Qualified Opportunity Zones Under the *Tax Cuts and Jobs Act*

Overview

- Provided under Internal Revenue Code (IRC) Sections 1400Z-1 and 1400Z-2
- Taxpayers may elect to defer recognition of capital gain realized on the sale to an unrelated party
- Requires a 180-day reinvestment of gain directly into a qualified opportunity (QO) fund
  - o A QO fund is a corporation or partnership that holds at least 90 percent of its assets in **QO zone property**
- Substantial improvements must be made to tangible QO zone business property, unless the property's original use is with the fund
- Deferral ends on the earlier of the date of the next sale or December 31, 2026
- After five years, taxpayers receive a basis step-up equal to 10 percent of the original gain
- After seven years, taxpayers receive an additional basis step-up equal to 5 percent of the original gain
- Taxpayers also may elect to permanently exclude the gain related to the appreciation on their QO fund investment after a 10-year holding period

> Heads up! **QO zone property** can include stock or partnership interests in a business where substantially all of the tangible property owned or leased is in the zone. Certain businesses are excluded, such as golf courses, country clubs and casinos.

Example

On August 15, 2018, Kate sold stock with a tax basis of $150,000 for $1.15 million. She reinvested the entire $1 million gain in a QO fund in a timely manner. Consider the following potential scenarios:

1) Kate sells the investment in October 2022 (year four); the entire $1 million deferred gain would be taxable.	**2)** Kate sells the investment in October 2023 (year five); only $900,000 of the deferred gain would be taxable.	**3)** Kate sells the investment in October 2025 (year seven); only $850,000 of the deferred gain would be taxable.	**4a)** Kate holds the investment through December 31, 2026 (the end of the temporary deferral period); she would recognize an $850,000 gain on her 2026 tax return.	**4b)** Kate sells the investment in October 2028 (year 10); she wouldn't recognize any additional gain (beyond the $850,000 recognized in scenario 4a).

In this example, if Kate keeps her QO fund investment for the full 10-year holding period (scenario 4b), the only tax liability associated with her investment would be on the $850,000 gain recognized at the end of the temporary deferral period on December 31, 2026. Any appreciation in value occurring after August 15, 2018, would be permanently excluded.

> Heads up! A taxpayer may either locate a QO fund in which to invest or create and self-certify a new fund. All zone property investments must go through a QO fund.

Additional Resource Links

- **Opportunity Zones Frequently Asked Questions**
- **Opportunity Zones Resources – Includes a map of all designated QO zones**
- **Notice 2018-48 – Designated Qualified Opportunity Zones Under IRC §1400Z-2**

What's Next?

The IRS and U.S. Department of the Treasury need to provide additional guidance regarding the specific requirements for opportunity zone and QO fund eligibility. At this time we're also waiting for the release of the self-certification form, which allows taxpayers to create a QO fund.

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