, e.g.*, Randall Crane & Michael Manville, *People or Place? Revisiting the Who Versus the Where of Urban Development*, LAND LINES 2–4 (July 2008).

[126] *Id.* at 7.

[127] *Id.*

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Finally, the Nash equilibrium cited by proponents of Opportunity Zones applies with at least equal force as it relates to disinvested housing markets.[128] A simple illustration follows. In a neighborhood experiencing disinvestment, current homeowners face choices as to whether to invest in their homes, while prospective new homeowners must decide whether to purchase there or somewhere else. If a critical mass invested in homes in the neighborhood, declines in neighborhood property values might be avoided and even reverse course. But the odds of any one homeowner or purchaser getting a return on her investment decreases significantly if no one else follows suit. The uncertainty of what others will do can lead to a "bad" Nash equilibrium, where everyone refrains from investing to minimize their losses because they do not see evidence of anyone else investing. Decline becomes inevitable. Public subsidization of home investments could signal a more favorable climate for investment and aid a turnaround.

C. Current Homeowner Subsidies

As a general matter, American governments at all levels subsidize homeownership. This is because homeownership is widely viewed as a good investment for the homeowner, as reducing the homeowner's dependence on the government, and also as creating spillover benefits for those who live around the homeowner (i.e., "positive externalities").[129] Governmental support of homeownership takes various forms, and some of the most popular include: underwriting credit markets that provide home mortgages, homeownership counseling programs, and, most pertinent to this Article, individual homeowner subsidies. Direct homeowner subsidies from government usually come in the form of tax breaks. The two most common sources are the federal government and local (in the case of cities, municipal) governments.

1. Federal Income Tax Subsidies

Historically, Congress has been very generous to homeowners. The federal income tax code provides an array of tax breaks to homeowners, three of which merit discussion here as by far the most commonly used and the most expensive. These are the mortgage interest deduction, the property tax deduction, and the exclusion

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[128] Housing scholars have utilized game theory similarly to explain change in declining neighborhoods. *See, e.g.*, Mark Granovetter, *Threshold Models of Collective Behavior*, 83 AM. J. SOC. 1420 (1978); RICHARD P. TAUB ET AL., PATHS OF NEIGHBORHOOD CHANGE 156–57 (1984); Galster, *supra* note 115, at 13–17.

[129] *See, e.g.*, Edward L. Glaeser & Jesse M. Shapiro, *The Benefits of the Home Mortgage Interest Deduction* 22–24 (Nat'l Bureau of Econ. Research, Working Paper No. 9284, 2002).

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from taxation of home sale gains.[130] Generally speaking, a homeowner may choose to deduct from her federal taxable income the interest she pays on a mortgage she takes out to purchase, construct or substantially improve her home.[131] She may also choose to deduct the property tax she pays on the home.[132] The property tax deduction is part of a larger deduction available for most state and local taxes ("SALT").[133] Furthermore, when she sells her home she often does not have to pay tax on her gain.[134]

All three of these income tax subsidies are subject to limitations and caps of various forms. Most significant is that the mortgage interest deduction and SALT are itemized deductions, which means they are only of value to those taxpayers whose total itemized deductions exceed the standard deduction that the tax code otherwise automatically provides to all taxpayers.[135] Via the TCJA, the same tax reform bill that created Opportunity Zones, Congress approximately doubled the size of the standard deduction, significantly reducing the number of taxpayers who will find it advantageous to itemize their home mortgage interest and SALT.[136] And, for those who will still find it advantageous, the TCJA reduced the amounts of both of these items that they can deduct.[137] The exclusion of home sale gains survived the TCJA intact, but it is subject to its own statutory caps on the amount of gain that can be excluded and other limitations.[138] Nevertheless, the three principal tax breaks still

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[130] *See* Michael Novogradac, *Confirmed, Again: Cost of Community Development Tax Incentives Is Comparatively Small*, NOVOGRADAC (June 22, 2018, 12:00 AM), https://www.novoco.com/notes-from-novogradac/confirmed-again-cost-community-development-tax-incentives-comparatively-small (analyzing the federal tax code's tax expenditures and identifying these three as by far the largest Housing Tax Expenditures for Homeownership, amounting to a combined annual average of $93.5 billion in forgone tax revenue for years 2017–2021).

[131] I.R.C. § 163(h) (2018).

[132] *Id.* § 164.

[133] *Id.*

[134] *Id.* § 121.

[135] *Id.* § 63(c).

[136] Tax Cut and Jobs Act of 2017, Pub. L. No. 115-97, § 11021, 131 Stat. 2054 (2017).

[137] For mortgage debt incurred after December 15, 2017, Section 11043 limited the amount of mortgage interest that may be deducted to the interest paid on the first $750,000 of mortgage debt. *Id.* § 11043. It also eliminated the interest deduction for new or existing home equity debt. *Id.* Section 11042 capped the itemized deduction for state and local income, sales, and property taxes at $10,000. *Id.* § 11042. Each of these provisions expires on December 31, 2025. *Id.* §§ 11042(a), 11043(a).

[138] I.R.C. § 121.

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represent a substantial federal investment in homeownership. Over the next five-year period, they are projected to cost the federal government more than $93 billion per year in forgone revenue,[139] far in excess of what Congress allocates to both federal housing programs through the Department of Housing and Urban Development and other targeted investments in disinvested communities combined.[140]

Ostensibly, these subsidies are meant to be broadly available to homeowners and to increase accessibility to homeownership.[141] If this were true, the subsidies would be claimed by a significant percentage of those who own a home and, in particular, those who face financial constraints to owning one. Even prior to the TCJA, a phalanx of economists, policy makers, and academics skewered the deductions on mortgage interest and SALT on both grounds.[142] Historically, less than 30% of American taxpayers—most of them in the top income brackets—have found it worthwhile to itemize deductions limiting the benefits of the deductions to those who are higher income.[143] The changes made by the TCJA have only exacerbated this. Estimates of the percentage of taxpayers who would itemize in 2018, the first year following the TCJA, vary but typically hovered around 10%.[144] Furthermore, those who will itemize will represent an even wealthier slice of American taxpayers.[145] Because wealthy people tend to live among others who are wealthy,[146]

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[139] Novogradac, *supra* note 130.

[140] *Id.*

[141] *See* Rossman, *supra* note 15, at 213–14.

[142] *See, e.g.*, Andrew Hanson, *Size of Home, Homeownership and Mortgage Interest Deduction*, 21 J. Hous. Econ. 195 (2012); Jeremy Horpedahl & Harrison Searles, *The Home Mortgage Interest Deduction*, Mercatus Ctr.: Mercatus on Pol'y Series (Jan. 8, 2013), https://www.mercatus.org/publication/home-mortgage-interest-deduction; Dean Stansel & Anthony Randazzo, *Unmasking the Mortgage Interest Deduction: Who Benefits and by How Much? 2013 Update*, Reason Found. (Dec. 18, 2013), http://reason.org/news/show/mortgage-interest-deduction-benefit.

[143] *See* Benjamin H. Harris et al., *New Perspectives on Homeownership Tax Incentives*, *in* Tax Notes 1318–19 (2013), https://www.taxpolicycenter.org/publications/new-perspectives-homeownership-tax-incentives/.

[144] *See, e.g.*, Tax Policy Center, T18-0001—Impact on the Number of Itemizers of H.R.1, The Tax Cuts and Jobs Act (TCJA), By Expanded Cash Income Level, 2018 (2018), https://www.taxpolicycenter.org/model-estimates/impact-itemized-deductions-tax-cuts-and-jobs-act-jan-2018/t18-0001-impact-number.

[145] *See* Emily Cauble, *Itemized Deductions in a High Standard Deduction World*, 70 Stan. L. Rev. Online 146, 146 (2018).

[146] *See, e.g.*, Albouy & Zabek, *supra* note 12; *see also* Tankersley & Mellnik, *supra* note 12.

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the beneficiaries of the mortgage interest deduction and SALT will also be even more heavily concentrated in wealthy communities where housing markets are already robust.

The exclusion of gains on home sales can be claimed by most taxpayers who realize a gain when selling their homes.[147] However, it also turns out to be slanted towards higher-income taxpayers and higher-income communities and of significantly less value to disinvested housing markets. Those with very high incomes pay the capital gains tax at a higher rate and so they also tend to receive a larger tax break.[148] Furthermore, wealthier taxpayers tend to own more expensive homes, which, all other factors equal, generate larger gain.[149] Finally, as noted above, wealthier homeowners tend to live in more exclusive and wealthier neighborhoods, where home values appreciate at greater rates and homeowners receive larger amounts of tax-free gain upon re-sale.[150]

Apart from the fact that the benefits of these tax breaks accrue largely to upper income households rather than those financially constrained from purchasing a home, I have previously criticized the federal homeowner subsidies for another serious flaw.[151] The federal tax code rewards homeowners at large, at least in concept. This stems from an overly simplistic presumption that only good things happen when someone decides to invest in a home. In fact, homeowner decisions can also impose costs on others (i.e., "negative externalities"). These include choices that, among other things, serve to disinvest less well-off communities, heighten economic and racial housing segregation, increase environmental degradation, and locate homeowners in environmental hot spots setting the table for publicly funded bailouts.[152]

By providing tax subsidies to homeowners without regard to the varying amounts of positive and negative externalities their decisions create, the homeowner subsidies are often socially inefficient and work at cross purposes with other

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[147] I.R.C. § 121 (2018).

[148] *Id.* § 1(h); *Topic Number: 409—Capital Gains and Losses*, IRS: TAX TOPICS, https://www.irs.gov/taxtopics/tc409.

[149] *See* Harris et al., *supra* note 143, at 1315, 1319.

[150] *Id.*; Tankersley & Mellnik *supra* note 12.

[151] Rossman, *supra* note 15.

[152] *Id.* at 218, 226, 232–33.

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government policies that seek to remedy negative housing externalities.[153] As it relates to disinvestment and residential segregation specifically, the current federal subsidies actually fuel homeowner decisions that tend to worsen these conditions because the benefits of the tax breaks are typically most fully realized by avoiding struggling places and purchasing in well off and exclusive communities.[154]

I have proposed that the federal government design and adopt "smarter" homeowner subsidies that more narrowly target homeowner decisions that result in greater net societal benefit—for example, those that counter disinvestment and segregation, or at least do not exacerbate these conditions.[155] At the same time, I recognized the daunting challenge of crafting policy at the federal level that tries to tackle multiple housing externalities that vary, sometimes dramatically, across and within thousands of different localized housing markets.[156]

2. Local Tax Abatement

The principal mechanism through which local governments subsidize homeownership is local tax abatement. Abatement means a reduction in taxes a taxpayer otherwise owes.[157] It is typically offered as an inducement by a city government to a prospective or current homeowner to purchase and live in, or make renovations to, a home within that city.[158]

An ever-growing number of cities have adopted residential tax abatement policies, primarily in response to population declines and chronic disinvestment.[159] That said, there is a great deal of variety among these policies and they are becoming increasingly sophisticated. Policies vary in the percentage and type of local taxes that are abated, the length of the abatement, whether the abatement amount is uniform throughout or gradually stepped back, the types of homeowner decisions that are

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153 *Id.* at 238.

154 *Id.* at 224, 232.

155 *See id.*

156 *Id.* at 255–62.

157 *See, e.g.*, *Tax Abatement*, CITY OF CLEVELAND, OHIO, http://www.city.cleveland.oh.us/CityofCleveland/Home/Government/CityAgencies/CommunityDevelopment/TaxAbatement (last visited Apr. 18, 2019).

158 *Id.*

159 Mark S. Rosentraub et al., *Residential Property Tax Abatements and Rebuilding in Cleveland, Ohio*, 42 ST. & LOC. GOV'T REV. 104, 104 (2010).

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eligible for abatement (e.g., new construction, substantial rehabilitation, exterior renovations), and whether the abatement is available throughout the city or only in certain neighborhoods.[160] Cities sometimes alter their policies over time based on their effectiveness or due to changes in the market place. For example, Cleveland, Ohio has modified its policy multiple times to increase its value and to include substantial exterior renovations of existing homes.[161] Columbus, Ohio recently changed its policy to exclude certain neighborhoods where the housing market had recovered to the point where abatements no longer seemed necessary.[162] With recent exponential advances in the quantity and sophistication of real estate market data, cities are often hiring property market experts to consult on how to best target their policies to get the maximum bang for their buck.[163]

As described above, local tax abatement polices are unquestionably more sensitive to homeowner externalities than the existing federal homeowner tax breaks. In fact, local policies are not really sold as increasing home affordability. Rather, local governments primarily view them as ways to attract new investment and expand the tax base within municipal boundaries in order to offset and ultimately reverse the human, social, and economic costs associated with deteriorating neighborhoods.[164] Some cities design their policies to address other housing externalities as well. For example, Cleveland requires that properties meet green building standards in order to be eligible for tax abatement,[165] while Cincinnati offers additional incentives for doing so.[166] However, combatting disinvestment is at the core of these policies.

Because homeowner subsidies are externality-sensitive and capable of being carefully tailored and periodically refined to match the unique dynamics and needs of localized housing markets, local tax abatement policies meet some important

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[160] *See id.* at 106.

[161] *Id.*

[162] Brent Warren, *City Unveils New Policy for Incentives and Tax Abatements*, COLUMBUS DISPATCH (Jan. 28, 2018), https://www.columbusunderground.com/city-unveils-new-policy-for-incentives-and-tax-abatements-bwl.

[163] *See, e.g.*, HR&A & VSI SPECIALISTS, INCENTIVES POLICY EVALUATION, FINAL REPORT (2017), https://www.columbus.gov/WorkArea/DownloadAsset.aspx?id=2147498426.

[164] Rosentraub et al., *supra* note 159, at 104.

[165] CITY OF CLEVELAND, *supra* note 157.

[166] *Transforming a City One Home at a Time*, U.S. Green Bldg. Council, https://www.usgbc.org/sites/default/files/transforming-a-city.pdf (last visited Apr. 8, 2019).

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criteria of what I consider to be smarter homeowner subsidies. At the same time, some question whether tax abatement is effective at achieving its desired result of combatting disinvestment.[167] This is, of course, an important question. Unfortunately, research on the effectiveness of residential tax abatement is relatively limited. What does exist suggests that tax burdens are a factor homeowners consider in home investment decisions[168] and that, if appropriately calibrated, tax abatement can cause home purchasers and homeowners to invest in disinvested communities when they otherwise would not.[169] This is not, however, a guarantee that disinvestment trends will be reversed or that desired neighborhood outcome measures will be achieved.[170] Success turns on a variety of circumstances related to the condition of the market one seeks to affect, the design and monitoring of the subsidy, the length of time it is in place, and its coordination with other efforts to combat disinvestment.[171]

D. The Case for a Federal Homeowner Subsidy to Combat Disinvestment

Assuming, *arguendo*, that local policy makers are capable of identifying those markets in which tax subsidies can encourage homeowner decisions that will effectively combat disinvestment and can accurately calibrate the subsidies to spur this behavior, should not local tax abatement be the answer? Why not leave "smarter" homeowner subsidies to local governments, which are presumably more knowledgeable about local housing conditions? I will offer here three reasons why a federal homeowner subsidy has some significant advantages.

The first is resources. Any local government faces constraints on how much taxable revenue it can forgo in the short-term and, thus, on the size and scope of an abatement program it can undertake. Particularly constrained are the very communities that are compelled to offer tax abatements to induce investment. They typically have decreasing property values, poorer populations, and shrinking local

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[167] *See, e.g.*, Doreen Swetkis, Residential Property Tax Abatement: Testing a Model of Neighborhood Impact 1 (Dec. 2009) (unpublished Ph.D. dissertation, Cleveland State University) (on file at http://engagedscholarship.csuohio.edu/cgi/viewcontent.cgi?article=1285&context=etdarchive).

[168] Erik B. Johnson & Randall Walsh, *The Effect of Property Taxes on Location Decisions: Evidence from the Market for Vacation Homes* 2 (Nat'l Bureau of Econ. Research, Working Paper No. 14793, 2009).

[169] *See, e.g.*, THOMAS BIER ET AL., CLEVELAND'S RESIDENTIAL TAX ABATEMENT STUDY: ITS IMPACT, EFFECTS AND VALUE i–xi (2007).

[170] Swetkis, *supra* note 167.

[171] Rossman, *supra* note 15, at 252–53.

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tax bases and, thus, need tax abatement to attract and retain homeowners.[172] Affluent communities with robust housing markets (i.e., those with the resources to actually afford tax abatement), can attract homeowners without it. Resource constraints on local government in many disinvested communities have only increased in recent years as state governments across the country have pursued budget austerity initiatives that have shrunk cash transfers to local governments, disproportionately impacting those communities with larger social service and infrastructure costs.[173]

By comparison, the federal government can spread the cost of disinvestment subsidies across a much broader tax base, as it draws revenue from both affluent and non-affluent communities. Even with the rollback of the mortgage interest deduction and the property tax deduction via the TCJA, the federal government still plans to forgo over $93 billion annually in tax revenue on homeowner subsidies that inure primarily to the benefit of wealthy homeowners and robust housing markets.[174] Bringing to bear just a portion of the forgone revenue from the current federal homeowner subsidies could make a sizeable impact on disinvested housing markets without drawing from their already stressed municipal budgets.[175]

The second reason involves tax equity. A principal criticism of local tax abatement programs is that they are inequitable in that they forgo tax dollars that would otherwise fund schools, municipal services, infrastructure, and neighborhood revitalization projects and put that money in the hands of private homeowners, who are typically more affluent than the average resident of a disinvested community.[176] Opponents of this criticism would counter that effectively designed tax abatements

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[172] *See, e.g.*, CITY OF AKRON, *Planning to Grow Akron*, https://www.akronohio.gov/cms/site/5184b0720f880d29/index.html (recommending Akron adopt property tax abatement as part of a comprehensive strategy to increase the supply of marketable, market-rate housing in the city, to attract residents with middle to high incomes, to reverse Akron's gradual decline in population and to grow the City's tax base).

[173] *See, e.g.*, Rich Exner, *Ohio Tax Changes Under Gov. John Kasich Leave Villages, Cities Scrambling to Cope with Less*, CLEVELAND.COM (Mar. 9, 2016), https://www.cleveland.com/datacentral/2016/03/ohio_tax_changes_under_gov_joh.html.

[174] Novogradac, *supra* note 130; *supra* notes 141–50 and accompanying text.

[175] Interestingly, the proponents of the Opportunity Zones program proclaim it will make a transformative impact on economically distressed communities with only $1.6 billion annually in forgone tax revenue. Tankersley, *supra* note 4.

[176] *See, e.g.*, Robert W. Wassmer, *Property Tax Abatement as a Means of Promoting State and Local Economic Activity*, *in* EROSION OF THE PROPERTY TAX BASE: TRENDS, CAUSES, AND CONSEQUENCES, LINCOLN INSTITUTE OF LAND POLICY 221 (Nancy Y. Augustine et al. eds., 2009).

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do not forego tax revenue if the activity they induce would not have occurred within that government's municipal boundaries but for the abatement.[177]

Whichever side of this argument one comes down on, it is true that government costs are borne by those who pay taxes and, therefore, those who receive an abatement are benefiting from schools, roads, and services that they are not paying for (or at least not in an equal share). Accordingly, a disproportionate share of the local government's costs is instead borne by those who previously lived within its boundaries or have not substantially renovated their homes (depending on the activity the tax abatement targets). Given that abatements are typically offered in disinvested communities, this can mean that lower income residents are paying for the civic expenses of those with newer and nicer homes and higher incomes who were attracted by the abatement. Again, a federal homeowner subsidy would spread its cost across the country and, on average, over a more affluent tax base.

The third reason for a federal homeowner subsidy aimed at combatting disinvestment, interestingly enough, circles back to a purported rationale for the current federal homeowner subsidies—that is, accessibility to homeownership. One of the principal concerns voiced in connection with revitalizing disinvested housing markets is that, if successful, home costs will rise and become out of reach for its current residents.[178] This phenomenon, known as gentrification, has occurred in other revitalized housing markets, although not always at the scale it is perceived or feared.[179] Nevertheless, it presents a conundrum for those on the local level who craft abatement policies, the very objective of which is to restore functioning housing markets in places suffering market distress. Creating these abatement policies requires thinking past the day when the housing market will function again and planning for those who might struggle to live within that market and, thus, contribute less to meeting the city's financial bottom line.

A financially enticing, but selectively available, federal homeowner subsidy could help to ensure that baseline protections for housing affordability are part of the planning process for any community that wishes to be eligible for the subsidy. Congress could leverage this subsidy to encourage a focus on and perhaps even innovation in local community planning. Furthermore, given the experience it has gained in administering other programs that require fair housing planning, the federal

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[177] *See, e.g.*, Nathan B Anderson, *Commentary to Property Tax Abatement as a Means of Promoting State and Local Economic Activity*, *in* EROSION OF THE PROPERTY TAX BASE: TRENDS, CAUSES, AND CONSEQUENCES, LINCOLN INSTITUTE OF LAND POLICY 111 (Nancy Y. Augustine et al. eds., 2009).

[178] *See, e.g.*, MALLACH, *supra* note 105, at 116–17.

[179] *Id.*

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government could offer expertise and resources to those communities seeking to engage in this type of planning. This is a point that this article will elaborate on further in Part IV.

III. A HOMEOWNER ANALOGUE TO OPPORTUNITY ZONES

So, what would a federal homeowner subsidy analogous to the tax breaks offered through the Opportunity Zones program (a "homeowner analogue") look like? If sticking close to the Opportunity Zone model, it would mean something conceptually similar in terms of the underlying aim, tax benefit, zone selection process, and operational structure. At the same time, there are structural differences between home and business investments, as well as distinct strategies for combatting housing versus economic disinvestment that should be taken into account.

Before getting too deep into the weeds, it probably helps to clarify what types of places a homeowner analogue would look to assist and what specific problem it would seek to solve. The Opportunity Zones program seeks to unblock the flow of capital for business activity in strategically selected communities suffering from chronic economic disinvestment. A homeowner analogue would aim to do likewise for homeowner investment in strategically selected disinvested housing markets.

It is also important to acknowledge upfront the difficulty of creating a housing market typecast (like "disinvested") that applies across the country. Housing market narratives, in certain respects, seem as plentiful as the number of housing markets. Even the most cursory glimpse across the country shows high-density cities that struggle with affordability,[180] post-industrial Rust Belt regions with vast inventories of antiquated and abandoned homes,[181] coastal areas with housing at risk of rising tides,[182] emerging Southwestern markets where limited natural resources are stretched by new growth,[183] and lots of variation in between.

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[180] *See, e.g.*, EDWARD L. GLAESER & JOSEPH GYOURKO, RETHINKING FEDERAL HOUSING POLICY 142–71 (2008), http://www.aei.org/wp-content/uploads/2014/03/-rethinking-federal-housing-policy_101542221914.pdf.

[181] *See, e.g.*, Ford, *supra* note 100, at 16.

[182] *See, e.g.*, Coral Davenport & Campbell Robertson, *Resettling the First American 'Climate Refugees,'* N.Y. TIMES (May 6, 2016), https://www.nytimes.com/2016/05/03/us/resettling-the-first-american-climate-refugees.html; *see also* Robert Freudenberg et al., *Buy-in for Buyouts*, LINCOLN INST. 27 (July 2016), https://www.lincolninst.edu/sites/default/files/pubfiles/buy-in-for-buyouts-0716ll.pdf.

[183] N. Light Prods. & Lincoln Inst. of Land Policy, *Making Sense of Place–Phoenix, The Urban Desert*, YOUTUBE (Mar. 15, 2013), https://www.youtube.com/watch?v=y0qOD0l9dbQ.

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And yet, as with economic disinvestment, there are common hallmarks of chronic housing disinvestment. Most prominent are census tracts that have both high poverty rates and depressed median property values relative to the metropolitan areas in which they are located.[184] An aging housing stock, a higher than average property vacancy rate, lower levels of homeownership and home rehabilitation activity, and dysfunctional home sale activity are further evidence.[185] In the later stages of entrenched housing market disinvestment, long-term consequences manifest, like a prevalence of housing related environmental hazards and home demolitions, and local government experiencing a fiscal crisis due to serious decreases in property tax revenue.[186]

A distinguishing feature of the Opportunity Zones model is that it does not include all areas experiencing disinvestment. Rather, it required states to select those census tracts possessing the best combination of opportunity and need—or, to put it in game theory terms, census tracts where a disruption in a bad Nash equilibrium can make the biggest difference. If designing something comparable is the goal, a homeowner analogue should likewise require states to choose among their disinvested housing markets and submarkets. A disinvested market's proximity to strong markets, or those undergoing a revitalization, and to other amenities and competitive strengths would be pluses. Also useful would be the presence of other public sector or philanthropic interventions in the market that could be leveraged with a targeted federal tax break. On the other hand, those selected should be housing markets that need a spark that is elusive and where the positive impact of the spark on its residents would be substantial. At this point, it should help to depart from the purely theoretical realm and introduce a real example of a place that fits this description, both to add context and explore how private market actors think about these places. With a point of reference in place, Part III will then go further into other design features of the homeowner analogue.

A. Glenville—Portrait of a Disinvested Community

The Glenville neighborhood in Cleveland, Ohio is in many ways the classic story of Rust Belt community disinvestment. Sitting five miles east of downtown Cleveland, it transitioned during the early 1900s from a quiet and affluent lakeside

[184] Neighborhood Homes Inv. Act Coal. Ohio, Neighborhood Homes Tax Credit (July 20–21, 2017), https://www.dropbox.com/s/048w8v0mygpihmt/NHTC_Ohio_presentation_FINAL.pdf?dl=0.

[185] *See generally* Rossman, *supra* note 15, at 218–23.

[186] *Id.*

community to a bustling city neighborhood.[187] Residents were drawn to its vibrant business and retail blocks, places of worship, and array of well-built and distinctive homes.[188] By mid-century, the population of Glenville began to change quickly in a way that reflected larger metropolitan trends. Over three decades, the neighborhood's largely Jewish population moved to adjacent eastern suburbs and the city's growing African American population replaced it.[189]

Marginalized by a changing post-World War II economy that pushed better paying jobs to outer-lying suburban areas, at the same time as governmental housing policies and entrenched racial discrimination prevented African American residents from moving there to obtain them, the new residents of Glenville were considerably poorer than their predecessors.[190] This set into motion a long decline in the neighborhood's physical condition, including its housing stock.[191] Declining conditions and housing trends continued to drive out neighborhood residents with more resources and drive away new prospective homebuyers, preventing the infusion of new waves of home investment. Glenville's long descent was accelerated by last decade's foreclosure crisis, which hit communities that were low-income and primarily minority particularly hard.[192] Subprime mortgages infested the

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[187] Encyclopedia of Cleveland History: Glenville, CASE W. RES. U., https://case.edu/ech/articles/g/glenville (last visited May 25, 2019).

[188] Garth Holman, *Glenville Riots*, YOUTUBE (Apr. 27, 2009), https://www.youtube.com/watch?reload=9&v=BPYmQ0AxgC0.

[189] Encyclopedia of Cleveland History, *supra* note 187.

[190] David M. Swiderski, Approaches to Black Power: African American Grassroots Political Struggle in Cleveland, Ohio, 1960–1966 (Sept. 2013) (unpublished Ph.D. dissertation, University of Massachusetts Amherst) (on file at https://scholarworks.umass.edu/cgi/viewcontent.cgi?article=1849&context=open_access_dissertations).

[191] For a discussion of the downward trajectory of Glenville and other similarly situated Cleveland neighborhoods, *see, e.g.*, Carol Poh Miller & Robert A. Wheeler, *Cleveland: The Making and Remaking of an American City, 1796–1993*, *in* CLEVELAND: A METROPOLITAN READER 42–45 (William Dennis Keating et al. eds., 1995).

[192] *See, e.g.*, Peter Dreier et al., *Underwater America Underwater America: How the So-Called Housing "Recovery" is Bypassing Many Communities*, HAAS INST. 6 (2014), http://haasinstitute.berkeley.edu/sites/default/files/haasinsitute_underwateramerica_publish_0.pdf; *The State of the Nation's Housing 2018*, JOINT CTR. FOR HOUS. STUD. OF HARV. U., 31–32 (2014), https://www.jchs.harvard.edu/sites/default/files/Harvard_JCHS_State_of_the_Nations_Housing_2018.pdf (asserting that price drops as a result of the Foreclosure Crisis were three times greater in minority neighborhoods than in white neighborhoods).

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neighborhood and led to concentrated numbers of foreclosures.[193] This literally caused the bottom to fall out of Glenville's housing market, reducing median home sale prices by a shocking 95% from its pre-foreclosure crisis peak to the low point of the crisis.[194]

At present, the median Glenville home price sits at only 21% of its pre-foreclosure crisis peak.[195] Other indicators of chronic disinvestment abound—approximately 27% of its homes are delinquent on property taxes, 17% of its buildings are vacant, and over 10% of all of its standing structures received a "D" or "F" in a recent city-wide property inventory study, indicating they are in such bad shape that they should simply be demolished.[196] These housing conditions provide a nexus to Glenville's unusually high child lead exposure levels, poorly performing schools, high poverty rate, and shorter resident life expectancy.[197]

Meanwhile, Glenville abuts University Circle, one of Cleveland's most prosperous neighborhoods. The Circle is home to Case Western Reserve University, three hospitals (including the world-renowned Cleveland Clinic), and many of Cleveland's finest arts institutions.[198] While Glenville has cratered, University Circle has seen $3.65 billion in new development in the last fifteen years.[199] This has included large expansions by its "eds and meds" institutions, a significant uptick in jobs, strategic public transit investments, and private development of new town houses and even high rise apartment buildings.[200]

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[193] Frank Ford, *Housing Market Recovery in Cuyahoga County: Race and Geography Still Matter*, W. RESERVE LAND CONSERVANCY 35 (July 30, 2018), https://www.wrlandconservancy.org/wp-content/uploads/2018/07/Cuyahoga-Housing-Trends_7-30-18.pdf.

[194] *Id.*

[195] *Id.*

[196] *Cleveland Neighborhoods by the Numbers*, CASE W. RES. U. (Aug. 22, 2016), https://www.wrlandconservancy.org/wp-content/uploads/2016/08/ClevelandPropertyInventory_issuu .pdf.

[197] *See, e.g.*, *Exploring the Relationship Between Vacant and Distressed Properties and Community Health and Safety*, CASE W. RES. U. (June 5, 2017), https://case.edu/socialwork/sites/case.edu.socialwork/files/2018-10/vacant_distressed_props_comm_health_safety.pdf.

[198] *See* U. CIRCLE, INC., https://www.universitycircle.org/history (last visited May 16, 2019).

[199] *University Circle Becomes Second Downtown, Attracting New Residents and Billions in Investment*, CLEVELAND 2016 HOST COMMITTEE, https://www.2016cle.com/working-in-cleveland/more-working-in-cleveland/university-circle-becomes-second-downtown-attract (last visited May 25, 2019).

[200] *Why University Circle?*, U. CIRCLE, INC., https://www.universitycircle.org/work/why-university-circle (last visited May 16, 2019).

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With all of the nearby momentum, why has Glenville's housing market not turned around? Private capital has been slow to enter. Conventional banks and lending institutions reject mortgage applications in Glenville at a very high rate.[201] Bank lending practices, like refusing to lend to owners of low value properties, of which Glenville has lots, restrains an important form of homeowner capital.[202] Banks also have a legacy of discrimination against prospective African American borrowers, which hinders the potential for a housing market rebound in predominantly African American communities like Glenville.[203] It would be naïve to not also acknowledge the entrenched biases and concerns higher and middle income homeowners have about purchasing in African American neighborhoods, in general,[204] and the Glenville neighborhood, in particular, stemming from racial tension and riots in the late 1960s.[205]

More broadly, conditions in Glenville's housing market have led to the perception that it is simply a bad value proposition. Housing market commentators have long debated how homeowners and prospective home buyers bundle a community's level and quality of public goods, tax rates, quality of life factors, and likely return on investment into their decisions.[206] Yet abundantly clear is that a home's total value proposition is a significant factor.[207] Glenville sits in a high tax city,[208] where important public goods, like the school system, are subpar, quality of life challenges abound, and the return on housing investment, especially in recent years, is terrible.[209] Because each of these conditions emanate to a significant degree from disinvestment, we can think of this as a "disinvestment penalty" that hinders

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[201] Michael Lepley & Lenore Mangiarelli, *Cuyahoga County Mortgage Lending Patterns*, FAIR HOUSING CTR. FOR RTS. AND RES. (July 2018), http://www.thehousingcenter.org/wp-content/uploads/2018/07/Cuyahoga-County-Mortgage-Lending-Patterns-2018-BEST-FOR-PRINT.pdf.

[202] *Id.* at 4.

[203] *See, e.g.*, Monique W. Morris, *Countering Discrimination and Mortgage Lending in America*, NAACP (Apr. 2010), https://naacp.org/wp-content/uploads/2016/04/Countering_Lending_Discrimination.pdf.

[204] Squires, *supra* note 113; RUSK, *supra* note 113.

[205] *See* Holman, *supra* note 188.

[206] *See generally* Charles Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416 (1956).

[207] *Id.*

[208] Rich Exner, *Cuyahoga County's Highest City Income Tax Rates*, CLEVELAND.COM (Feb. 2, 2016), https://www.cleveland.com/datacentral/index.ssf/2016/02/cuyahoga_countys_highest_city.html.

[209] *See supra* notes 189–94 and accompanying text.

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home investment in Glenville. This penalty has been difficult to dislodge or overcome, notwithstanding the neighborhood's advantageous location.

Recognizing its advantageous location, as well as the potentially transformative effect that improving the housing market could have on both Glenville residents and the city as a whole, several local stakeholders are working to attract homeowners to the neighborhood. A coalition of University Circle's nonprofit institutions have created a forgivable loan program to encourage their workers to live in surrounding neighborhoods, with modest success.[210] The City of Cleveland recently chose a portion of Glenville that sits close to University Circle, and which the city has rebranded "Circle North," as the first location for its ambitious Neighborhood Transformation Initiative ("NTI").[211] NTI will use a combination of city bond proceeds and bank and philanthropic capital to help fund the construction of a modest number of new single family homes (as infill on vacant lots that resulted from demolitions), the construction of a new mixed-use, mixed-income development on a prominent neighborhood corner, and a home buyer and current homeowner loan program for home purchases and qualified improvements.[212] Cleveland commissioned a report by Cleveland State University's Levin College of Urban Affairs to inform its selection of neighborhoods for NTI, and the report recommended Circle North as a strong candidate because of its proximity to anchor institutions and to an appreciating housing market.[213] In addition, several University Circle institutions have collaborated with the city to alter the neighborhood's landscape to invite access from adjoining neighborhoods like Glenville, with some visually dramatic results.[214] The seeds of new development and some nascent

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[210] *What is Greater Circle Living?*, GREATER CIRCLE LIVING, https://greatercircleliving.org/ (last visited May 16, 2019).

[211] Frank G. Jackson, *Mayor Frank G. Jackson's Neighborhood Transformation Initiative: Partnership to Stop Decline, Stabilize, and Secure the Future Growth of Cleveland Neighborhoods*, CLEVELAND CITY COUNS., https://www.clevelandcitycouncil.org/ClevelandCityCouncil/media/CCCMedia/Documents/557-17-Neighborhood-Transformation-Initiative.pdf (last visited May 17, 2019).

[212] *Id.*

[213] Richey Piiparinen et al., *Preparing for Growth: An Emerging Neighborhood Market Analysis Commissioned by Mayor Frank G. Jackson for the City of Cleveland*, CLEV. ST. U. (May 2017), https://engagedscholarship.csuohio.edu/cgi/viewcontent.cgi?article=2473&context=urban_facpub.

[214] Steven Litt, *Can University Circle's Beautiful New Nord Greenway Heal a Racial Divide?*, THE PLAIN DEALER (June 3, 2018), https://www.cleveland.com/architecture/index.ssf/2018/06/nord_greenway_is_beautiful_but.html.

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positive housing market indicators have begun to sprout, if only on the few blocks right next to University Circle.[215]

B. Design

Returning to the design features of a potential homeowner analogue to the Opportunity Zones model, a baseline question is: What type of homeowner investments would it subsidize? The crafters of the Opportunity Zones program settled upon new and patient business capital from investors realizing significant capital gains. As the program aims to attract currently unrealized capital gains off of the sidelines and into Opportunity Zones, its tax advantages only apply to investments that occur after December 31, 2017.[216] The Opportunity Zones program also seeks to attract longer term investors, rather than those looking to make a quick buck. So even though capital gain tax deferral applies to Opportunity Zone investments of any length, additional and more lucrative benefits do not begin to roll out until the investment has lasted at least five years and they continue to roll out the longer the investment continues.[217]

Of course, housing market disinvestment is not identical to economic disinvestment, and the homeowner analogue should tie to the investment needs of its target communities. A homeowner analogue could also only subsidize new investments (i.e., home purchases and significant home renovations that occur after a particular date). Local government-funded, homeowner tax abatement programs typically work this way.[218] As the trajectory of Glenville shows, however, housing market disinvestment can be as much about financially mobile homeowners pulling up their stakes and leaving disinvested markets as about prospective homeowners choosing not to enter them. Moreover, a central feature of the equity argument against local tax abatement strategies is that they reward new and often better resourced homeowners over long-time residents. So it seems sensible and fairer to craft a tax benefit that is broad enough to also encompass the decisions of current homeowners to weather the storm in disinvested housing markets.

A second critical question is what tax benefit to offer. There are several possibilities, and this Article will identify and discuss a few of them, although not with the goal of being exhaustive. To most closely resemble the tax breaks in Opportunity Zones, the homeowner analogue would provide tax breaks on capital

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[215] Piiparinen et al., *supra* note 213, at 18.

[216] I.R.C. § 1400Z-2(d)(i)(I) (2018).

[217] *See supra* notes 76–81 and accompanying text.

[218] *See supra* Part II(C)(2).

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gain resulting from home sales. Deferring and discounting capital gain tax for a homeowner who sells her current home and then purchases in a qualifying disinvested housing market would mimic closely some components of the Opportunity Zones breaks, although this benefit would not incentivize current residents to stay put and invest in their homes. Discounting, or excluding altogether, the tax a homeowner in a disinvested housing market would have to pay on the gain she realizes when she sells her home in that market after she lives in the home for a specified period of time (e.g., ten years) would reflect the other component and could encompass all homeowners.

There is a critical problem with contemplating these types of tax breaks, however, that is difficult to overcome. The federal income tax code already excludes from tax capital gain on most home sales.[219] This has not always been the case. Prior to 1997, the tax code's home sale benefit was primarily a deferral on paying capital gain tax if the homeowner invested the gain in another home purchase.[220] Since then, however, the code has provided for the full exclusion of most, if not all, of the capital gain of most taxpayers who sell their homes.[221] Reversing course and making this benefit only available for those who purchase in distressed housing markets might make strong policy sense, but would be politically very difficult to achieve, as those who sought to roll back this benefit even marginally as part of the TCJA learned.[222]

There are other options to consider. The flip side of an exclusion of capital gain from income tax is a deduction of capital loss. It is worth brief mention here how the tax code determines capital gain or loss on a home sale. Put most simply, upon sale, a taxpayer calculates her "adjusted basis" in her home (typically, what she paid for the home plus the cost of physical improvements she made to it) and subtracts the adjusted basis from the sale price.[223] If the difference is a positive number, she has capital gain, which is usually excluded from tax due to the special tax break Congress

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[219] I.R.C. § 121(a).

[220] For a brief history on the evolution of the home sale capital gain deferral to an exclusion, see Lily Kahng, *Path Dependence in Tax Subsidies for Home Sales*, 65 ALA. L. REV. 187, 191–99 (2013).

[221] I.R.C. § 121(a).

[222] *See The Tax Cuts and Jobs Act—What it Means for Homeowners and Real Estate Professionals*, NAT'L ASS'N OF REALTORS 1, 1 (Dec. 20, 2017), https://www.nar.realtor/tax-reform/the-tax-cuts-and-jobs-act-what-it-means-for-homeowners-and-real-estate-professionals (describing Senate bill's failed attempts to require longer period of home occupancy to qualify for exemption and to impose income restrictions on who could qualify).

[223] *See* I.R.C. §§ 1011(a), 1012(a), 1016(a).

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has given homeowners discussed in the previous paragraph.[224] If it is a negative number, the homeowner has a capital loss, but she cannot deduct it from her taxable income because it is assumed to reflect personal consumption.[225] A common problem for homeowners in disinvested housing markets is selling their homes for less than what they have invested in them, especially once improvements to the home are counted.[226] The prospect of a home investment losing money acts as a significant impairment to the decision to purchase or rehab.

As the analogue federal homeowner subsidy, Congress could allow homeowners in disinvested housing markets to deduct capital losses they realize when they sell their homes. This would ensure that most of these homeowners receive a tax benefit on their investment upon sale regardless of how the housing market fares—an exclusion from gain if it improves and a deduction of loss if it does not. Depending on how troubled a particular market is, a loss deduction may actually prove to be more viable for many homeowners than a gain exclusion. On the other hand, as a deduction against taxable income, the return on a loss is only equal to a percentage of the actual loss; depending on what marginal tax bracket a homeowner sits in, the value of the deduction could be as low as 10% or 12% of the loss.[227] This may not be enough of an incentive to move the needle for those on the fence. Furthermore, while a capital gain exclusion follows from success, a loss deduction feels like a consolation prize; imagine trying to promote the tax break by proclaiming "you can lose less on your home than you otherwise would have." Reminding the homeowner of the prospect of a loss in a particular housing market may mute any positive impact the tax break provides.

Another option, although one that bears less direct resemblance to the Opportunity Zone tax breaks, would be to provide homeowners in disinvested housing markets with a federal tax break aimed at reducing their local taxes. The Glenville case study brought to light the "disinvestment penalty" faced by prospective and current homeowners.[228] Maps of local tax rates in the Cleveland

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[224] *Id.* § 121.

[225] Treas. Reg. § 1.165-9(a) (1964).

[226] *See generally* Rossman, *supra* note 100 (describing the prevalence of this problem in the wake of the Foreclosure Crisis). For evidence of its present day persistence, *see, e.g.*, Ford, *supra* note 193, at 35–36; *Seriously Underwater U.S. Properties Increase From A Year Ago*, ATTOM DATA SOLUTIONS (May 7, 2019), https://www.attomdata.com/news/market-trends/q1-2019-home-equity-underwater-report/.

[227] Rev. Proc. 2018-18, 2018–10 I.R.B. 394-95.

[228] *See supra* Part III(A).

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metropolitan area make the local tax component of this penalty very clear. As a general matter, the closer one moves towards disinvested communities, like the City of Cleveland and its inner ring suburbs, the higher the local income and property tax rates.[229] A homeowner in Glenville pays these taxes at rates that are roughly double those paid by homeowners in affluent outer ring suburbs like Pepper Pike and Westlake, which have superb schools and very little poverty.[230] Discounting local taxes in disinvested housing markets via a federal tax credit equal to a percentage of those taxes would directly reduce the penalty.

Via the itemized deduction for SALT, the federal tax code actually already provides taxpayers a discount on local taxes and it is theoretically available to most taxpayers.[231] Historically, it was only claimed by the 30% of taxpayers for whom it made sense to itemize deductions and, now, post-TCJA, the increased standard deduction means only approximately 10% or so of taxpayers will itemize.[232] Those who do itemize will tend to be high-income and have valuable homes, and so it will primarily be only taxes paid in robust housing markets that will be discounted.[233] A tax credit on local taxes in qualifying disinvested housing markets would essentially create a version of SALT for those places where a bad value proposition acts as a barrier to investment. As a tax credit, rather than a tax deduction, it could be made available to almost all homeowners, regardless of what tax bracket they sit in, making it a less regressive tax break.[234]

If the tax credit was equal to a percentage of a homeowner's local taxes, it would provide a larger benefit to higher income taxpayers or those with more valuable homes. Because these homeowners contribute more revenue to the local tax base in disinvested communities, this could be a desirable outcome. The amount of the tax credit would also increase for homeowners who make improvements that increase their home values and, thus, their property taxes. Again, this is probably a good result if reversing market-wide disinvestment is the overarching goal.

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[229] Rich Exner, *Property Tax Rate per $100,000 of Home Value*, CLEVELAND.COM, http:// media.cleveland .com/datacentral/photo/northeast-ohio-property-tax-rates-2016-for-2017.png (last visited May 25, 2019); Exner, *supra* note 208.

[230] *See* Exner, *supra* note 208; Exner, *supra* note 229.

[231] I.R.C. § 164 (2018).

[232] *See supra* notes 145–48 and accompanying text.

[233] *Id.*

[234] *See generally* Lily L. Batchelder et al., *Efficiency and Tax Incentives—The Case for Refundable Tax Credits*, 59 STAN. L. REV. 23 (2010).

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In a sense, this approach represents local tax abatement funded by the federal government. Rather than hoisting the cost of abatement on the most cash-strapped local governments in disinvested communities, as it currently is, the cost would be spread across the entire federal tax base (i.e., among affluent and non-affluent communities alike). There is an element of economic justice in this because proximate to many disinvested communities are well-off communities populated to some degree by those whose housing choices put disinvestment into motion and were accelerated by a great variety of governmental policies. Furthermore, this tax credit would extend to existing homeowners in disinvested communities who do not qualify for local tax abatement; in fact, those who already receive local tax abatement would not qualify for the federal credit for that portion of their taxes that are abated because the credit would only apply to taxes paid.

Some commentators would undoubtedly contend that this type of a tax break will simply encourage local governments with residents who qualify for the tax credit to increase their tax rates and, therefore, nullify any benefit to homeowners.[235] This type of an argument makes certain assumptions about housing market inelasticity that probably do not apply in disinvested housing markets. Homeowner tax incentives might indeed become largely or fully capitalized into higher tax rates where local housing supply is limited and no other comparable housing markets exist.[236] But at the very core of housing disinvestment is that supply is not limited, and that close by and comparable (in fact, stronger) housing markets do exist—otherwise, the disinvested market would not have become disinvested. While it is certainly possible that local governments in some qualifying disinvested communities may raise taxes to an extent to meet needed services, raising taxes too much would offset the improved value proposition to homeowners provided by the tax credit and, therefore, should curb this type of response. The rest of this Article assumes a tax credit on a percentage of local taxes is the homeowner analogue tax

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[235] This argument would be similar to those contending that SALT acts as a federal subsidy for high-income, high-tax jurisdictions where taxpayers choose to have more amenities. *See, e.g.*, Jared Walczak, *A Federal Subsidy for High-Tax States and Cities Is Standing in the Way of Tax Reform*, WASH. EXAMINER (Oct. 2, 2017), https://www.washingtonexaminer.com/a-federal-subsidy-for-high-tax-states-and-cities-is-standing-in-the-way-of-tax-reform.

[236] For literature addressing similar claims about the capitalization of the mortgage interest deduction and the role of housing market elasticity in the extent to which this occurs, see Christian A. L. Hilber & Tracy M. Turner, *The Mortgage Interest Deduction and Its Impact on Homeownership Decisions*, 96 REV. ECON. & STAT. 618 (2013); Dennis R. Capozza et al., *Taxes, Mortgage Borrowing and Residential Land Prices*, *in* ECONOMIC EFFECTS OF FUNDAMENTAL TAX REFORM 171–98 (Henry J. Aaron & William G. Gale eds., 1996); Joseph Gyourko & Richard Voith, *The Tax Treatment of Housing and Its Effects on Bounded and Unbounded Communities* (Fed. Res. Bank of Phila., Working Paper No. 98–23, 1998).

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break, not only because it could serve as a meaningful incentive but also because rolling back the now broadly available home sale capital gain exclusion and limiting it only to homeowners in disinvested housing markets seems politically very difficult to achieve.

As for which housing markets could qualify for the tax break, the Opportunity Zones model provides a straightforward template.[237] Congress would need to establish threshold qualification standards. The concept of low-income census tracts borrowed from the New Market Tax Credit program has become a familiar method for establishing geographically concentrated poverty levels sufficient to qualify for federal tax breaks that encourage private investment.[238] While no measurement is perfect, a census tract, which is a statistical subdivision of a county that is smaller than a zip code and optimally includes around four thousand people, is granular enough to reflect many distinctions in market conditions that exist within metropolitan area housing markets.[239] In other words, census tracts probably come closest among existing systems of federal geographic measurements to lining up with distinct housing submarkets within larger markets.[240]

Whether a standard designed to identify if an area is low income is sufficient to establish whether it also has a disinvested housing market is debatable. Certainly, there is a great deal of overlap between poverty and housing disinvestment. However, it would probably be worthwhile to also include a measurement of property values as part of the qualifying standards. Proponents of a federal Neighborhood Homes Tax Credit, which resembles the New Market Tax Credit for housing, used a combined low-income/depressed property values standard for determining qualifying neighborhoods, which probably would be ideal in this instance.[241]

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[237] *See supra* notes 59–64 and accompanying text.

[238] I.R.C. § 45(D)(e) (2018).

[239] United States Census Bureau, *Geographic Terms and Concepts—Census Tract*, https://www2.census.gov/geo/pdfs/reference/GTC_10.pdf.

[240] There is, however, a significant body of literature questioning the utility of census tracts. *See, e.g.*, John M. Clapp & Yazhen Wang, *Defining Neighbourhood Boundaries: Are Census Tracts Obsolete?*, 59 J. URB. ECON. 259–84 (2016).

[241] Neighborhood Homes Inv. Act Coal., *supra* note 106, at 10.

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Borrowing the Neighborhood Homes Tax Credit standard, approximately one-fifth of United States census tracts would qualify as disinvested.[242] Not surprisingly, given the overlap, this is roughly equal to the percentage of census tracts that are low-income and could have qualified as Opportunity Zones. To adhere to the Opportunity Zones model, however, a homeowner analogue should require that states prioritize and select a specified percentage of the qualifying census tracts as eligible for the tax break. States would be encouraged to work with municipalities and stakeholders in communities across their boundaries to determine where the best combination of opportunity and need exists.

A neighborhood like Glenville provides a good example of the types of choices states would face. The neighborhood encompasses ten separate census tracts,[243] all of which would clearly meet the qualifying housing market disinvestment standards discussed above.[244] The census tracts representing the Circle North portion of the neighborhood are a focal point for city and philanthropic revitalization efforts.[245] They also sit right next to prospering University Circle. For these reasons, it is easy to foresee Ohio policy makers deciding that the Circle North census tracts are an ideal place for the tax break, as these housing submarkets show potential for a turnaround that a tax break could catalyze. Other parts of Glenville show less severe signs of disinvestment, sit next to park space, and have large numbers of unique, historic homes.[246] These census tracts would also be good candidates. But what of the remaining tracts? The scars of disinvestment are much more significant here and they sit further away from housing market rebounds. The input of local planners and community stakeholders would be key here, as would market data. States would face some difficult choices.

Following the Opportunity Zone model would mean that the formal role of states, cities, and communities would essentially end once the selection process is complete. The Secretary of the Treasury would review the census tract choices of the states to ensure they meet the appropriate legal standards, but after that review the tax breaks would be put in place and the choices of individual homeowners and

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[242] *Id.* at 11.

[243] *Cleveland Neighborhood Fact Sheet Glenville Statistical Planning Area*, CITY OF CLEVELAND, http://planning.city.cleveland.oh.us/census/factsheets/spa32 (last visited May 25, 2019).

[244] Neighborhood Homes Inv. Act Coal., *supra* note 106, at 14 (showing all Glenville census tracts coded as qualifying as meeting this program's median income and depressed property value criteria).

[245] *See supra* notes 210–14 and accompanying text.

[246] *Glenville*, LIVE CLEVELAND, http://livecleveland.org/glenville/ (last visited May 25, 2019).

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prospective home buyers would determine whether housing market revitalization in the selected census tracts succeeds or fails.

Administratively and structurally, a homeowner analogue should be much easier to implement than the Opportunity Zone tax breaks. Homeownership is much less complex than most of the business investments covered by the Opportunity Zones program. Presumably the homeowner analogue would reward an individual household's ownership of a principal residence. In most cases, that means a single owner (household) with a single qualifying asset. This eliminates the need for an intermediary fund, like QOFs, capable of holding the investments of multiple owners in multiple qualifying investments and, thus, many of the early complications associated with Opportunity Zones.[247] Moreover, the qualifying investment—a home purchase—is relatively easy to define and demonstrate. Many of the hundreds of pages of proposed Treasury Department regulations implementing Opportunity Zones attempt to clarify issues which are open to interpretation, like which businesses with a presence in QOZs are actually actively conducting a trade or business there, what constitutes new/qualifying business activity, and whether various highly nuanced forms of investment fall within fairly broad statutory categories.[248] While that is not to say the homeowner analogue would not result in issues of interpretation and implementation, they should be considerably more straightforward and easier to resolve.

The homeowner analogue, if adopted as a tax credit for a percentage of local taxes, could do without another complexity of the Opportunity Zone model—the five-, seven-, and ten-year holding periods required for an investor to qualify for a substantial amount of its benefits.[249] Making the tax credit immediately available to those who make a home in a selected census tract their principal residence would probably be the most sensible and impactful approach to influencing housing investment.

It is debatable whether limiting the availability of the tax credit to ten years would mimic the Opportunity Zone program, as certain of its benefits will end after December 31, 2026,[250] while others may continue until December 31, 2047.[251] But if limited to ten years, Congress would probably want to reconsider this limit if the

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[247] *See supra* note 48.

[248] *Id.*

[249] For a description of these vesting periods, *see supra* notes 76–81 and accompanying text.

[250] I.R.C. § 1400Z-2(a)(2)(B).

[251] Prop. Treas. Reg. § 1.1400Z-2(c)-1, 84 Fed. Reg. 18652 (May 1, 2019) (including investments held for at least ten years).

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homeowner analogue were a success, in particular for those housing markets where an extension of the tax credit would make good policy sense.

IV. IS THE HOMEOWNER ANALOGUE A SMARTER SUBSIDY?

As the preceding sections of this Article demonstrate, there are several well-founded rationales for a federal homeowner subsidy that combats housing disinvestment, and the Opportunity Zones model provides one plausible template for designing such a subsidy. But plausible does not necessarily mean smart. In a previous article, I examined homeowner subsidies at length, including the track record of demand-side subsidies at the local and state levels that have sought to combat disinvestment, and concluded that "smart" subsidies should satisfy several qualitative criteria.[252] They should also be externality-sensitive.[253] In other words, private market decisions are consequential for others in a variety of ways, some positive and some negative. Smart subsidy design takes account of the significant externalities resulting from the underlying activity it looks to encourage and targets those decisions that maximize societal benefit. Smart subsidies should also "pencil out" by demonstrating a return that exceeds forgone tax revenue.[254] Part IV examines the homeowner analogue to the Opportunity Zones tax breaks with these standards in mind (as well as a few additional considerations).

A. *Qualitative Criteria for Smart Subsidies*

Smart subsidies are tailored, limited, variable, and complementary.[255] What follows is a brief explanation of what each of these criteria mean, as well as a discussion of whether a homeowner analogue would satisfy it.

Tailored means "crafted to encourage behavior that squarely addresses the identified problem."[256] The homeowner analogue would be meant to combat housing market disinvestment in areas in which it is prevalent and yet where the potential for a rebound exists, by encouraging current homeowners to stay and invest in their homes and prospective home buyers to purchase in those markets. Using the design blueprint described in Part III, Section B, the specific mechanism would be a federal

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[252] Rossman, *supra* note 15, at 253–54.

[253] *Id.* at 238–41.

[254] *Id.* at 253–54.

[255] *Id.*

[256] *Id.* at 253.

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tax credit to reduce a portion of homeowners' local taxes in selected census tracts as a way of lowering their disinvestment penalty.

Homeowner tax abatement, when properly calibrated, has successfully attracted homeowner investment to certain disinvested housing markets.[257] Homeowner investment, when it achieves the proper scale, can induce housing market rebounds. A significant challenge with a federal credit would lie in achieving the right calibration, not only to actually induce homeowner investment, but also to do so across many different types of housing markets. The exact percentage of local taxes or monetary amount of the credit is an issue that policy makers would need to consider carefully, and is beyond the scope of this Article. But it is at least fair to contend that local tax abatement funded by the federal tax base by way of this type of a tax credit could induce homeowner investment and aid in reversing housing market disinvestment in strategically selected markets. Less clear is at what scale reinvestment needs to occur to engineer a rebound and, further, to reverse long-term problems and conditions associated with entrenched disinvestment.

A *limited* subsidy means one that is restricted to those homeowner decisions that will achieve the subsidy's objective.[258] In other words, a subsidy that is not more broadly available than necessary to achieve its objectives. A principal concern voiced about Opportunity Zones tax breaks is that they are too broadly available and will be used primarily in communities where investment does not need a subsidy or for businesses that provide little benefit to those residing in communities that do need a subsidy.[259]

According to the design blueprint in Part III, Section B, the homeowner analogue tax break would likewise be broadly available to those who own or purchase their home within a qualifying zone. Arguably, the tax break should be limited to incoming homeowners or homeowners who purchase a newly constructed home or make a significant renovation or improvement to their homes as these actions constitute new investment. But, as noted earlier, there is a strong argument

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[257] *See, e.g.*, BIER ET AL., *supra* note 169.

[258] Rossman, *supra* note 15, at 253.

[259] *See, e.g.*, Hilary Gelfond & Adam Looney, *Learning from Opportunity Zones: How to Improve Place-Based Policies*, BROOKINGS INST. (Oct. 2018), https://www.brookings.edu/research/learning-from-opportunity-zones-how-to-improve-place-based-policies; Samantha Jacoby, *Potential Flaws of Opportunity Zones Loom, as Do Risks of Large-Scale Tax Avoidance*, CTR. ON BUDGET & POL'Y PRIORITIES (Jan. 11, 2019), https://www.cbpp.org/research/federal-tax/potential-flaws-of-opportunity-zones-loom-as-do-risks-of-large-scale-tax.

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that disinvestment is as much about homeowners leaving as it is about new investment.[260] Viewed from this perspective, including a broader pool of homeowners does seem appropriately tied to the subsidy's objective.

As with Opportunity Zones, debates would likely ensue about whether state decision-makers picked the right census tracts.[261] A homeowner analogue that allowed for a longer and more deliberate selection process and/or provided more specific standards for census tract selections could ameliorate this problem.

A *variable* subsidy is one that allows for modification across and within different markets.[262] As applied here, this definition has two meanings: (i) it is modifiable in its benefits and structure to meet the strengths and weaknesses of different housing markets and (ii) it is modifiable over time to ensure it is appropriately calibrated to achieve its objectives. The homeowner analogue would not be variable in the first sense because it is aimed only at the problem of disinvestment and seeks to combat it monolithically (i.e., through only one form of subsidy). However, this might be acceptable as a policy matter if the homeowner analogue is not viewed as a substitute for all federal homeowner subsidies, but rather as one subsidy aimed at the particular problem of chronic housing market disinvestment.

One might also question whether the homeowner analogue is appropriately variable if it offers roughly the same amount of subsidy in disinvested markets throughout the country. For example, an annual tax credit of $1,000 would do significantly less to change behavior in metropolitan areas with a much higher cost of living (e.g., in California metropolitan areas) than in the post-industrial Midwest, where home prices are much lower.[263] Making the credit equal to a percentage of local taxes, as Part III, Section B proposed, helps address this concern.

If it adheres strictly to the Opportunity Zones model, the homeowner analogue would clearly not be variable in the second sense. The Opportunity Zones program has a fixed end date (i.e. December 31, 2028), has no data gathering or public impact

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[260] *See supra* Part III(A).

[261] *See, e.g.*, Gelfond & Looney, *supra* note 259; Michelle Jarboe, *Opportunity Zones Raise Hopes for Investment, Questions of Equity in Cleveland*, PLAIN DEALER (Apr. l 8, 2018), https://www.cleveland.com/realestate-news/2018/04/opportunity_zones_raise_hopes.html.

[262] Rossman, *supra* note 15, at 253.

[263] *See, e.g.*, *Home Prices in the 100 Largest Metro Areas*, KIPLINGER, https://www.kiplinger.com/tool/real-estate/T010-S003-home-prices-in-100-top-u-s-metro-areas/index.php (last updated Jan. 2019).

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review process, and provides no formal opportunity to revisit zone choices or to recalibrate benefits. While the predictability and reliability of benefits can be important features of an effective tax incentive, the Opportunity Zones model's lack of oversight and review are serious downsides if it turns out to be ineffective in producing the desired results or, worse yet, becomes a haven for abuse. Although Congress has the right to step in and modify the program in the case of either of the above, this type of intervention is harder to conceive of without a formal reporting and review mechanism.

In its original form, the Opportunity Zones legislation required the Treasury Department to periodically report to Congress on program results and with respect to a variety of performance metrics tied to the program's objectives.[264] The TCJA removed this requirement.[265] A smart homeowner analogue would include a meaningful reporting and review process. This process would also be useful if the homeowner analogue proved to be a success at turning around disinvested housing markets. Congress could use the information gathered to establish standards for when and how to reduce or eliminate the tax breaks in revitalized markets and, potentially, to reallocate them to other disinvested markets.

Finally, a *complementary* subsidy is one that supports, rather than contradicts, other federal, state, and local public sector efforts to address a particular problem.[266] It also coordinates well with community planning and the investment of private and philanthropic resources that aim to address the problem. In this respect, a homeowner analogue to the Opportunity Zone model scores well. Development finance experts have lauded the relative ease with which Opportunity Zone tax benefits, due to their broad availability and flexibility, can be stacked onto other public-sector and philanthropic financing incentives available for a particular transaction, increasing the likelihood it moves forward.[267] Moreover, the Opportunity Zones program has prompted many states, cities, and nonprofit development agencies across the country to create complementary tax breaks and business capital programs to accelerate

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[264] Investing in Opportunity Act, S. 293, 115th Cong. § 1400Z-2(c) (2017–2018).

[265] *See supra* notes 94–96 and accompanying text.

[266] Rossman, *supra* note 15, at 253.

[267] *See, e.g.*, *Navigating the Opportunity Zones: Community Partners*, LOCAL INITIATIVES SUPPORT CORPORATION, http://www.lisc.org/opportunity-zones/community-partners-playbook/ (detailing the first in a series of Opportunity Zone "playbooks", which brings attention to the importance of coordinating Opportunity Zone incentives with other federal, state, and local governmental tax incentives).

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development within their Opportunity Zones.[268] It is certainly possible that the homeowner analogue could inspire similar enthusiasm and a battery of complementary initiatives.

A separate question is whether the housing markets selected would complement existing reinvestment strategies. The proponents of the Opportunity Zones model consistently voiced their opinion that states should think strategically about which census tracts they nominated and look to target those areas that were already the focus of state, local, and private economic development efforts and resources.[269] The evidence from how the states went about this process suggest that most states were intentional about engaging local governmental agencies and other community stakeholders in the selection process.[270] A substantial percentage of the states made zone selections based on existing investments in communities or on a broader strategic plan involving projections as to which places were the best bets for future development.[271] That is not to say it was a perfect process. Some states divided up selected zones proportionally across different population centers of the state, which seemed to cut against the intention of the program.[272] Other choices left local policy experts wondering if cities and states had too often bowed to politics or relied on the wrong considerations in making selections.[273]

Interestingly, Congress relied solely on the cap on how many census tracts states could nominate to make Opportunity Zones complementary and simply assumed states would make wise decisions to get there. In fact, the TCJA removed language included in the original legislation that provided states with more guidelines.[274] Although a homeowner analogue could likewise rely solely on a cap, a smarter approach would be to include zone selection guideline language and, better yet, to provide for a more significant federal role in ensuring states honor the intent of the guidelines in making their decisions.

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[268] *See, e.g.*, STATE INFORMATION, NOVOGRADAC, https://www.novoco.com/resource-centers/opportunity-zone-resource-center/state-information (tracking the various legislative efforts in states to pass legislation creating tax incentives that conform with federal Opportunity Zone tax benefits).

[269] *Hearing Before the Joint Econ. Comm.*, *supra* note 3.

[270] *Opportunity Zones: The Map Comes Into Focus*, ECON. INNOVATION GRP. (June 15, 2018), https://eig.org/news/opportunity-zones-map-comes-focus.

[271] *Id.*

[272] *Id.*

[273] *See, e.g.*, Jarboe, *supra* note 261.

[274] Investing in Opportunity Act, S. 293, 115th Cong. § 1400Z-1(d) (2017–2018).

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Finally, the manner in which the Opportunity Zone program was executed posed challenges to making the subsidy as complementary as it could be. Rushed by quick statutory deadlines, states had to make decisions on Opportunity Zone nominations within a matter of months of learning about the program. This in part had to do with Congress tacking Opportunity Zones onto the TCJA at the last minute and not including longer deadlines, which gave states little advance time to process the program's requirements and its potential for coordination with existing economic development efforts. A smarter homeowner analogue would be more carefully executed.

Overall, the homeowner analogue to the Opportunity Zones program shows mixed results when judged based on the above criteria. It is well-tailored to address disinvestment and, if used wisely, could be highly complementary to existing community planning efforts and the investment of public-sector and philanthropic resources aimed at disinvested housing markets. On the other hand, like the Opportunity Zones program, it is a monolithic tax break and could be a challenge to calibrate to match differing local housing market conditions. Like many subsidies, it is also, by design, susceptible to concerns that it will be used primarily in the best performing selected communities where a subsidy is not really necessary and not nearly as much in those places where it is. As is true for Opportunity Zones, the homeowner analogue would perform better if the selection process for qualifying housing markets was more deliberate and subject to guidelines, and if Congress provided for an appropriate ongoing review process and refined the subsidy over time as needed to meet its objectives.

B. Sensitivity to Externalities

The Opportunity Zone model is single-minded in its focus and, relative to predecessors aimed at the same goal, simple in its design. Advocates for the Opportunity Zone model profess that good results will follow by simply unlocking the door to investment in places suffering from economic distress. The Opportunity Zone model places some conditions on the types of investments and business activity that will qualify, but devotes virtually no attention to which businesses ultimately receive investments or the resulting ripple effects on the communities in which these businesses are located.

There is virtue to this single-mindedness, but also significant shortcomings. This may be particularly true as it relates to housing markets in which, as pointed out above, homeowner decisions often result in a myriad of different costs and benefits to the communities directly affected as well as society at large.[275] It can be socially

[275] *See generally* Rossman, *supra* note 15.

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inefficient to subsidize a decision that yields some societal benefit, but at the same time imposes significant costs on others. As it relates to subsidies to reverse housing market disinvestment, one potential negative externality that merits particular attention is the loss of affordable housing for current residents.

It seems paradoxical to worry about housing becoming too expensive in places where home values are depressed. Yet it is almost axiomatic that when housing prices in a revitalizing neighborhood go up, concerns about pricing out those who live in the neighborhood soon follow.[276] This progression has solid footing in the Nash equilibrium. A housing market with pent up demand due to an overabundance of investor caution will, once this equilibrium is disrupted, experience an infusion of demand that, unless met with corresponding increases in supply, drive up prices. This phenomenon, known as gentrification, has been on display in selected urban housing submarkets for decades.[277] Although successful at repairing the fundamentals of a disinvested housing market, gentrification can simply shuffle lower-income residents out of recovering markets and into other poor neighborhoods suffering from the ailments of disinvestment.

In fact, this is a becoming a frequently voiced concern regarding Opportunity Zones.[278] Business activity eligible for Opportunity Zone investments includes the rehabilitation and leasing of residential rental property.[279] At this early stage, most of the Opportunity Zone investments that are in the works are for residential development projects.[280] Interestingly, Zillow reported that home sale prices across census tracts designated as Opportunity Zones spiked significantly in the year

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[276] *See* MALLACH, *supra* note 105, at 117.

[277] *Id.* at 97–121.

[278] *See, e.g.*, *Real Estate Funds Move Into Opportunity Zones, Raising Concerns About Displacement*, IMPACTALPHA (Aug. 1, 2018), https://impactalpha.com/real-estate-funds-move-into-opportunity-zones-raising-concerns-about-displacement/.

[279] *E.g.*, Investing in Qualified Opportunity Funds 18652, *supra* note 48 (The Treasury Department clarified this point in its "second tranche" of proposed Opportunity Zone regulations published on May 1, 2019: "However, these proposed regulations provide that the ownership and operation (including leasing) of real property used in a trade or business is treated as the active conduct of a trade or business for purposes of section 1400Z-2(d)(3).").

[280] *See, e.g.*, James Tassos, *More Than $28 Billion of New Investment Expected in Opportunity Zones*, NAT'L COUNCIL OF STATE HOUS. AGENCIES (May 7, 2019), https://www.ncsha.org/blog/more-than-28-billion-of-new-investment-expected-in-opportunity-zones/ (reporting that of the 130 Opportunity Zone Funds listed in NCSHA's directory, 91% have invested in multifamily residential, student housing, mixed-use, hospitality, or other commercial development, by far the largest category).

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following their selection relative to unselected tracts that met QOZ standards.[281] It is not far-fetched to think that a neighborhood positioned for a rebound might find an infusion of tax-preferenced, homeowner investment to be the springboard to a rejuvenated housing market that raises affordability concerns for those whose lives the program was meant to improve.

For example, Glenville's Circle North, with its historic housing stock and proximity to University Circle jobs, seems particularly susceptible to gentrification. The City of Cleveland, through its Neighborhood Transformation Initiative, appears to have an eye out for this.[282] It plans to balance funding to support new home infill development with forgivable loans to finance rehab projects by existing homeowners, financing for a mixed income, mixed used development, and funding for nonprofits to support employment networking, mentorship and funding to neighborhood-based business start-ups.[283]

With this in mind, a solution may be for Congress to condition the selection of an otherwise-qualifying census tract for the homeowner analogue on local government having established a plan to preserve housing affordability within the census tract. For example, the plan might include committing to a city ordinance requiring that once a census tract that qualifies for the homeowner analogue reaches certain population density or property value targets, new multifamily developments within the tract must set aside a minimum number of units that meet affordability standards. The plan could also include that the city impose a requirement on banks or other lending institutions that do business in the city to make a threshold amount of mortgage capital available to lower-income and minority homebuyers or homeowners within census tracts that qualify for the analogue.

A recent effort by the United States Department of Housing and Urban Development ("HUD"), during the Obama administration, to aid cities and public housing authorities in complying with the federal Fair Housing Act ("FHA") may provide a template.[284] In 2015, HUD issued regulations intended to amplify the obligation of HUD funding recipients to affirmatively further fair housing pursuant

[281] Alexander Casey, *Sale Prices Surge in Neighborhoods With New Tax Break*, ZILLOW (Mar. 18, 2019), https://www.zillow.com/research/prices-surge-opportunity-zones-23393/.

[282] Jackson, *supra* note 211.

[283] *Id.*

[284] Fair Housing Act, 42 U.S.C. § 3604 (2018).

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to the FHA.[285] In connection with this, HUD clarified guidelines for cities on how to meet the Affirmatively Furthering Fair Housing ("AFFH") obligation, created publicly accessible databases and mapping tools to aid community members and local leaders in setting local fair housing priorities and goals, and encouraged local jurisdictions to craft fair housing plans responsive to unique local market conditions and challenges.[286] It also offered specifically tailored technical assistance to fund recipients with the goal of helping them meet the obligation.[287] The Trump Administration's HUD has effectively shelved the AFFH regulations.[288] But clearly the federal level expertise, technology, and resources exist to help cities adopt targeted fair housing plans and monitor their results.

The subsidy associated with the homeowner analogue might also be leveraged to address other negative housing externalities. Some cities use local tax abatement to require homeowners who wish to receive it to adhere to green building standards as a strategy for encouraging new construction and rehab work that reduces the amounts of environmental degradation that results from homes.[289] One phase of the federal Neighborhood Stabilization Program, adopted in the wake of last decade's national foreclosure crisis, provided funds to cities to stabilize housing markets in hard hit areas and required applicant cities to show how their housing plans would accomplish certain environmental objectives.[290] It is not unreasonable to think that the homeowner analogue could be conditioned on and serve as effective leverage to bring about a home's adherence to similar standards and objectives. In addition, the selection process for qualifying census tracts might include criteria that rule out or weigh in favor of certain tracts based on their contribution to or reduction of other externalities (e.g., avoiding housing in census tracts particularly prone to rising sea levels or promoting housing close to public transit).

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[285] *HUD Rule on Affirmatively Furthering Fair Housing*, HUD USER https://www.huduser.gov/portal/sites/default/files/pdf/AFFH_Final_Rule_Executive_Summary.pdf (last visited May 25, 2019).

[286] *Id.*

[287] *Id.*

[288] *See* Ben Lane, *HUD Kills Key Tool Used to Enforce Obama Fair Housing Rule*, HOUSINGWIRE (May 18, 2018), https://www.housingwire.com/articles/43415-hud-kills-key-tool-used-to-enforce-obama-fair-housing-rule.

[289] USGBC, *Transforming a City One Home at a Time*, https://www.usgbc.org/sites/default/files/transforming-a-city.pdf.

[290] Congress authorized Phase 2 of the Neighborhood Stabilization Program—which included these requirements—as part of the American Recovery and Revitalization Act, 123 Stat. 115 (2009).

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Of course, with each externality addressed comes an additional level of federal oversight. The proponents of Opportunity Zones sought to make the program function unencumbered by federal oversight. Yet it would seem that policy makers could seek out a middle ground which leaves the flow of capital relatively unencumbered so that a critical mass of home investment dollars reach places that need it, while still advancing other important federal policy interests related to housing.

C. Penciling Out

My previous article also emphasized that smart subsidies should in some fashion "pencil out" (i.e., demonstrate a net gain and return on the forgone tax revenue) in order to be politically and financially sustainable.[291] In an ideal scenario, government can show that the subsidy pays for itself. This exercise can be fraught with political gamesmanship and is ultimately an imprecise one as the economic costs of the subsidy will almost certainly exceed its budgetary cost and the economic benefits are often difficult to accurately quantify.

The Congressional Joint Committee on Taxation, in its report on the TCJA, showed the Opportunity Zone program costing $1.6 billion over a ten-year period.[292] According to the report, an annual average of about $1.5 billion in forgone tax revenue associated with deferred and discounted taxes on capital gains during the first eight years of the program will be mostly offset, presumably by federal tax revenue gains resulting from new business growth, in the final two years of the program.[293] This is a highly speculative estimate since there will be no defined and separate stream of federal tax revenue attributable to Opportunity Zone businesses. In addition, it will be hard to measure how much of the tax revenue from these businesses will come from activity that would not have occurred but for the Opportunity Zones versus activity that might have still taken place somewhere else in the country. Furthermore, it does not reflect cost savings or revenue gains at the state and local level. Accurately measuring the cost of federal homeowner analogue to Opportunity Zones would run into similar issues.

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[291] Rossman, *supra* note 15, at 253–54.

[292] JOINT COMMITTEE ON TAXATION, ESTIMATED BUDGET EFFECTS OF THE CONFERENCE AGREEMENT FOR H.R. 1, THE "TAX CUTS AND JOBS ACT," JCX 67–17 (Dec. 18, 2017), https://www.jct.gov/publications.html?func=startdown&id=5053.

[293] *Id.*

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One significant advantage for the homeowner analogue, however, is that it could be funded by modifying or ending other federal homeowner subsidies. As noted earlier in this Article, post-TCJA, the federal government still forgoes over $93 billion annually via the existing individual homeowner subsidies, which inure even more exclusively to the benefit of wealthy homeowners and robust housing markets than they did before the TCJA.[294] The Joint Committee on Taxation estimates that the mortgage interest deduction alone will amount annually, on average, to $43.2 billion in forgone federal tax revenue over the next five years.[295] A strong case could be made for ending this tax break and using it to pay for the homeowner analogue to Opportunity Zones.

To put this in perspective, reallocating the cost of the mortgage interest deduction alone equally among each homeowner in 25% of United States housing market census tracts considered disinvested, assuming for the sake of analysis that census tracts contain equal numbers of homeowners, would result in an annual subsidy of over $10,000 per homeowner.[296] That would, of course, add up to $100,000 per homeowner over ten years. This math is rough and based on assumptions made to simplify the analysis. Furthermore, policy makers would ultimately have to agree on the appropriate amount for the subsidy and ensure it is well-calibrated. But the point is that Congress could adopt a sizable homeowner analogue to Opportunity Zones without a hit to current federal income tax revenue.

D. Other Considerations

In my prior article's critique of solutions like the homeowner analogue for changing the way that the federal government subsidizes homeowner decisions, what

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[294] Novogradac, *supra* note 130; *supra* notes 144–46 and accompanying text.

[295] JOINT COMMITTEE ON TAXATION, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2017–2021, JCX-34-1837 (May 25, 2018), https://www.jct.gov/publications.html?func=startdown&id=5095.

[296] The U.S. Census Bureau reports 78.5 million homeowner households as of the second quarter of 2019. *See* U.S. Census Bureau, *Quarterly Residential Vacancies and Homeownership, Second Quarter 2019* (July 25, 2019, 10:00 AM), https://www.census.gov/housing/hvs/files/currenthvspress.pdf. I multiplied 78.5 million by 5.525% (which is equal to one quarter of the 22.1% of census tracts that, according to the Neighborhood Home Investment Act Coalition, have disinvested housing markets). Assuming that census tracts contain equal numbers of homeowners, then approximately 4.3 million homeowners live or would live in disinvested housing markets; $43.2 billion in tax subsidies divided up equally among these 4.3 million homeowners equals a tax subsidy of a little more than $10,000 per homeowner.

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I categorized as the "Subsidy Eligible/Ineligible Zones" model, I raised two additional concerns.[297] They are worth mention here.

The first involves an unaddressed constitutional issue. The Uniformity Clause of the United States Constitution requires that federal tax code provisions apply uniformly throughout the United States.[298] Theoretically, this Clause prohibits Congress from enacting tax provisions that distinguish taxpayers in one geographic area over those in another.[299] The very limited on point case law has applied this Clause quite narrowly, allowing tax laws that only apply in certain places to stand provided they discuss the distinction in nongeographic terms or where it is at least possible that they could do so.[300] In other words, the Uniformity Clause does not prohibit Congress from making a tax distinction based on "geographically isolated problems"[301] (such as, presumably, housing market disinvestment), as long as this distinction is motivated by the condition and not "actual geographic discrimination."[302] While this interpretation appears to provide Congress a good deal of leeway in crafting tax subsidies, it also indicates some outer limits.[303]

Opportunity Zones, and a homeowner analogue to that model, would appear to test these outer limits. Although eligibility for designation as an Opportunity Zone was based on standards that could be characterized as geographically neutral (the definition of "low-income community"), the decisions by states to select and the Treasury Department to certify only some qualifying census tracts could invite a claim of geographic discrimination. At this time, it appears no one has raised this issue, and standing for this type of a claim may be difficult to establish.[304] Furthermore, there is a workaround if legislators are concerned about it: Congress

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[297] Rossman, *supra* note 15, at 254–57.

[298] *See* U.S. CONST. art. I, § 8 cl. 1. ("The Congress shall have Power to lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States.")

[299] Ellen P. Aprill & Richard Schmalbeck, *Post-Disaster Tax Legislation: A Series of Unfortunate Events*, 56 DUKE L.J. 51, 78–84 (2006).

[300] *See, e.g.*, United States v. Ptasynski, 462 U.S. 74 (1983).

[301] *Id.* at 84.

[302] *Id.* at 85.

[303] *But see* Aprill & Schmalbeck, *supra* note 299 at 84 (explaining practical limitations on establishing standing to bring this type of a claim).

[304] *Id.*

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could instead provide the homeowner analogue subsidies outside of the tax code (for example, as HUD-administered grants) and this might actually also be preferable as an administrative matter.[305]

A separate, although not completely unrelated, concern is a political one. Choosing among qualified census tracts creates winners and losers among housing markets plagued by the same problems. For a neighborhood already suffering from chronic housing market disinvestment, not being selected could be a bitter pill to swallow, especially when those chosen places possess more potential for a turnaround and so, presumably, are less severely disinvested. Similar political concerns followed from the selection of Opportunity Zones and yet it moved ahead.[306] The homeowner analogue gets directly to the issue of where people live, however, and so the consequence of being a loser in this selection process would probably be perceived as more personal. Moreover, homeowners in disinvested or other struggling census tracts proximate to ones selected might even see their housing markets suffer as prospective homeowners choose to live in subsidized census tracts over theirs. The fact that only 25% of eligible tracts would be winners, while 75% would be losers only adds fuel to the potential political fire.

It is worth noting that the strategy of prioritizing distressed communities with better capacity and/or potential to catalyze investments is not a novel one, even when the focus involves revitalizing housing markets.[307] Governments and foundations with resources that fall far short of needs face this decision constantly and often decide that strategically concentrating those resources in communities that are best poised for a turnaround rather than spreading them more thinly across all places in need is more likely to yield success.[308] Proponents of this approach would also contend that first turning around a distressed housing market with rebound potential means resources can then be re-allocated and concentrated in other distressed

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[305] *See* Rossman, *supra* note 15, 264–65 for a discussion of the advantages of advancing this type of social policy through HUD rather than the IRS.

[306] *See* Gelfond & Looney *supra* note, at 259.

[307] *See, e.g.*, George Galster, Peter Tatian & John Accordino, *Targeting Investments for Neighborhood Revitalization*, 72 J. AM. PLAN. ASS'N 457 (2007); Wendy Jackson, *Rebuilding from Strength as a Strategy to Safeguard Middle Neighborhoods in Detroit: A Philanthropic Perspective*, *in* ON THE EDGE: AMERICA'S MIDDLE NEIGHBORHOODS 141, 141–44 (Paul Brophy ed., 2016); Richey Piiparinen et al., *supra* note 213; ALAN MALLACH, CUT TO INVEST: CREATE NEW BOND AND TAX CREDIT PROGRAMS TO RESTORE MARKET VITALITY TO AMERICA'S DISTRESSED CITIES AND NEIGHBORHOODS 4 (2012), https://www.brookings.edu/wp-content/uploads/2016/06/06-land-use-bonds-taxes.pdf.

[308] *Id.*

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markets.[309] In the case of the homeowner analogue, advocates for this approach would also want to stress the ways in which the current homeowner subsidies do little to help disinvested housing markets, and in fact probably heighten disinvestment within them.[310] Crafters of such a proposal might also think about how components could be added that provide another type of assistance to homeowners in non-selected qualifying census tracts. Nevertheless, the political challenges following from including some distressed housing markets, but excluding others, could be formidable.

CONCLUSION

There is little disputing that Opportunity Zones are an innovative approach to an entrenched, corrosive, and costly problem. The model is also untested and represents a potentially costly gamble. Chronic housing market disinvestment poses similar challenges and costs as economic disinvestment, and so it is fair to ask whether the Opportunity Zones model is worth a try for it as well.

Upon careful consideration, this Article concludes that a homeowner analogue to the Opportunity Zones model has potential to serve as a smarter federal homeowner subsidy, particularly when viewed in contrast to the current federal homeowner subsidies and subject to some important refinements. Asserting this does not mean that there are not other, even smarter ways of addressing housing market disinvestment or that this one subsidy is a fix for all housing problems that concern the public sector. This Article does not come to either of these conclusions. It does, however, consider a homeowner analogue a potentially viable option for combatting housing market disinvestment and worth further discussion.

As this Article argues, to be a smart subsidy a homeowner analogue should be carefully designed to reflect unique aspects of housing market disinvestment, implemented with better planning than the Opportunity Zones program, include some level of zone selection, reporting and program oversight by the federal government, and used as leverage to get state and local governments to advance other federal housing policies in concert with housing market recovery. Achieving the right balance of inducing homeowner investment into disinvested markets while managing it to control the ripple effects is no easy task and hardly a given, but the upside to crafting such a subsidy could be significant. If done right, a homeowner analogue to Opportunity Zones could improve living conditions in disinvested markets, reduce government costs, and foster broader housing market rebounds.

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[309] Galster et al., *supra* note 307, at 468; MALLACH, *supra* note 307, at 5.

[310] Rossman, *supra* note 15, Part IV(A)(2).

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