ISSUE LIST FROM 2-14-19 IRS HEARING ON OPPORTUNITY ZONE PROPOSED REGULATIONS

The following points were raised at the February 14, 2019 IRS hearing on the October 2018 proposed regulations addressing opportunity zones. It is not a comprehensive list and there are additional comments presented in written form that were not raised at the hearing.

The hearing took 5 hours, which included a 45-minute break. Great interest in the topic generated 90 minute check-in times. Twenty-two scheduled speakers presented and two additional speakers added comments. A transcript made available by Tax Notes is 213 double-spaced pages.

There is usually limited feedback from government representatives and a recitation of the some of the presenters written comments. Each presenter has ten minutes, with a light system to indicate remaining time.

A link to the Thompson Hine comment letter follows
https://www.thompsonhine.com/publications/opportunity-zones-and-start-up-tech-companies

With respect to the next set of IRS guidance, a government representative at the hearing commented that such guidance will hopefully see the light of day shortly.

1. For capital gains recognized during 2018, extend the 180-day period to invest such capital gains in Qualified Opportunity Fund (QOF) through the first 180 days of 2019. Comment made in connection with the uncertainty regarding implementation of the rules. In the same manner that members of partnerships/LLCs are given the first 180 days of 2019 to invest partnership 2018 capital gains, the same should be expanded and applied to all 2018 capital gains.

2. Remove requirement provided by the proposed regulations that 50% of the gross income of a qualified opportunity zone business is derived from the active conduct of a business <u>in the qualified opportunity zone</u>. Same point applies to requirement added by the proposed regulations that substantial portion of intangible property of opportunity zone business is used in the active conduct of a business <u>in the qualified opportunity zone</u>.

As has been stated in reported summaries of certain government feedback, the government representatives at the hearing seemed receptive to this request in the context of where the corporate opportunity zone businesses have their corporate headquarters, including working staff, within the qualified opportunity zone. However, the focus of concern were situations where the only tangible property within the opportunity zone were computer servers without any or very few employees and the servers provided operations for users outside the opportunity zone.

3. Rather than requiring GAAP reporting to test 90% and 70% requirements, allow for election to merely use unadjusted cost basis. This point was emphasized in the context of arrangements where existing land or buildings are leased to the operating entity. The request to allow for the use of the unadjusted cost amount would provide a zero amount allocated to the leasing arrangement. Otherwise, GAAP reporting would require present value of lease payments that would be too high and potentially impair the requirement that 70% of tangible property be qualifying property. Interesting, this comment was articulated clearly in the context of Indian Tribal lands that cannot be sold and can only be leased to the QOF or operating entity, but the same point arises in many ordinary leasing contexts.

4. Apply requirement that tangible property be substantially improved based on the aggregate tax basis of the tangible property acquired (other than land), and not require that substantial improvement need to occur as to each separate item of tangible property acquired.

Additional point is that if building is substantially improved, then the cost of the land should be included as qualifying property.

5. Address issue of permitting "suspended passive losses" associated with property sold and gain deferred in QOF investment. Suspended passive losses are triggered when gain is recognized but in the context of QOF investments, gain is deferred and partially excluded.

6. With respect to the 31-month safe harbor to maintain operating cash for building construction, provide additional time for delays based on events beyond the operating company's control, with specific reference to federally designated disaster areas. The same point was made with respect to start- up companies, along with making the 31-month safe harbor period for operating cash be available for non-real estate operations.

7. Allow QOF to sell interest in zone business or interest in operating entity, or have operating entity sell zone property and reinvest proceeds and permit deferred gain and tax free appreciation to continue uninterrupted.

8. Provide rules focusing on exit considerations. For example, rather than requiring sale of QOF interest allow for sale of operating company assets or QOF interests in operating companies and step up in tax basis of these assets if 10-year holding period is met. Also, permit debt-financed distributions to match step up in tax basis of QOF interest.

9. Allow for remediation and demolition costs to be included in substantial improvement calculation and extend the 31-month safe harbor when demolition is included. Also, if property is demolished allow entire new development to qualify as original use.

10. Provide QOF with 12 months to invest capital gain proceeds.

11. Any QOF reporting should be simple and unobtrusive.

12. Allow vacant land and property that has not been utilized for more than one year to qualify as original use within the opportunity zone.

13. When assets held in grantor trusts, allow for grantor to make election to make deferred gain election and allow grantor trust to invest in QOF. Also, if grantor dies before ten-year holding period, allow estate or beneficiary to make election for tax free appreciation.

We hope this abbreviated summary is useful.

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