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Additional Opportunity Zone Regulations Issued

REAL ESTATE, TAX, TAX REFORM
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On April 17, the IRS finally issued additional guidance (the 4/17 proposed regulations) concerning qualified opportunity zone (QOZ) investments following up on the first set of rules issued in October 2018 (see our article from October 24, 2018). The guidance came in the form of a second set of proposed regulations that had been promised since early December. Further, in two separate announcements, the IRS noted that it may, or it may not, decide to issue a third set of regulations in a couple of months.

While QOZs promise economic development in designated low-income communities in exchange for tax benefits taxpayers willing to invest in those areas (see our article from July 11, 2018), some taxpayers appeared hesitant to invest in these areas until the IRS provided the guidance necessary to fully understand how the rules would be applied. While much too voluminous to cover in detail within this article, the 4/17 proposed regulations answer a number of open issues including:

- The definition of a trade or business (Hint: triple net lease activity is an issue);
- The treatment of Section 1231 gains and losses and timing for reinvestment;
- The consequences of purchasing unimproved land;
- The definitions of various terms including “original use” and “substantially all”;
- The treatment and valuation of leased property, including from related parties;
- The events triggering deferred gain prior to a sale of interest or December 31, 2026;
- How a qualified opportunity fund can reinvest capital upon the sale of qualifying property; and
- How qualifying testing requirements are applied.

Further, the new regulations answer some, but not all, of the questions taxpayers and their advisors raised since the provision was enacted as part of the Tax Cuts and Jobs Act signed into law in December of 2017. One significant unresolved item that potentially requires legislative action is the taxability of qualifying property sales. Relief was provided regarding reinvestment of those proceeds to continue qualification, but the resulting gain from sale is taxable under normal tax rules. Additionally, issues left unanswered include the amount and type of data to be reported to the IRS, as well as penalty provisions for failure to meet the various qualification requirements.

In summary, for those taxpayers interested in taking advantage of the tax benefits offered by investing in qualified opportunity funds, there is now sufficient guidance to provide investors the confidence necessary 1to structure their transactions to meet regulatory requirements. The government desires to incentivize investment in QOZs and has done so by providing generally taxpayer-favorable regulations.

Please do not hesitate to reach out to us if you have any questions on qualified opportunity zones.

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