

Qualified Opportunity Zones



Presented by David Schon
June 20, 2019

Where are Opportunity Zones?

Located within “low-income communities” (“LICs”)* but not all LICs are opportunity zones – 25% designated – 8,700 census tracts

- Full list of opportunity zones can be found here on the CDFI Fund’s website:
<https://www.cdfifund.gov/Pages/Opportunity-Zones.aspx>
- Full tax benefit for investments through end of 2019—but still get most/many benefits if invest before 6/30/2027



The screenshot shows the top of a website page. At the top right, there is a logo for the CDFI Fund and the U.S. Department of the Treasury, Community Development Financial Institutions Fund. Below the logo are two navigation links: "MAIN MENU" and "SEARCH SITE". The main heading of the page is "OPPORTUNITY ZONES RESOURCES".

The authority to implement IRC 1400Z-1 and 1400Z-2 has been delegated to the IRS. The CDFI Fund is supporting the IRS with the Opportunity Zone nomination and designation process under IRC 1400Z-1 only.

The IRS has issued an initial set of [regulations and guidance](#) on how the Qualified Opportunity Zone benefit under IRC 1400Z-2 (including the certification of Qualified Opportunity Funds and eligible investments in Qualified Opportunity Zones) will be administered; and has posted a list of [Frequently Asked Questions about Opportunity Zones](#). Please send any comments or questions related to Opportunity Funds and Opportunity Zone Investments to CC.ITA.Section.1400@irs.counsel.treas.gov.

Opportunity Zones

- **List of designated Qualified Opportunity Zones (QOZs)**: This spreadsheet was updated **June 14, 2018**, to reflect the final QOZ designations for all States. (See [IRS Notice 2018-48, 2018-28 Internal Revenue Bulletin 9](#), July 9, 2018, for the official list of all population census tracts designated as QOZs for purposes of Internal Revenue Code §§ 1400Z-1 and 1400Z-2.)
- For a **map** of all designated QOZs, [click here](#).
 - To view all designated QOZs, click on the “Layers” tab on the menu on the right hand side of the screen. Select “Opportunity Zone Tract” and unselect “2011-2015 LIC Census Tract,” and zoom in to a specific area on the map. Designated QOZs will appear in **blue**.
 - To view a specific census tract, enter the tract number in the search bar, select “2011-2015 Census Tract” by clicking on the mailbox symbol on the left of the search bar, click search, and select the census tract number that appears in the results below.
- **Additional Resources**
 - **IRS Revenue Procedure**: Provides information on the eligibility criteria for census tract designation as a Qualified Opportunity Zone and the nomination and designation process.
 - **Opportunity Zones Information Resource**, with sortable lists by State of all census tracts originally eligible for designation as a QOZ.
 - **Opportunity Zones Shapefile**: This Zip file contains a Geographic Information System (GIS) shapefile of all population census tracts designated as QOZs as well as all population census tracts originally eligible for designation as a QOZ. See Readme text document for additional detail.

Guidance

- Initial Proposed regs released by Treasury last fall
<https://www.gpo.gov/fdsys/pkg/FR-2018-10-29/pdf/2018-23382.pdf>
- Issued in coordination with Revenue Ruling 2018-29.
- Further proposed regs released April 2019 by Treasury that provide guidance and “update portions of previously proposed regulations”
<https://www.irs.gov/pub/irs-drop/reg-120186-18-nprm.pdf>



2nd Tranche of Regulations

— Key updates included guidance on:

- Operating Businesses:
 - Gross income requirements
 - Clarifications on substantially all test for tangible and intangible property
 - Reasonable working capital definitions
- Real Estate
 - Unimproved land improvements
 - Safe harbors
 - Triple net leases
- Investor Regulations
 - Basis step-ups
 - Cash or property investments, not services
 - Deferred gain inclusion events



What Are The Tax Incentive Benefits?

1. Defer Tax on Capital Gains—These are capital gains from other transactions where an amount equal to this gain is rolled into an OZ investment or when the investment is sold, if earlier (Tax in 2026).
2. Partial forgiveness—up to 15% of Investment into Opportunity Zone Fund.
3. Forgiveness of additional gains—100% of fair market value after 10 years (until 12/31/47).



5, 7 and 10 year hold

Investments in Designated Low Income Census Tracts...

... with Tax Deferral and Tax Avoidance Benefits

Commercial
Real Estate
Development
and Renovation
*in Opportunity
Zones*

Opening a New
Business
*in Opportunity
Zone*

Expansion of an
Existing
Business
*into Opportunity
Zones*

Large
Expansions of
Businesses
already
*in Opportunity
Zones*



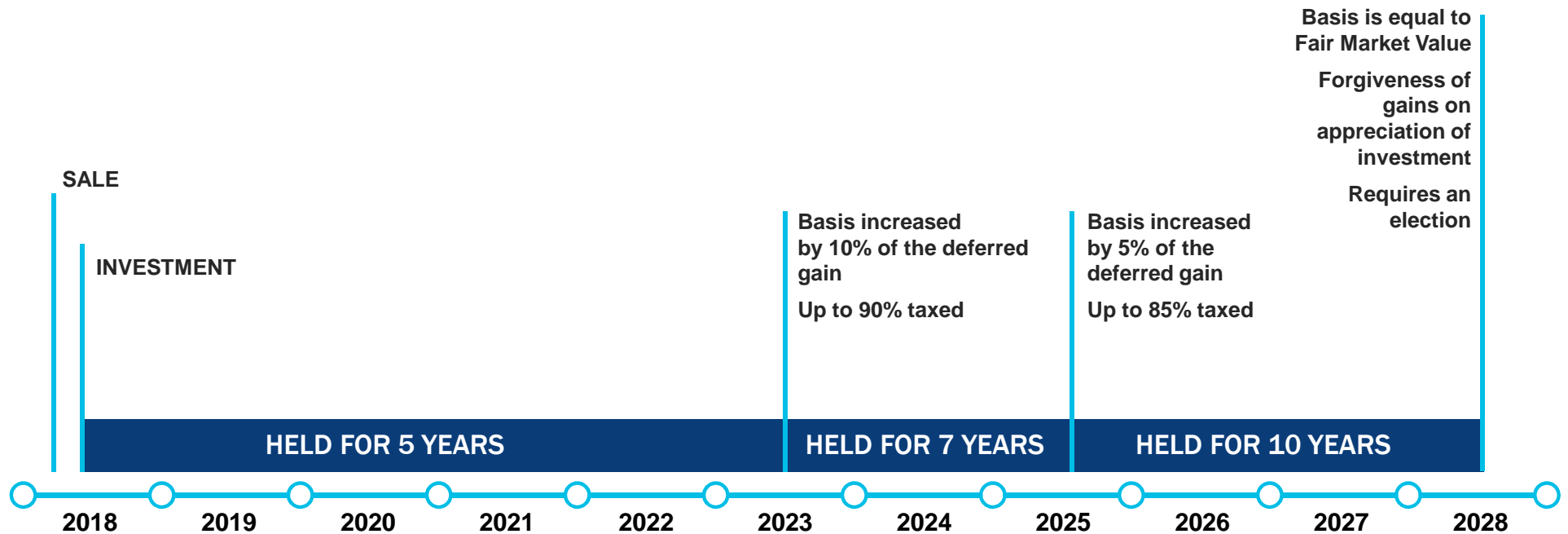
Key Timing (and other) Issues

1. **180 days** after capital gain to invest that amount in an Opportunity Zone Fund.
2. Then, **six months** (basically) for the Fund to acquire partnership or LLC interest, stock or actual assets —**70 percent** of a partnership, LLC or corporation's assets must be an Opportunity Zone Business.
3. Safe harbor to build or rehab a project of **up to 31 months**.

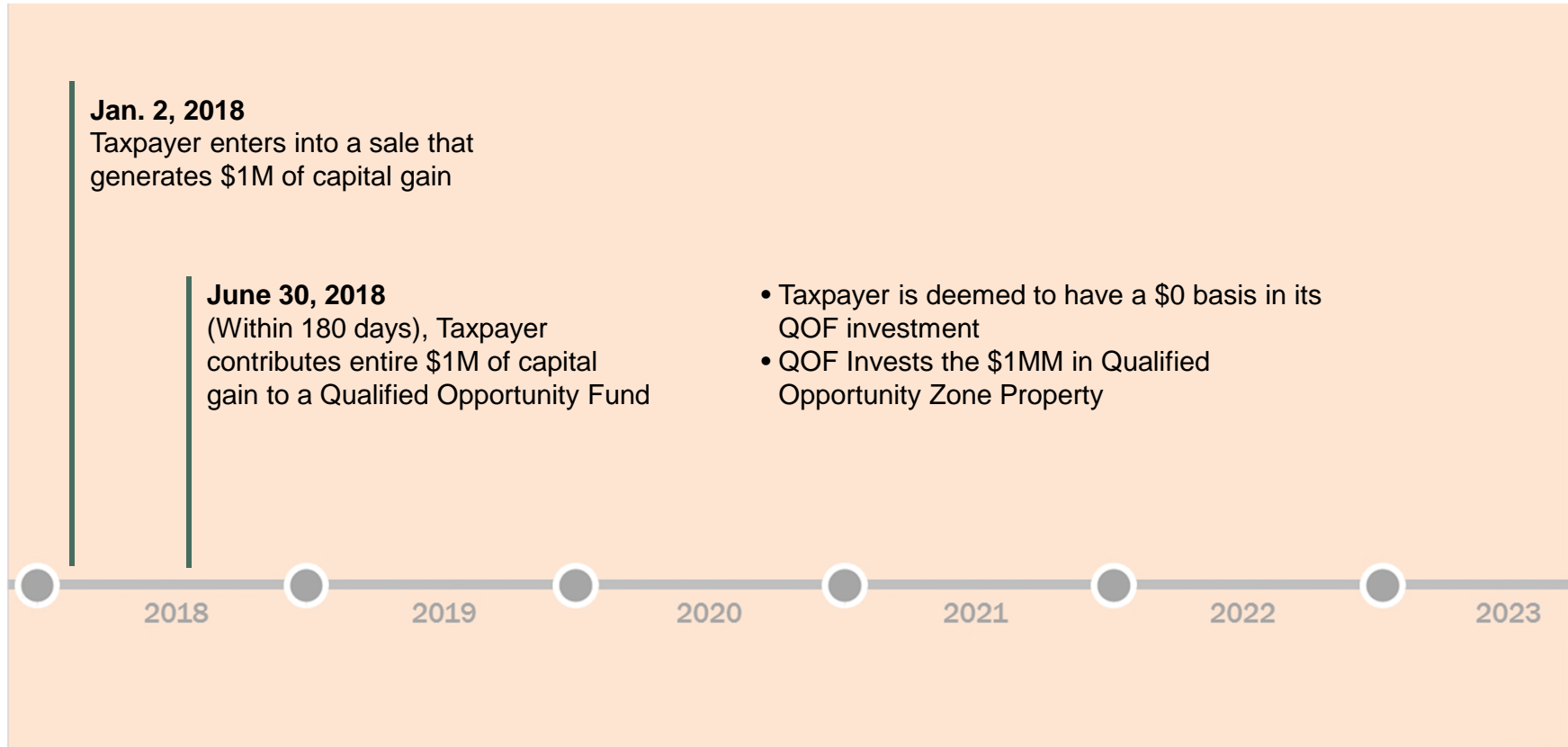
Rehabilitating Used Property

- Over a 30-month period, an Op Zone business must incur additions to basis with respect to used property equal to the property's basis at the start of the 30-month period.
- When computing required capital expenditures for existing property **do NOT include land.**

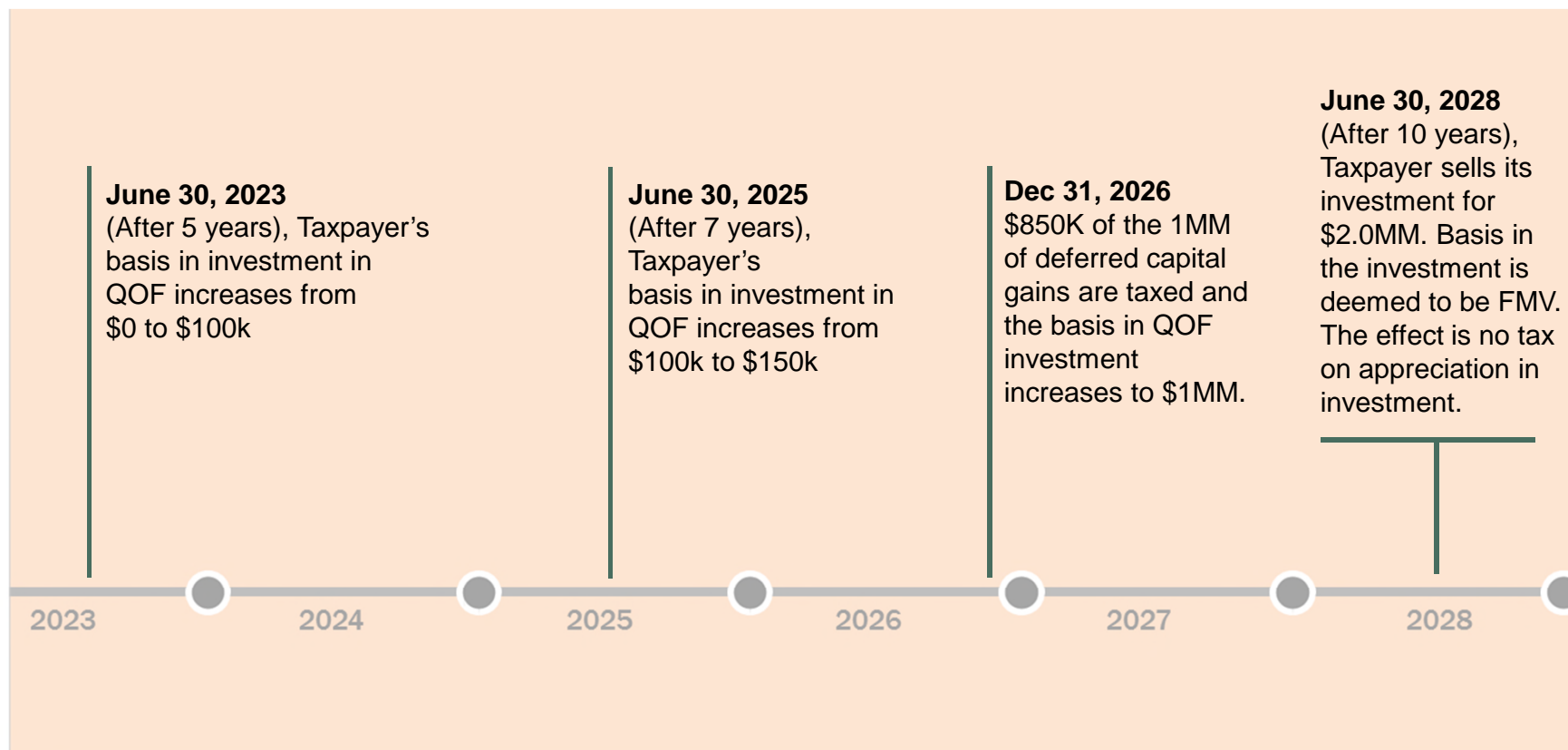
How It Works | Tax Deferral and Tax Exemption



Sample Investment



Sample Investment (cont'd)



Opportunity Zone Fund Formation

- Taxed as a Corporation or Partnership—can include LLCs
- Organized in any State or in the Territory in which the zone and investment is located
- Self-certified, likely will be most useful to have one Fund per asset

Opportunity Funds Must Invest in Qualified Opportunity Zone Property:

- Qualified Opportunity Zone Stock
- Qualified Opportunity Zone Partnership Interest
- Qualified Opportunity Zone Business Property

Note: Funds must maintain 90% of their assets in Qualified Opportunity Zone Property to continue to qualify as a Qualified Opportunity Fund.





Qualified Opportunity Zone Stock and Partnership Interests

- Investment must be acquired after December 31, 2017 in exchange for cash
- Must be a qualified opportunity zone business or is being organized for the purpose of being a qualified opportunity zone business
- Must remain a qualified opportunity zone business for substantially all of the qualified opportunity fund's holding period



Qualified Opportunity Zone Business

A trade or business in which substantially all of the tangible property owned or leased by the taxpayer is qualified opportunity zone business property and

- At least 50% of income is derived from Active Conduct
- Substantial portion of intangible property is used in active conduct of business
- <5% unadjusted basis of property is nonqualified financial property
- Not a “sin business”



Qualified Opportunity Zone Business Property

- Tangible Property used in a trade or business
- Acquired by purchase from an unrelated party (20% standard) after December 31, 2017
- During substantially all of the holding period, substantially all of the use is in a Qualified Opportunity Zone
- Original Use commences with taxpayer OR taxpayer substantially improves the property

During any 30-month period after acquisition, additions to basis exceed an amount equity to the adjusted basis of such property at the beginning of such period.



Who Can Invest

- Persons or Entities that recognize capital gain
- Pass-through entities (like partnerships, S corporations) can invest or can set up provisions for its partners or shareholders to invest.
- **Leverage and liquidity**—can borrow money to make the investment, pledge interest in the Fund as collateral.

Opportunities

- Side-by-side investing with other financing sources, like tax equity
- Entrepreneurial opportunities for business that may significantly appreciate
- Tax savings techniques for service providers who can get a tax-free promote
- Technology parks where prior use is no longer productive
- Workforce and dormitory housing

Opportunity Zones & the HTC

58% of Part 2 applications received in 2018 overlap with Opportunity Zones

46% of designated Main Street Communities overlap with Opportunity Zones

Source: National Trust Community Investment Corp.



OZ Limitations Re: HTC/NMTC

- Regs. limit easily combining OZ investments with NMTC or HTC
- Property must be acquired by purchase after 12/31/2017
 - Either old law HTC or OZ, not both; 5 year HTC and OZ ok
- Uncertainty regarding leases
 - “Active conduct” issue re: HTC master lease structure
 - Valuation for “Substantially All” requirement
- Zero basis requirement
 - Ok to claim the HTC in single entity structure?
 - Suspension of losses?

Policy and Practical Benefits of NMTC & HTC

Promote sustainability and community impact

- HTCs and NMTCs reuse buildings, create jobs and other benefits for low-income people

Grant/debt options OZs lack

- NMTC provides debt or equity
- HTC drives investment analysis

Risk/return analysis varies

- NMTC investors prioritize compliance
- OZ investors requirements tough for high social impact projects

Opportunity Zones – What's Next

- **Comments to second set of regulations due July 1st**
- **OZ advocates continue to submit comments and suggestions**
- **Public hearing scheduled for July 9th**
- **New legislation**
 - Sen. Tim Scott (R – S.C.) plans to introduce a bill extending deadline to invest to benefit from 15% basis step
 - Sen. Scott and Sen. Cory Booker (D – N.J.) introduced a bill that would reinstate information-reporting requirements removed from the original opportunity zones legislation

How to put a deal together:

- **Find a developer** who is willing to build, improve or develop in a qualified opportunity zone
- **Find a business** that wants to locate or relocate to a qualified opportunity zone
- **Find an investor** with a capital gain in the past 6 months or the ability to trigger one now



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