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An Overview of the Opportunity Zones Program

4/3/2019

What is the Opportunity Zones Program?

The Opportunity Zones Program was established by Congress in the 2017 Tax Cut and Jobs Act as an innovative approach to spur long-term private sector investments in low-income urban and rural communities nationwide. The program has two primary components:

Opportunity Zones (OZ) and
Qualified Opportunity Fund (QOF).

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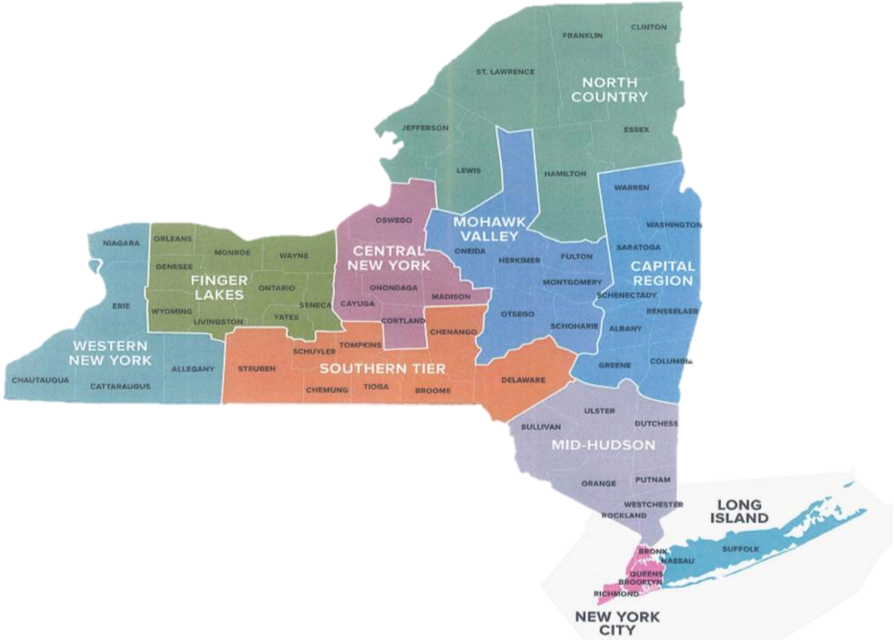
What are Opportunity Zones?

- **Opportunity Zones (OZ):** Designated by the Governor on April 20, 2018 and approved by the U.S. Treasury on May 18, 2018, OZ are eligible low-income census tracts (LICs) in the New York State that allow for Federal and NYS income tax benefits.
- OZ are designated until December 31, 2028.

Where are New York State's Opportunity Zones?

There are 514 Designated OZ across the 10 regions of New York State.



NYS OZ maps are available at https://esd.ny.gov/opportunity-zones

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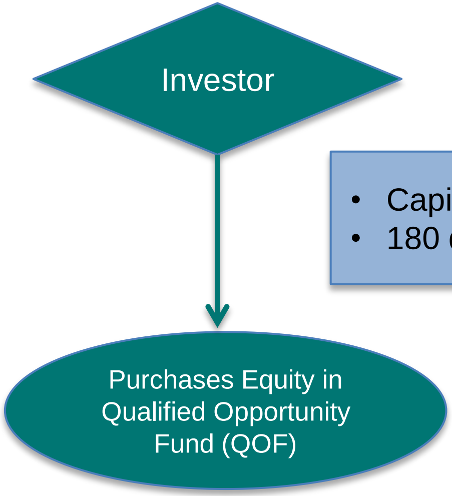
What Does This Mean As Investor?



- Capital Gain Event
- 180 days to invest in Qualified Opportunity Fund

- Holds investment for 5 years – 10% reduction on original capital gain tax
- Holds investment for 7 years – 15% reduction on original capital gain tax
- **12/31/2026 – Original Capital Gain Tax due to IRS**
- Hold investment for 10 years + - No capital gain on appreciation of equity in Opportunity Fund

The tax exemption OZ status expires on December 31, 2047.

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Investor Tax Benefits in Opportunity Zones

Investment Length	Income Tax Benefits Received
Fewer than 5 years	Deferred payment of the original capital gains tax until either (a) December 31, 2026 or (b) the date the Opportunity Fund investment is sold or exchanged whichever is sooner.
5 to 7 years	Benefits above + 10% reduction of the tax on the original capital gains.
7 to 10 years	Benefits above + additional 5% reduction of the tax on the original capital gains (total 15% reduction).
December 31, 2026	Payment of the original capital gains tax is due.
Greater than 10 years	Investor pays no capital gains tax on the Opportunity Fund investment appreciation.

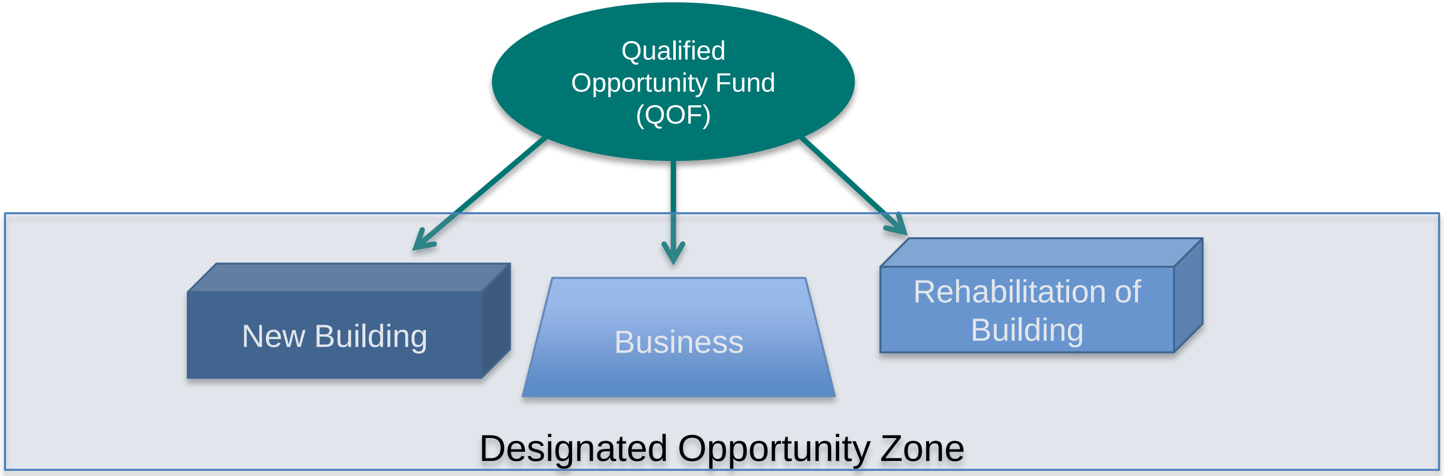
The tax exemption status expires on December 31, 2047.

Investor Example

- Investor sell 1,000 shares of XYZ company stock for $1.25 million on January 1, 2018.
- Their original basis in the stock is $250,000.
- The capital gains is $1 million and the capital gains tax owed would be $200,000.
- QOF invests the $1 million in real estate in Designated Opportunity Zones.

Date	Income Tax Benefits Received
By 6/29/2018	Investor buys $1 million worth of shares in Qualified Opportunity Fund (QOF). Original capital gains tax payment deferred for investing QOF.
6/30/2023	Investor can reduce the capital gains taxed owed by 10% or $20,000.
6/30/2025	Investor can reduce the capital gains taxed owed by another 5% or $10,000.
12/31/2026	Investor pay the original capital gains taxed owed of $170,000. Original capital gains tax of $200,000 - $30,000 tax reduction = $170,000.
12/31/30	Investor exits the QOF and receives $2.5 million. The appreciation of QOF or the new capital gain of $1.5 million is not taxed.

What Does This Mean As Fund?



- QOF must be set-up as corporation or partnership
- QOF must have 90% of the QOF's assets located in designated Opportunity Zones.
- Applies to acquisition of stock or property after December 31, 2017 and after the fund start date.
- 2 test dates per year – 6 months after the fund start and December 31.
- Fund self-certify with IRS on Form 8996.

What is Qualified Opportunity Fund (QOF)?

- Qualified Opportunity Fund (QOF) is an investment vehicle that is organized as a corporation or a partnership for the purpose of investing in Qualified Opportunity Zone Property (QOZP) in designated Opportunity Zones.
- QOF must invest 90% of its assets in QOZP and has 2 test dates each year.
  - Invest in subsidiary that operates a Qualified Opportunity Zone Business (QOZB) or
  - Operate QOZB directly holding Qualified Opportunity Zone Business Property (QOZBP).
- QOF can be organized in any state or U.S. Territory.

Overview of Proposed Regulations for Investing in Qualified Opportunity Fund (QOF)

On October 19, 2018, the Treasury Department published *Proposed Regulations* for Investing in QOF. The document offers direction and guidance on QOF including but not limited to:

- Type of gains that maybe deferred;
- Eligible taxpayers;
- Eligible entities;
- QOF requirements; and
- QOF certification process.

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Types of Gains Allowed

- U.S. taxpayer must sell an asset to an unrelated party that triggers a capital gain.
  - The asset sold does not need to be the same as the investment e.g. sale of real estate does not need to be reinvested in real estate.
- Only capital gains can be invested to receive income tax benefits.
- The capital gain must be reinvested in a QOF within 180 days of realizing the initial capital gain for an individual investor.
- Partnerships have different rules for the time of investment depending if the full partnership will reinvest or single partners.

List of Eligible U.S. Taxpayers to Defer Capital Gains Under the Opportunity Zones Program

- Individuals;
- Corporations;
- Regulated Investment Companies (RICs);
- Real Estate Investment Trusts (REITs);
- Partnerships;
- Trusts;
- Common trust funds;
- Estates; and
- Certain other pass-through entities.

How can one invest in OZ?

- Eligible U.S. taxpayers invest their capital gains in a Qualified Opportunity Fund (QOF) by buying equity shares in the QOF.
- The taxpayer must fill IRS Form 8949 to defer the capital gains.
- The QOF must be set-up as corporation or partnership.
- The QOF must invest 90% of its assets in OZ.
- Assets purchased or invested in by QOF must be after December 31, 2017.

Qualified Opportunity Fund (QOF) Certification Process

- A corporation or partnership self certifies as a QOF by using IRS Form 8996 which is filed with the QOF's tax return.
- A QOF must be formed and pick a start date and tax year before it can accept investment capital.
- IRS Form 8996 also serves as the reporting tool and ensures compliance with the 90% asset test.

Qualified Opportunity Fund Uses

Qualified Opportunity Fund has several ways to invest its funds. Below are a few examples:

- New construction of real estate;
- Substantial improvement of an existing building within an OZ;
- Expansion of a business already in OZ; or
- Opening new business in OZ.

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Investment Parameters

- QOF must have 90% of the QOF's assets located in designated Opportunity Zones.
- Applies to acquisition of stock or property after December 31, 2017.

Real Estate
The property must be "substantially improved" which means the improvements to existing building or the construction of a new building must equal or exceed the cost of the acquisition less the cost of land over a 30 month period.

Qualified Opportunity Zone Business (QOZB)
70% of the QOZB's tangible assets need to be used in the designated Opportunity Zone (OZ).
50% of the gross income from QOZB must be derived from the active conduct of the business in the OZ.
QOZB must be an operating business for substantially all of the QOF's holding period.

Working Capital Safe Harbor

- Qualified Opportunity Zone Business (QOZB) can hold reasonable amounts of cash, cash equivalents or debt instrument less than 18 months.
- In addition, QOZB can hold cash in safe harbor for tangible property if:
    - A written plan that identifies the financial property as property held for acquisition, construction or substantial improvement of the tangible property;
    - Property can be held for up to 31 months;
    - Written schedule of how the money will be used in the 31 months; and
    - Taxpayer retains the written plan for their records.

Ineligible Businesses

- Country Clubs;
- Liquor Stores;
- Golf Courses;
- Massage Parlors;
- Racetracks; or
- Gambling Venues.

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