

Big Incentives Available for Opportunity Zone Investments

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Investors got some great news in the Tax Cuts and Jobs Act, which enables them to delay paying the tax on capital gains. If a taxpayer generates a capital gain and invests that amount in a *qualified opportunity fund* within 180 days, the tax will not be due until the fund investment is sold or exchanged or, if earlier, Dec. 31, 2026.

Moreover, if the taxpayer owns the qualified opportunity fund investment for at least five years, the taxpayer will recognize only 90% of the original gain, at most. If the investment is held for seven years, then only 85% of the original gain will be recognized.

Additionally, the increase in value of the qualified opportunity fund investment is excluded from taxation if the investment is held for at least 10 years.

What is A Qualified Opportunity Fund?

A qualified opportunity fund is a company treated as a corporation or partnership for tax purposes which is organized for the purpose of investing in *qualified opportunity zone property*, other than another qualified opportunity fund. The fund will be certified under rules prescribed by the Treasury Department.

Qualified opportunity zone property can be qualified opportunity zone stock, qualified opportunity partnership interests, or qualified business property. The company issuing the stock or partnership interest must be a qualified opportunity zone business.

A qualified opportunity zone business receives more than half of its income from the active conduct of a trade or business, and uses a substantial portion of its intangible property in the active conduct of a trade or business and substantially all of its tangible property is *qualified opportunity zone business property*.

Qualified opportunity zone business property is tangible property (both real and personal property) used in a trade or business in a qualified opportunity zone. The property must be acquired by purchase and must be new property or used property which is substantially improved.

What is A Qualified Opportunity Zone?

The governor of each state is given the opportunity to nominate *qualified opportunity zones*. Each zone is a population census tract that is a low-income community or, in some cases, a census tract next to a low-income community tract. The legislative history suggests that the census tract (i) should be the focus of reinforcing state, local or private economic development policies (ii) have demonstrated success in geographically targeting development programs and (iii) have recently experienced significant layoffs due to business closures or relocations.

The nominations are to be submitted on or before March 22 (or April 21 if an extension granted) and the Secretary of the Treasury has the opportunity to certify the nomination and designate the tracts.

Some Initial Thoughts

Continued

An investment in a qualified opportunity fund requires only an investment of the gain realized by the taxpayer. As a result, it seems more advantageous than a like-kind exchange where the taxpayer has to reinvest not only gain but most of the basis of the property that was sold.

Qualified opportunity zones can exist in any state or any possession of the United States, so there can be a wide variety of investment locations.

Regulations clarifying the activities which qualify as active trades or businesses will be needed.

As the statute is currently written, it seems as though 85% of the deferred gain has to be recognized on or before Dec. 31, 2026. But if the qualified opportunity fund investment is held for at least 10 years none of the appreciation on that investment needs to be recognized. Moreover, when determining the amount of gain that can be subject to tax on or before Dec. 31, 2026, the amount to be recognized will be limited to the fair market value of the qualified investment zone investment.

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