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Housing Affairs Letter
THE INDEPENDENT WASHINGTON REPORT ON HOUSING SINCE 1961

Opportunity Zone Guide Stirs Investors

A long-awaited tax guide intended to clarify questions about the Trump administration's Opportunity Zone initiative stirred excitement among investors when the Internal Revenue Service unveiled its guideline details Oct. 19.

Real estate development and investment fund communities have been anticipating the rules that are expected to unleash redevelopment of 8,761 so-called "opportunity zones" in the 50 states, District of Columbia, and five U.S territories that will provide investors and developers with tax breaks.

The zones, created by the 2017 Tax Cuts & Jobs Act, were little noticed when the law was passed in late 2017 amid the hubbub over individual and corporate tax cuts.

The zone section of the law intended to spur investment in struggling poverty areas by allowing deferral and reduction of capital gains from existing investments if they are reinvested in a qualified project. The zones have already been designated directly by state governors, and there has been some activity; but most decisions have been delayed until lingering questions were resolved.

Forbes magazine, considered the bible on finance, industry, investing, and marketing, estimated there is about $6 trillion of potential reinvestment of available capital gains cash that could use OZs to drive investment into applicable Qualified Opportunity Zone business or real estate.

Banks, communities, and others are allowed to create Opportunity Funds to direct tax-advantaged investments to the OZs which are intended to reverse blight and revive neighborhoods with private investment in business, housing, education, and other social amenities.

The key features of OZs include:

- Deferral of capital gain taxation until the reinvestment is sold or the last day of 2026, whichever comes first;
- A 10% tax break if reinvestment is held for 5 years; increased to 15% if held over 7 years;
- No tax gains on OZ investments held longer than 10 years but the investments may be held through 2047 without losing tax benefits.

The new guidance clarifies:

o Investors can be individuals, C corporations, S corporations, partnerships, regulated investment companies, real estate investment trusts and estate trusts. There are special rules for gains of partnerships and other pass-through entities;
o Defines "substantially all" as 70% for the requirement that assets be in an opportunity zone;
o Clarifies how to certify and set up a Qualified Opportunity Fund;
o An investment in a QOF must be equity but an investor in a QOF may use its interest in a QOF as collateral for a loan;
o Debt investment is not allowed. Only equity investments qualify;
o A QOF must be an entity classified as a corporation or partnership for federal income tax purposes -- noting that LLCs, Real Estate Investment Trusts, LCs, Regulated Investment Companies, and common trusts under Section 584 work for this purpose.

The proposal provides greater flexibility to a QOF in the most problematic requirements for use of the OZ program.

The IRS also specifies that funds don't have to include the value of land when calculating how much the law requires them to spend renovating or rehabilitating a property.

The 60-day period for written comments and suggestions for discussion topics began Oct. 19. A public hearing is scheduled for Jan. 10, 2019, to discuss those topics and find out how the rules will be used.

Meanwhile, the National Council of State Housing Agencies unveils its "Opportunity Zone Fund Directory." The online resource provides descriptions and contact information for publicly announced Opportunity Funds formed for the purpose of attracting investment in OZs. The NCSHA says it will regularly update the directory.

Info: See the IRS proposal at www.cdpublications.com/docs/9560 and the NCSHA directory details at www.cdpublications.com/docs/9561

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