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Top 10 Things Every Tax Professional Should Understand About Opportunity Zones (Part 2)

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This is the final installment of a two-part series covering the top 10 key points for professionals to understand about Opportunity Zones (OZs). OZs were established by Congress in the Tax Cuts and Jobs Act of 2017 to provide an incentive to encourage long-term investments in low-income communities throughout the United States. To read the first five items, [click here](#).

#6: Original use of the property in the Qualified Opportunity Zone (QOZ) must commence with the entity, or the entity must “substantially improve” the property.

For property that has been vacant for at least five years, the prior use will be disregarded and the QOF’s investment will qualify as original use. Property acquired by purchase that is not “original use” property must be “substantially improved” to qualify as QOZ business property. To “substantially improve” a property, the qualified opportunity fund (QOF) has 30 months to double the adjusted basis (for real estate, land value is generally not included and not considered in original use if it is used in an active trade or business).

#7: QOFs/QOF businesses have 31 months (or potentially nearly 43 months) to fully deploy capital. Newly received (within 6 months) cash is excluded from the annual 90% asset test. Together with the reasonable 31-month working capital safe harbor for working capital used for developing a trade or business, a QOF can theoretically have up to 43 months to fully deploy its capital. For instance, if the QOF took in capital in early January, the sixth month grace period would make the first test for that capital at year-end (about 12 months later), and the QOF could then contribute the capital to the QOZ Business, which would have 31 months to use it.

#8: Don’t forget about state and local incentives for Opportunity Zone investments. Several states now have Opportunity Zone initiatives. For instance, Ohio offers a state income tax credit (10% of a qualifying investment) for investments made 100% in Ohio opportunity

zones. Louisiana includes structures in opportunity zones in its Restoration Tax Abatement program. Connecticut incentivizes certified historic structures in opportunity zones (increasing the tax credit from 25% to 30%) and gives priority to opportunity zone projects for several other state programs. But caution -- states vary as to whether they are automatically conforming, opting in, or decoupling from the Opportunity Zone benefits -- check your tax statutes.

#9: Under current law, opportunity zone boundaries cannot be expanded or amended. Although the boundaries and designated zones are set through 2028, the Treasury did clarify what happens when property is only partially in an Opportunity Zone. The Treasury looked to empowerment zone rules and determined that the entire property will qualify if the property is contiguous and the square footage of the property inside the zone is substantial (if the unadjusted cost of the real property inside a qualified opportunity zone is greater than that outside of the zone).

#10: Securities laws apply. Caution, funding solicitation raises securities law questions. On July 19th, the SEC and NASAA (North American Securities Administrators Association) issued guidance providing that interests in qualified opportunity funds offered and sold to investors will typically be securities. QOFs must follow SEC and state securities regulations including the registration and anti-fraud provisions.