

# What's The Buzz With Opportunity Zones

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For more than a year now, Opportunity Zones and their related funds and businesses have been buzzing with media and industry attention. The Opportunity Zone Program (“OZ Program”) was created as part of The Tax Cuts and Jobs Act of 2017. The OZ Program’s purpose is to encourage investment in low-income areas via tax incentives available for qualified investments. This blog post will highlight high-level information regarding low-income areas, tax incentives, and qualified investments.

The OZ Program permitted chief executives of U.S. states and territories to nominate 25% of their low-income communities (“LICs”) as Opportunity Zones. LICs in the OZ Program were required to be U.S. census tracts that met the same definition of a LIC as defined under the New Markets Tax Credit Program of 2000 and based on the U.S. Census Bureau’s American Community Survey data from 2011 – 2015 or 2012 – 2016. States and territories were also permitted to select certain adjacent tracts to LICs, subject to additional requirements. Ultimately, the U.S. Department of Treasury (“Treasury”) designated 8,764 Opportunity Zones, which cannot be altered.[\[1\]](#)

The OZ Program’s tax benefits center around capital gains. Capital gains realized by a taxpayer (e.g., capital gains from the sale of stock investments, real estate properties, etc.) may be invested into a Qualified

Opportunity Fund ("QOF"). The timely investment of the realized capital gains into the QOF defers taxation on those realized capital gains. Additionally, an investor in a qualified opportunity fund receives a 10% step-up in basis (*i.e.*, 10% discount) on the taxable deferred capital gain amount for investments held for five years and a 5% additional step-up in basis (*i.e.*, 15% total discount) for investments held for seven years. The five and seven year holding periods must be met prior to the earlier of: (i) selling/transferring the investment; or (ii) December 31, 2026; at which point, the investor must pay taxes on the deferred capital gain amount. A qualified investment's holding period must begin by December 31, 2019, or December 31, 2021, to meet the seven-year holding period (15% discount) or five-year holding period (10% discount), respectively. If the qualified investment meets a ten-year holding period, then the investor does not pay taxes on any new profits from the investment.

Treasury and the Internal Revenue Service ("IRS") proposed regulations on October 19, 2018 and April 17, 2019 that provide guidance regarding various aspects of the OZ Program and, in particular, have offered some clarity on what constitutes a qualified investment.<sup>[2]</sup> With some exceptions, QOFs must be tested semi-annually to ensure that 90% of the QOF's assets are invested in an opportunity zone via qualified opportunity zone property ("OZ Property"). OZ Property is tangible and intangible property used in the active conduct of trade or business in an opportunity zone and can take three forms: stock ownership in an opportunity zone business ("OZ Business"), partnership interest in an OZ Business, or direct ownership of opportunity zone business property ("OZ Business Property"). OZ Businesses and OZ Business Properties are defined terms under the OZ Program. Generally, the definitions of OZ Property, OZ Business, and OZ Business Property include various tests and criteria that seek to ensure that the QOF is investing within the Opportunity Zone. A QOF must self-certify its compliance with the semi-annual 90% test on newly published IRS Form 8996, Qualified Opportunity Fund.<sup>[3]</sup>

Treasury and IRS are expected to issue additional guidance before year-end 2019 and will be holding a public hearing on July 9, 2019.

<sup>[1]</sup> <https://www.irs.gov/pub/irs-drop/n-18-48.pdf>

<sup>[2]</sup> IRS News Release on October 19, 2018: <https://www.irs.gov/newsroom/treasury-irs-issue-proposed-regulations-on-new-opportunity-zone-tax-incentive>; IRS News Release on April 17, 2019: <https://www.irs.gov/newsroom/irs-issues-guidance-relating-to-deferral-of-gains-for-investments-in-a-qualified-opportunity-fund>

<sup>[3]</sup> <https://www.irs.gov/forms-pubs/about-form-8996>

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