Opportunities abound
What you need to know about investing in qualified opportunity zones

As part of the Tax Cuts and Jobs Act of 2017 (the TCJA), Congress enacted sections 1400Z-1 and 1400Z-2 of the Internal Revenue Code. These sections, which were intended to promote investments in low-income communities (Opportunity Zones), offer significant opportunities to businesses and investors to defer, and potentially reduce, gains from sales or exchanges of property to unrelated parties. There are Opportunity Zones across the United States, including in major cities such as New York and Los Angeles.

A taxpayer can elect to defer gain from a sale or exchange of property to an unrelated party if, within 180 days, the taxpayer reinvests the amount of such gain (Reinvested Gain) in a “Qualified Opportunity Fund”—a US corporation or partnership that invests in qualified property or qualified businesses in an Opportunity Zone.

The following benefits are available with respect to any Reinvested Gain:

- Deferral of tax on the Reinvested Gain until the sale of the interest in the Qualified Opportunity Fund or December 2026, whichever comes first;
- If the investment in the Qualified Opportunity Fund is held for at least five years, the taxpayer’s basis in the Qualified Opportunity Fund is increased by an amount equal to 10% of the Reinvested Gain, which may effectively exclude such amount from income;
- If the investment is held for at least seven years, the taxpayer’s basis in the Qualified Opportunity Fund is increased by an amount equal to 5% of the Reinvested Gain (or 15% total), which may effectively exclude such amount from income; and
- If the investment is held for 10 years, gain from further appreciation of the investment in the Qualified Opportunity Fund is potentially permanently excluded from income.

In addition to offering significant benefits, these rules are relatively flexible. Generally, deferral regimes (like the like-kind exchange rules, which post-TCJA are only available for real property) limit the ability to receive cash without current tax. However, under these rules, only the gain needs to be reinvested, which permits taxpayers to qualify for these benefits while deploying the rest of the cash sales proceeds as they choose. Further, in the case of a taxable exchange of property, a taxpayer could potentially invest other cash in an amount equal to the gain on the exchange and be eligible for these benefits.

On October 19, 2018, the Treasury published proposed regulations that offered some clarification on the application of these rules, and another set of proposed regulations is expected to add additional clarity. For businesses and investors that plan to dispose of appreciated property to unrelated parties, these rules offer significant opportunities to defer, and potentially reduce, the gain from such property.

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