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[with Revised Exhibit A 2/6/2020]

Representative Shelly Boshart Davis
900 Court Street NE, H-239
Salem, OR 97301

Representative and House Minority Leader Christine Drazen
900 Court St NE, H-395
Salem, OR 97301

Re: Opportunity Zone Legislation in Oregon
Our File No.: CSR001.CMTY

Dear Representative Boshart Davis and Representative Drazen:

Representatives, I am writing on behalf of the individuals identified on Exhibit A, who are opposed to HB 4010. If Oregon decouples from the federal program, it will greatly damage Oregon's ability to have any development in Qualified Opportunity Zones ("QOZs"). It could effectively kill the program in Oregon. By decoupling, Oregon is saying to investors and developers that Oregon really does not care about receiving your money and your efforts to improve our state.

I am writing to respond to concerns raised by Bennett Minton, and I assume certain legislators related to the QOZ program. As you know, the QOZ program was initiated to create an incentive to cause individuals with capital gains to sell those assets and put the funds to work improving our communities. Oregon is unusual in the quality of its zones. That is because the zones were selected based on census data, and Oregon's data was old – the census data was last updated in 2010. That is why portions of downtown Portland and the Pearl District were designated. I have met with Business Oregon representatives who, along with the Governor, selected the zones in Oregon. One of the primary reasons those two zones were identified was to incent developers to build workforce housing in the areas. There has been much discussion of the advisability of using the QOZ program for a Ritz-Carlton in the Pearl. Although, of course, that was not the product that the Legislature had in mind when it passed the program, the development of that hotel has a tremendous impact on the tax base in Multnomah County. Disadvantaged areas in east Multnomah County will benefit from the increase in that tax base, and also from the income tax generated from the workers and vendors. In addition to the tax impact, the developer of that project wrote a check for \$7 Million to Portland's affordable housing fund in connection with the development.



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First, Downtown Portland has the highest concentration of dedicated (permanent) affordable housing in the state, so there could not be any displacement of low-income people due to OZ investment there. Second, if the downtown tracts were selected, that would preserve other tracts in North and Northeast Portland, which would, if designated, face significant gentrification pressures. Better to concentrate investment in areas that are already targeting large-scale development, then to encourage opportunistic investment that would accelerate gentrification and displacement in "close-in" neighborhoods.

Only California, Mississippi and North Carolina have decoupled from the federal program.

A concern noted is that the program is only for investors who have "substantial" unrealized capital gains. This is not accurate. In fact, the program works for the smallest and largest investor. As a lawyer working in this area, I have created one giant Qualified Opportunity Fund, two medium sized funds, and about 25 husband and wife, or other two-member funds. If a mom and pop business sells, and they have even \$25,000 in capital gains, the program works well for them. They can take their \$25,000 and invest into their own fund, and purchase a piece of land and with the addition of financing, build a rental duplex to aid in their retirement income. This not only helps the investor, it also creates housing that is so badly needed in Oregon. This structure is happening every day. However, because the numbers related to the project are not big, the projects do not get any press attention. If Oregon decouples, then that husband and wife are much less likely to sell their capital asset and put the money to work in Oregon.

There is a group in the Linn County/Albany area developing market-rate multi-family housing through the use of a Qualified Opportunity Fund. That project, like many proposed real estate projects today, suffers from marginal returns due to the cost of land, infrastructure costs, and the cost of labor and materials today. According to the developer, the QOF/QOZ benefits are the primary reason they are still considering the project viable.

Another statement is that "Opportunity Funds are a poor vehicle for investments that do not appreciate substantially better than other options". This is also not accurate. In fact, it is often the addition of the QOF benefit that makes some projects feasible. Charlene Zidell, Stephen Brooks and I have assembled a group of professionals to create workforce housing in rural communities. Other professionals on the team include Jonathan McGuire, Rob Justus and Ozone Capital Management. We are currently considering sites. As Charlene said in our first meeting: "I am sick of hearing people talking about workforce housing and not doing anything about it." So, we are doing something about it. We are developing a program to pair workforce housing and QOZs. We will begin with two projects in rural communities to prove our concept, and then syndicate this program all over the State. Workforce housing (60 to 120% of MFI) is the same product as federally funded affordable housing. It is cheaper to build, however, because of the lack of governmental regulation.



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As you can imagine, the returns for workforce housing are not compelling, typically between 3% and 5%. The benefit to a project by being in a QOZ can add another 2.5-4%. If you combine these returns, the investors can likely recover about a 7% return. 7% is not a compelling return for an ordinary real estate investor. However, for those thousands of people in Oregon who have a heart or mission for workforce housing, that 7% is compelling enough for them to invest and obtain the social impact benefit of creating the housing. Without the QOZ program, investors will likely not make the investment for a 3% return. Honestly, I do not know if our projects will go forward at all if Oregon decouples with the federal program.

I see a statement that a QOF is a lousy program for someone who would like to start up a business and run it as a career. I assume that is because of the liquidation after 10 years. However, the business does not have to liquidate in 10 years. First, the program allows the benefits of liquidating between 10 and 30 years. Also, the business does not have to be sold, but instead the investors with capital gains can be bought out after the hold period. This is exactly the kind of capital that is targeted to get companies off the ground and operating profitably.

I received a comment from a gentleman named L.D. Bailey who has invested in Qualified Opportunity Zone projects himself. He sees the program providing small businesses with the opportunity to move back to the small towns in Oregon. The capital gains advantages of the program will make such investments more attractive, and the rules allow investments into businesses as well as real estate. "Just the mention of this bill has started to slow the consideration of investment in our State," he wrote.

The program is compared by some to other tax preferences that may not have been effective. This program is different because it is not simply a tax benefit, it is a benefit tied to an investment. It has been shown across the country as a very effective benefit. Robb Crocker a small developer has done projects in Coos Bay and Reedsport. Those projects would not have been completed or feasible without the program. Mr. Crocker is using a Qualified Opportunity Fund for developing multi-unit housing in Reedsport designed to be 'workforce' housing, affordable for those above the poverty level who are still in the lesser income brackets. Reedsport in particular has not had a multi-family development since the 1970's. The investors in these local funds are all Oregon residents, with a maximum investment of \$100,000. Not the 'Fat Cat' investors that critics of the program have imagined.

The final substantive objection is that the cost to Oregon treasury is unknown, both from the deferral, step-up in basis, and permanent exclusion. I submit that the cost to Oregon as a whole is much greater than the unrealized tax income, and that cost is impossible to measure. Vanessa Sturgeon is operating one of the largest QOFs in the State. She reports



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that as soon as California decoupled from the QOZ program, she started getting numerous calls from investors that were going to invest in California QOFs, and changed their mind solely because of the decoupling. If Oregon decouples, it will lose out on projects that would have otherwise been developed, Oregon investors will sit tight with their capital assets, and investors from around the country will not invest in Oregon projects because of the Oregon law tax risk. Oregon will lose out on multitudes of revenue from projects that would otherwise be located here. This lost revenue will be from increases in the tax base, property tax on the developments, income tax from workers and vendors and income tax from the projects and businesses created with the program, not to mention the new Commercial Activity Tax. Another possible effect is that investors who may have considered a Qualified Opportunity Fund may instead choose to do a Section 1031 exchange to shelter the capital gains. There is no benefit to current tax revenues when that happens.

When HB 2144 was proposed, James Labar from the Governor's office asked me for talking points to use when speaking to legislators about decoupling. Thankfully that bill died in committee. Following are the talking points I shared with James.

This bill would confuse and alienate Oregon Investors because there is no clear reason for the State to eliminate a benefit that the Federal government thinks is a good use of tax dollars. The message to Oregon taxpayers is 'we don't believe your investment in the State is valuable'. This creates an advantage for these outside investors by having more cash to put into the investment, thus exercising greater control. I tend to think Oregon investors are better off having control of Oregon investment as they have a vested interest in the performance of the investment not only financially, but sustainability to preserve our Oregon way of life. It makes no sense to create a tax handicap for Oregon investors. I welcome outside investment, but let us give Oregonians the control of the investments that they deserve.

It has been clear to us as tax advisors when discussing the purpose of the program and the benefit to the community (beyond tax incentive for deferring tax) not one person could understand why Oregon would want to decouple from this program – seems a bit regressive thinking for a state that tends to boost themselves for caring for those in need. Even Oregon residents were looking to invest in programs in other states that do not decouple even though as an Oregon resident the answer would be the same (in general). Oregon has some great project opportunities and it would be a shame for nonresidents to be discouraged from such investments also (not as attractive without the state match in tax benefit).

Opportunity Zone investors are geographically diverse, and have many choices for investment opportunities. Decoupling from the federal law for the program puts Oregon at a competitive disadvantage for those investment dollars.



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There are many Opportunity Zones in Oregon located in low-income communities that are desperate for investments and jobs. Many of these will not realize such investments and jobs but for their Opportunity Zone status. Should Oregon choose to decouple Oregon from the Federal law, these low-income communities will be at a competitive disadvantage in attracting investments and jobs. Why would the State of Oregon choose a policy that is damaging to these low income communities? ~

As an attorney specializing in this area, I speak with sponsors, developers, brokers and investors every day. When the first decoupling legislation was proposed, I spoke with several potential investors who are passing on Oregon simply because of the uncertainty of Oregon's tax law. This is an issue of Oregon missing out on revenue, but not in the way you may think. Oregon investors are not nearly as likely to liquidate their capital assets and invest in their communities if Oregon does not follow the Federal law. If Oregon residents DO follow the Feds, then Oregon will likely have a BIG tax payday in 2026 as a result of the liquidation and reinvestment of their gains. Moreover, while the projects are being substantially improved, there will be substantial job creation. The dollars expended will roll up to 8 times, thus creating more taxable revenue.

It is well known all over the country that Oregon's OZs are the best quality of anywhere in the US. That means Investors from all over the country will invest their money into our zones. However, if 2144 passes, those investors will go to other states where they do not have any risk of state tax. So, again, by passing the bill, Oregon will lose revenue. Oregon will be perceived as business un-friendly and people will not want to invest here. From my perspective, if Oregon decouples from the program, it will be a net substantial loss in revenue dollars. The state may not get the gain revenue in 10-30 years when the assets sell, but it will also not get the additional economic development, property tax, employment tax and the other revenue that will come if they stay coupled with the program. If 2144 passes, very likely that Oregon investors will not liquidate their capital assets, or will invest in other states, and investors in other states will not invest in Oregon.

Investors in Oregon and nationwide have invested in Opportunity Zones in reliance on the fact that Oregon follows federal law for tax purposes. Many of those investors selected QOZ investments over 1031 Exchanges and will be substantially damaged if Oregon now decouples. Would it be Oregon's plan to have investors treated differently based on whether they invested before or after legislation passes? To apply the legislation retroactively would be extremely inequitable, but to treat investors differently is also discriminatory.

I hope that this helps provide substantive information necessary to help allow this new bill



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to also die in committee. Oregon should remain coupled with the Federal Government for the QOZ program and thus receive the substantial benefits resulting from the program. Please let me know if you need additional information. Thanks much.

Sincerely,

Coni S. Rathbone

CSR:tch

EXHIBIT A
(Revised 2/6/20)

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