

Opportunity Zone update: Treasury, IRS issue proposed regulations



David M. Kall | Friday, November 9, 2018

Investors are now moving forward with investments in underserved “Opportunity Zone” areas that could generate tax-free returns under [proposed tax regulations](#) issued Oct. 19, 2018. Congress created the Opportunity Zone program last year through the Tax Cuts and Jobs Act to encourage investment in low-income areas. The proposed regulations provide investors with flexibility to attain federal tax benefits including the deferral and reduction or elimination of capital gains tax. Meanwhile, a legislative bill is pending in the Ohio General Assembly that, if enacted, would provide an additional 10 percent credit against the Ohio income tax.

THE OPPORTUNITY ZONE PROGRAM

The [Opportunity Zone Program](#) encourages investors to reinvest capital gain proceeds into an Opportunity Fund to benefit and develop low-income areas designated as Opportunity Zones. Overall, the Treasury Department has approved [8700 Opportunity Zones](#) in the U.S. In Ohio, there are 320 qualified Opportunity Zones, per interactive maps available on the Ohio Development Services Agency [website](#).

The Opportunity Fund is an investment vehicle organized as a corporation or partnership that must be funded with capital gain proceeds, invest in designated Opportunity Zones, and satisfy other requirements. If the fund invests in qualified opportunity zone property, 90% of its assets must be qualified opportunity zone property. Under the proposed regulations, fund investments in an operating business require 70 percent of the business’s assets to be qualified opportunity zone property to qualify. “Qualified

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opportunity zone property” includes qualified opportunity zone stock or partnership interests, as well as qualified opportunity zone business property.

The benefits available to investors include deferring and reducing the reinvested capital gain income (the deferred gain) and potentially eliminating any capital gain income generated through their investment in the Opportunity Fund. With respect to the deferred capital gain income, an investor may defer any tax owed on such capital gains until Dec. 31, 2026, or at an earlier time that the investor disposes of their investment. In addition, the investor may exclude 10 percent of their deferred gain after 5 years of investment and an additional 5 percent on the deferred gain after 7 years. If the investor holds their interest in the Opportunity Fund for 10 years, then the appreciation on that investment is generally exempt from federal income tax.

Suppose, for example, an investor made \$100,000 in capital gain income from the sale of marketable securities. The investor could defer this capital gain income by timely reinvesting an Opportunity Fund and reduce the gain by 10-15 percent depending on how long she held that investment. If she held the investment for 10 years, she would see a 15 percent reduction on the initial gain and deferral of that gain to Dec. 31, 2026. Any appreciation on the Opportunity Fund investment would be tax-free.

OHIO PONDS TAX CREDIT

In August 2018, Ohio Representative Kirk Schuring introduced [House Bill 727](#), which would provide investors with a 10 percent tax credit against the Ohio income tax for their Opportunity Fund investment. If enacted, the credit would amount to 10% of the amount of the qualifying investment for an Opportunity Zone located entirely in Ohio. The bill has not yet advanced through the legislative process, but we could see developments in the next General Assembly and potentially during the Ohio biennial budget process in 2019.

We will keep you posted as more developments emerge. According to federal Treasury Officials, more rules are expected later this year.



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