International Economic Development Council Webinar

Opportunity Zones 201

PUBLIC PRIVATE STRATEGIES

THE PATH TO PASSAGE – Washington *Can* Work

- The Tax Cuts and Jobs Act (H.R. 1) was signed into law by President Trump on December 22, 2017
- The sweeping tax overhaul legislation included provisions from S. 293, the Investing in Opportunity Act
- Original Opportunity Zones legislation sponsored by Sen. Tim Scott (R-SC); originally co-sponsored by Sen. Cory Booker (D-NJ)
- House of Representatives counterpart, H.R. 828, sponsored by Reps. Pat Tiberi (R-WI) and Ron Kind (D-WI)
- Bipartisan support
    - 14 Senate co-sponsors
    - 81 House co-sponsors

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OPPORTUNITY ZONES TAX INCENTIVE

Opportunity Zones offer investors three incentives for putting their capital to work in economically distressed communities:

Temporary Deferral

A **temporary deferral:** An investor can defer capital gains taxes until the end of 2026 by rolling their gains directly over into an Opportunity Fund.

Step-Up In Basis

A **tax liability reduction:** The deferred capital gains liability is effectively reduced by 10% if the investment in the Opportunity Fund is held for 5 years and another 5% if held for 7 years.

Permanent Exclusion

A **tax exemption:** Any capital gains on subsequent investments made through an Opportunity Fund accrue tax-free as long as the investor stays invested in the fund for at least 10 years.

Graphics courtesy of Economic Innovation Group

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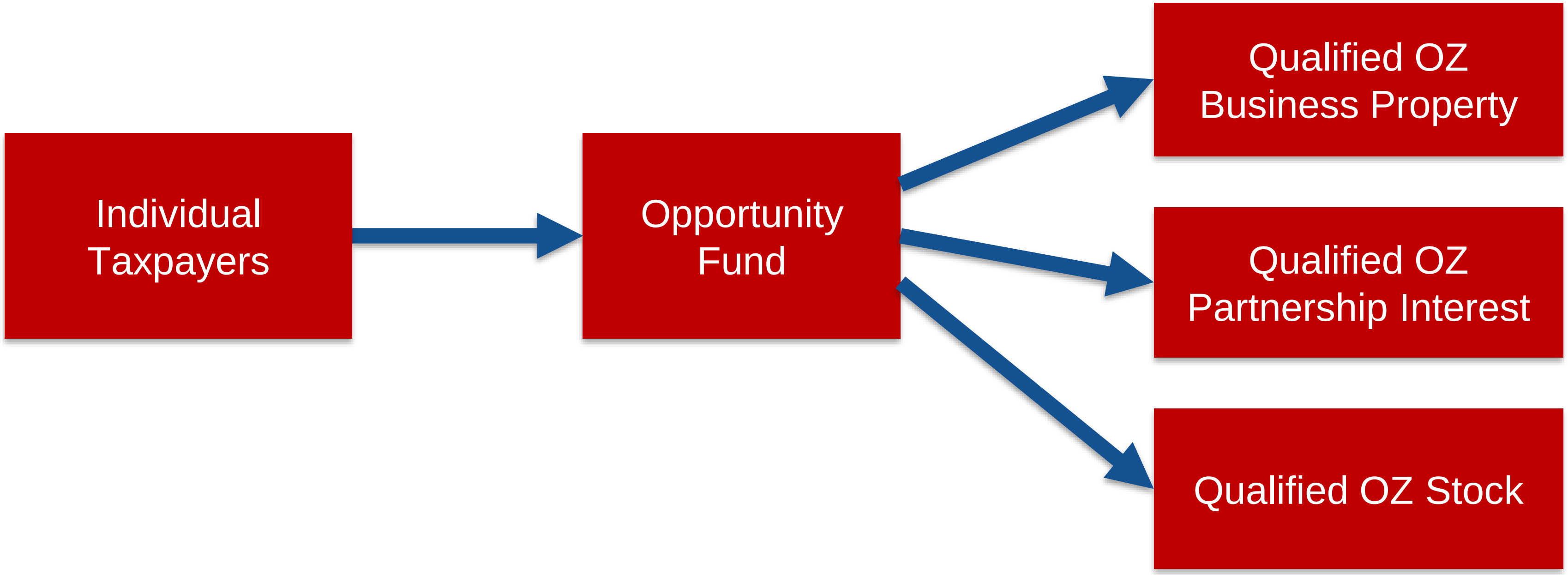
MECHANICS OF O ZONE INVESTMENTS



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OPPORTUNITY ZONES IN PRACTICE

There are three major components to Opportunity Zones:

Investments:
Opportunity Funds make equity investments in businesses and business property in Opportunity Zones.

Funds:
Opportunity Funds are investment vehicles organized as corporations or partnerships for the specific purpose of investing in qualified Opportunity Zones.

Zones:
States and territories nominated 25% of their eligible low-income census tracts as Opportunity Zones. Treasury approved final map.

Graphics courtesy of Economic Innovation Group

ASSETS ELIGIBLE FOR O ZONE INVESTMENT

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There are three types of property eligible for Opportunity Zone investment:

Stock of a qualified Opportunity Zone **corporation**

Partnership interest in a qualified Opportunity Zone partnership

Business property used in qualified Opportunity Zones

- A qualified Opportunity Zone business must use **"substantially all"** of its tangible property within a zone and meet a few additional basic tests. ***Treasury just released draft regulations setting the "substantially all" test at 70% of the basis of the building itself excluding the cost of land***
- Investments that **do not** qualify include funds of funds, "sin" businesses (e.g. golf courses, package stores, casinos), and financial institutions
- A **substantial improvement** test applies unless the business property is original use

Graphics courtesy of Economic Innovation Group

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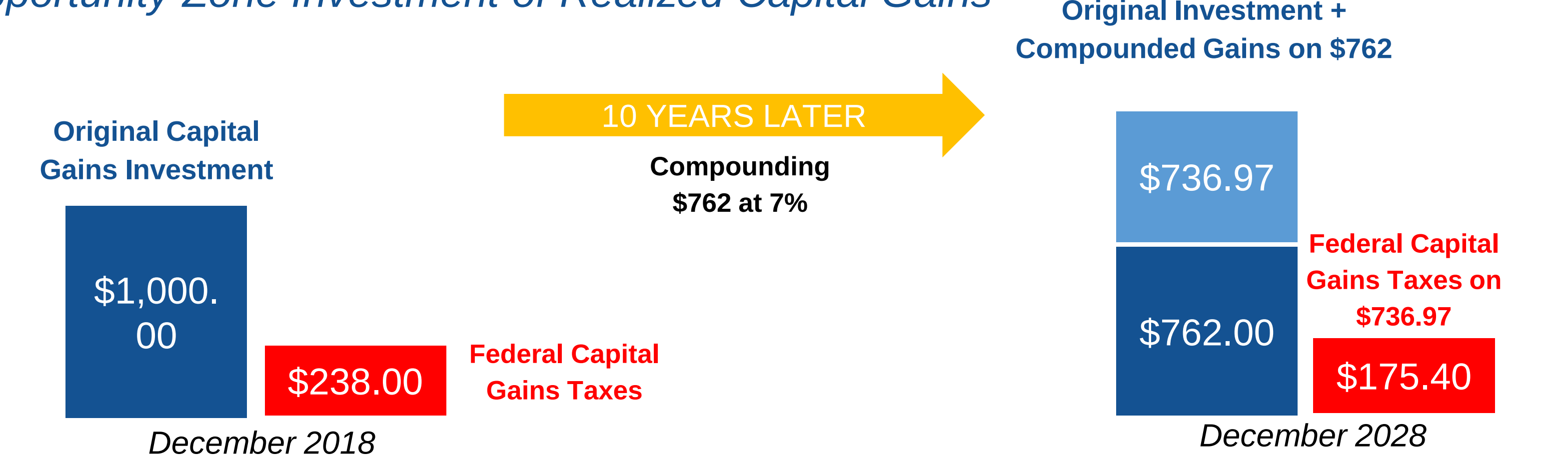
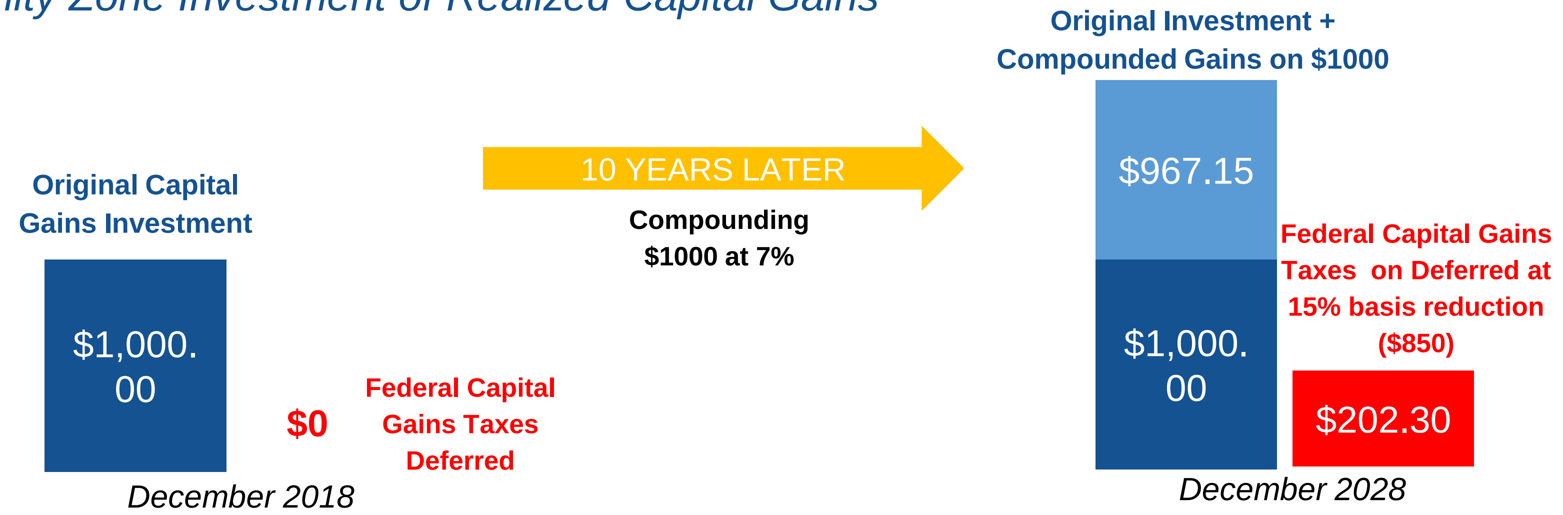
O ZONES INVESTMENT: A SIMPLIFIED EXAMPLE (4)

Non-Opportunity Zone Investment of Realized Capital Gains



Total Federal Taxes Over 10 Years:	$413.40
Total Gains Over 10 Years:	$736.97
Net Gain Over 10 Years:	$561.67

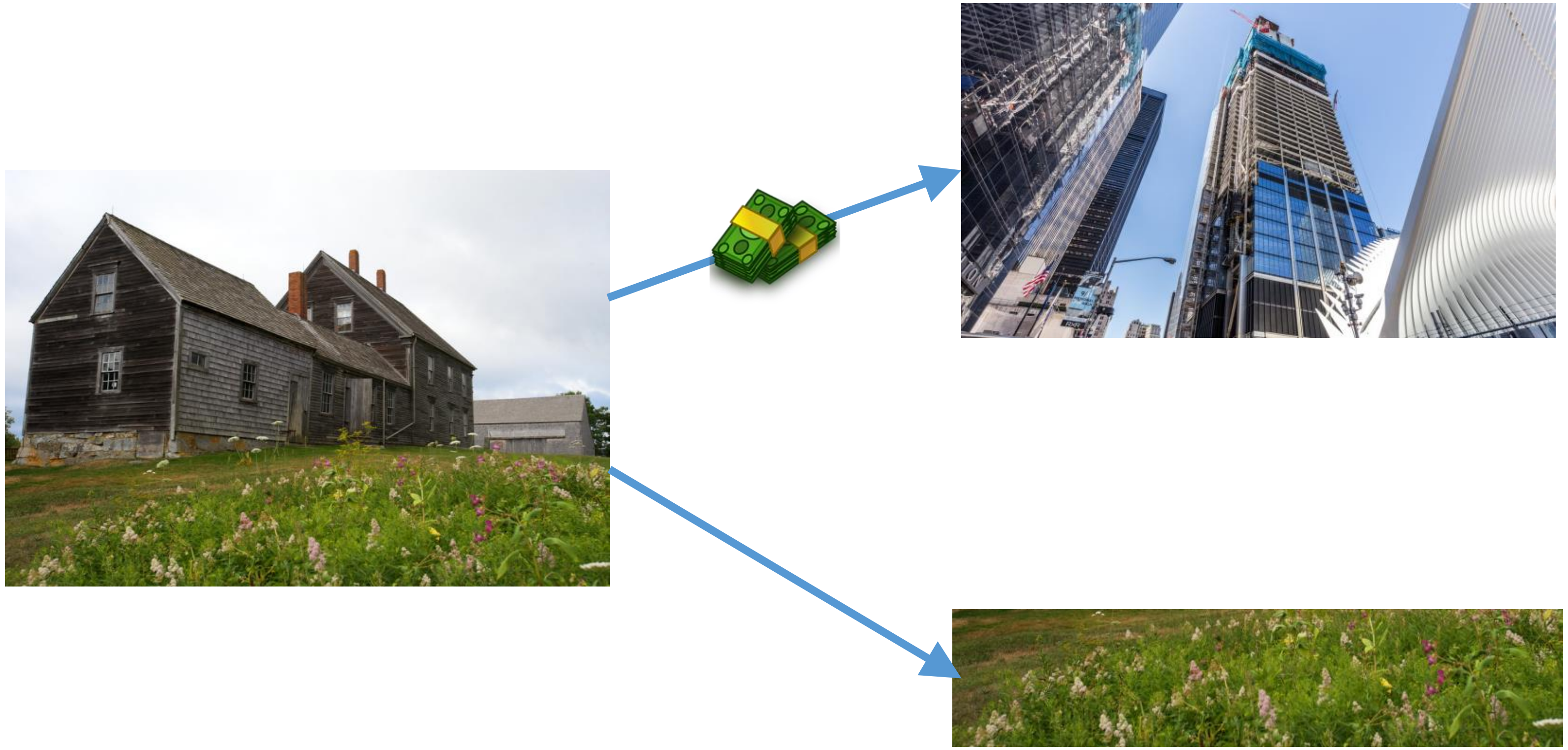
Opportunity Zone Investment of Realized Capital Gains



Total Federal Taxes Over 10 Years:	$202.30
Total Gains Over 10 Years:	$967.15
Net Gain Over 10 Years:	$764.85

LAND AND BUILDINGS

- Land does not require substantial improvement, but buildings do
- “Substantial improvement” is investment that meets or exceeds the cost basis of the buildings (excluding the land)

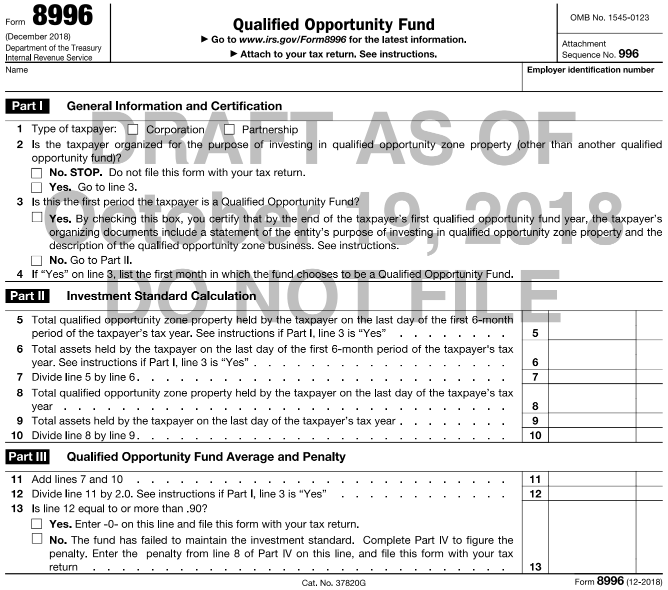


“SUBSTANTIALLY ALL” THRESHOLD

- **90%** of the assets of any Opportunity Fund must be situated in Opportunity Zones or invested in Opportunity Zone businesses.
- Qualified Opportunity Zone businesses must have **“substantially all”** of their tangible property located within an opportunity zone.
- According to the new guidance, **“substantially all”** is defined as **“at least 70%”** for determining whether substantially all of the tangible property owned or lease by a taxpayer is qualified opportunity zone business property (as defined under section 1400Z-2(d)(3)(A)(i)).

OPPORTUNITY FUND SELF-CERTIFICATION

Opportunity Funds will self-certify their compliance with applicable requirements using IRS Form 8996.



Form **8996**
(December 2018)
Department of the Treasury
Internal Revenue Service

Qualified Opportunity Fund
▶ Go to *www.irs.gov/Form8996* for the latest information.
▶ Attach to your tax return. See instructions.

OMB No. 1545-0123
Attachment Sequence No. **996**

Name | **Employer identification number**

Part I — General Information and Certification

1 Type of taxpayer: ☐ Corporation ☐ Partnership
2 Is the taxpayer organized for the purpose of investing in qualified opportunity zone property (other than another qualified opportunity fund)?
☐ **No. STOP.** Do not file this form with your tax return.
☐ **Yes.** Go to line 3.
3 Is this the first period the taxpayer is a Qualified Opportunity Fund?
☐ **Yes.** By checking this box, you certify that by the end of the taxpayer's first qualified opportunity fund year, the taxpayer's organizing documents include a statement of the entity's purpose of investing in qualified opportunity zone property and the description of the qualified opportunity zone business. See instructions.
☐ **No.** Go to Part II.
4 If "Yes" on line 3, list the first month in which the fund chooses to be a Qualified Opportunity Fund.

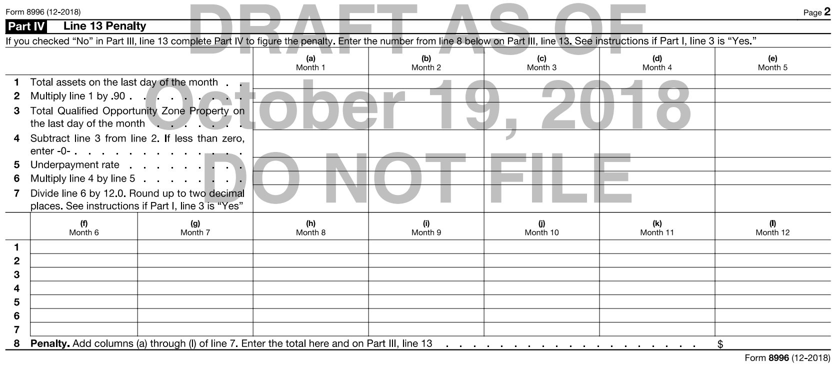
Part II — Investment Standard Calculation

5 Total qualified opportunity zone property held by the taxpayer on the last day of the first 6-month period of the taxpayer's tax year. See instructions if Part I, line 3 is "Yes" **5**
6 Total assets held by the taxpayer on the last day of the first 6-month period of the taxpayer's tax year. See instructions if Part I, line 3 is "Yes" **6**
7 Divide line 5 by line 6 . . . . **7**
8 Total qualified opportunity zone property held by the taxpayer on the last day of the taxpaye's tax year **8**
9 Total assets held by the taxpayer on the last day of the taxpayer's tax year **9**
10 Divide line 8 by line 9 . . . . **10**

Part III — Qualified Opportunity Fund Average and Penalty

11 Add lines 7 and 10 . . . . **11**
12 Divide line 11 by 2.0. See instructions if Part I, line 3 is "Yes" **12**
13 Is line 12 equal to or more than .90?
☐ **Yes.** Enter -0- on this line and file this form with your tax return.
☐ **No.** The fund has failed to maintain the investment standard. Complete Part IV to figure the penalty. Enter the penalty from line 8 of Part IV on this line, and file this form with your tax return **13**

Cat. No. 37820G — Form **8996** (12-2018)



Form 8996 (12-2018) — Page **2**

Part IV — Line 13 Penalty

If you checked "No" in Part III, line 13 complete Part IV to figure the penalty. Enter the number from line 8 below on Part III, line 13. See instructions if Part I, line 3 is "Yes."

	(a) Month 1	**(b)** Month 2	**(c)** Month 3	**(d)** Month 4	**(e)** Month 5
1 Total assets on the last day of the month					
2 Multiply line 1 by .90					
3 Total Qualified Opportunity Zone Property on the last day of the month					
4 Subtract line 3 from line 2. If less than zero, enter -0-					
5 Underpayment rate					
6 Multiply line 4 by line 5					
7 Divide line 6 by 12.0. Round up to two decimal places. See instructions if Part I, line 3 is "Yes"					

	(f) Month 6	**(g)** Month 7	**(h)** Month 8	**(i)** Month 9	**(j)** Month 10	**(k)** Month 11	**(l)** Month 12
1							
2							
3							
4							
5							
6							
7							

8 **Penalty.** Add columns (a) through (l) of line 7. Enter the total here and on Part III, line 13 . . . . $

Form **8996** (12-2018)

OPPORTUNITY FUND ORGANIZATIONAL STRUCTURE

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- Qualified Opportunity Funds can be:
  - LLCs
  - Partnerships
  - Corporations
- Taxpayers eligible to elect deferral under section 1400Z-2 (“gain deferral election”) are those that recognize capital gain for federal income tax purposes. These taxpayers include:
  - Individuals
  - C corporations (including Regulated Investment Companies and Real Estate Investment Trusts)
  - Partnerships, and
  - Certain other pass-through entities

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WORKING CAPITAL SAFE HARBOR

The safe harbor allows qualified opportunity zone businesses to apply the definition of working capital provided in section 1397C(e)(1) to property held by the business for a period of up to **31 months**, if three requirements are met:

1. There is a **written plan** that identifies the working capital assets as property held for the acquisition, construction, or substantial improvement of tangible property in the opportunity zone
2. There is a written schedule consistent with the ordinary start-up of a trade or business for the expenditure of the working capital assets, and under that schedule, the **working capital assets are spent within 31 months of the receipt by the business** of the financial property
3. The working capital assets are actually used in a manner that is **substantially consistent with the schedule**

COMMUNITY DEVELOPMENT POLICY TOOLS

Tax Credits

- Low Income Housing
- New Markets

Debt Financing

- Tax Exempt Capital Markets
- Federal Credit Programs: HUD, USDA

Community Targeting

- Opportunity Zones
- HUBZones
- Disaster Areas
- Other Criteria

KEY TOOLS FOR LOCAL GOVERNMENTS

- ✓ **Land use:** Address land use zoning as a means to protect/preserve affordable "commercial workspaces and locations"
- ✓ **Planning:** Local governments' proactive participation in negotiating redevelopment plans designed to prevent displacement of micro- and/or small businesses
- ✓ **Knowledge:** Conduct economic impact assessments that measure the value of business services to a city's resident base
- ✓ **Social Impact:** Small businesses are often more than service providers: they are social supports, particularly for lower-income communities
- ✓ **Incentives and Community Investment:** Economic incentives from Tax Increment Financing, Community Development Block Grant investment, infrastructure development, workforce training, and others contribute to creating stronger communities

QUESTIONS? CONTACT INFO BELOW

Jane Campbell
Senior Advisor for International Economic Development Council
Senior Advisor, Public Private Strategies
mayorjane@publicprivatestrategies.com