OPPORTUNITY ZONES

Revised 10-22-18

Tax Benefits for Investors
Capital for Businesses and Real Estate Developers

Key Terms and Requirements

TCJA's New Opportunity Zone Program - Key Terms and Requirements

Investor

Qualified Opportunity Fund

Qualified Opportunity Zone

Qualified Opportunity Zone Property

Opportunity Zone Stock | Opportunity Zone Partnership Interest | Opportunity Zone Business Property

Qualified Opportunity Zone Business

Investor – Who and What

- Individual, C or S corporation, partnership, LLC, trust, common trust fund, qualified settlement fund, or disputed ownership fund

- Taxpayer has "capital gain" from an actual or deemed sale or exchange of property, or any other gain included in the calculation of capital gain for federal income tax purposes
  - The sale or exchange of property must be with an unrelated 3rd party (20% standard applies rather than normal 50%)
  - Gain can be from personal, business, or investment property

- Taxpayer reinvests that capital gain into a Qualified Opportunity Fund (QOF) within 180 days of the transaction triggering the gain
  - Special rules apply for capital gains that do not necessarily have a transaction date

Investor – Why

- Federal tax benefits for investor
  - Investor can make an election for their reinvested capital gain to be deferred until *earlier* of the sale of their QOF investment or 12/31/26
  - Per proposed regulations, the deferral election is likely to be made on Form 8949.
  - In addition to the deferral of capital gain for up to 8 years, if the investor holds their QOF investment for at least:
    - 5 years = original deferred gain is reduced by 10%
    - 7 years = original deferred gain is reduced by another 5%
    - 10 years = if taxpayer elects, no taxable gain is recognized on the taxpayer's sale of their QOF investment, but a taxable loss can still be recognized

Investor – Tax Basis in QOF Investment

- Taxpayer's beginning tax basis in the QOF investment is $0

- If the QOF investment is held at least 5 years, the taxpayer's tax basis in the investment is increased by 10% of the original deferred gain

- If the QOF investment is held at least 7 years, the taxpayer's tax basis in the investment is increased by another 5% of the original deferred gain

- A tax basis increase in the QOF investment is also recognized when the deferred gain in recognized in the future, equal to the amount of such recognized gain

Qualified Opportunity Fund

- Corporation, partnership or LLC that is taxed as a corporation or partnership

- Includes a REIT organized as a corporation or a limited partnership

- The entity must be formed for the purpose of investing in Qualified Opportunity Zone Property

- The entity must hold at least 90% of its assets in Qualified Opportunity Zone Property
  - Average % measured semiannually, at the end of the Fund's first 6-months and again at year-end
  - The test is based on amounts shown on Applicable Financial Statements (AFS), or on cost if the QOF does not have AFS
  - A penalty applies if this 90% test not satisfied, equal to 5% of the shortfall under 90%

- The QOF self-certifies by attaching Form 8996 to its federal income tax return for its initial tax year as a QOF and all subsequent tax years

Qualified Opportunity Zone

- Generally, low-income census tracts, both urban and rural
- Nominated by CEO of each U.S. state, district or territory by 3/21/18 (30-day extensions granted)
- Certified by Treasury
- See bottom of http://eig.org/opportunityzones/resources for map of certified zones

Qualified Opportunity Zone Property - Stock or Partnership Interest

- New or existing domestic corporation, partnership or LLC taxed as a corporation or partnership
- Equity interest acquired by Fund after 12/31/17
- Equity interest must be acquired for cash
- Stock or partnership interest must be original issue
- Corporation or partnership must be a Qualified Opportunity Zone Business at the time the interest is acquired by the Fund and for substantially all of the Fund's holding period

Qualified Opportunity Zone Property - Qualified Opportunity Zone Business Property

- Tangible property that is used in the trade or business of the QOF or QOZ Business

- Property must be acquired by purchase from an unrelated party (20% standard applies rather than normal 50%)

- Property must be acquired after 12/31/17

Qualified Opportunity Zone Property - Qualified Opportunity Zone Business Property

- The "original use" of the property within the QOZ must either commence with the QOF or QOZ Business or "substantial" improvements must be made to the property

- Original use

  - "Original use" means the property is either newly built in the QOZ or is new or used property brought into the QOZ by the QOF or QOZ Business

  - In the case of the purchase of vacant land within a QOZ, this original use rule does not apply – an exception which should encourage the repurposing of vacant or otherwise underutilized land in distressed areas

Qualified Opportunity Zone Property - Qualified Opportunity Zone Business Property

- Substantial improvements
  - In order for improvements to be considered “substantial”, the cost basis of the property must be more than doubled during any 30-month period beginning after the date of the property’s acquisition
  - In the case of a purchase of existing land and building within the QOZ, this substantial improvement test is based on the taxpayer’s cost basis in the building only, not the land
    - Therefore, it is not necessary that the taxpayer’s cost basis in the land also be doubled during the 30-month period
    - This bifurcation should encourage the repurposing of vacant buildings in distressed areas

Qualified Opportunity Zone Business

- Substantially all (at least 70%) of the trade or business's tangible property, owned or leased, is QOZB Property
- A substantial portion of its intangible property is used in the active conduct of the trade or business
- A least 50% of its total gross income is derived from the active conduct of its trade or business

Qualified Opportunity Zone Business

- Less than 5% of the average of the aggregate unadjusted basis of its property is attributable to nonqualified financial property

  - Nonqualified financial property includes cash and cash equivalents, stocks, debt, partnership interests, options, futures and forward contracts, warrants, notional principal contracts, and annuities.

  - Working capital exception
    - An exception is made for reasonable amounts of working capital held as cash, cash equivalents or debt for 18 months or less

  - Safe harbor
    - The working capital exception can also be applied to property held by the QOZB for a period of up to 31 months, if:
      - There is a written plan for the property to be used for the acquisition, construction or substantial improvement of tangible property in the QOZ
      - There is a written schedule that the property will be used within 31 months
      - The business substantially complies with that schedule
      - The written plan and schedule are retained in the taxpayer's records

Qualified Opportunity Zone Business

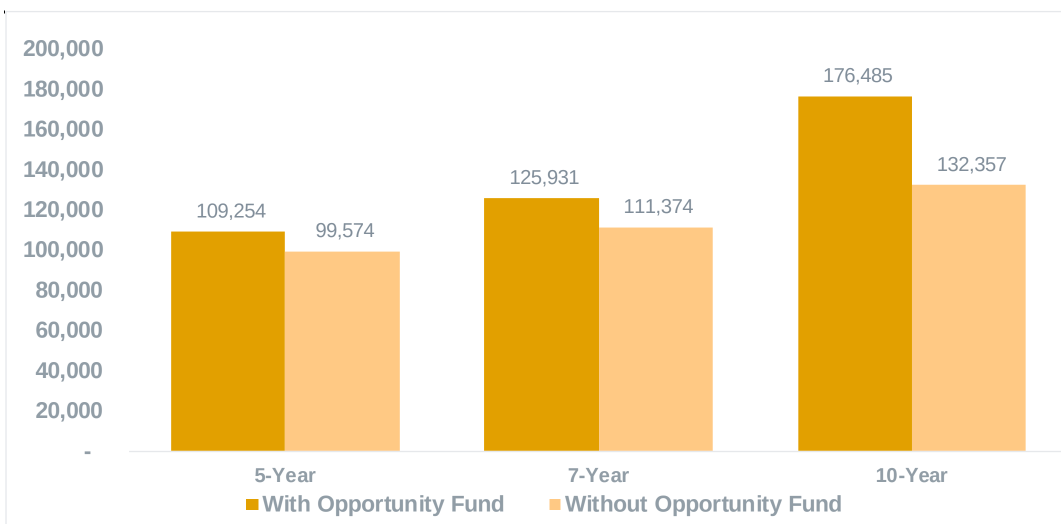
- The trade or business cannot be what is considered a “sin business”:
  - Private or commercial golf course or country club
  - Massage parlor, hot tub or suntan facility
  - Racetrack or other facility used for gambling
  - Any store with the principal business of selling alcohol for off-premise consumption

Comparison of After-Tax Cash Flow

Individual's capital gain reinvested in 2018	100,000
Federal capital gain tax rate	23.8%
Investment appreciation rate	7.0%

Summary of After-Tax Cash Flow Comparison

Holding Period	With Opportunity Fund	Without Opportunity Fund
5-Year	109,254	99,574
7-Year	125,931	111,374
10-Year	176,485	132,357



WIPFLi LLP

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