

THE LATE SHOW: OPPORTUNITY ZONES

white + burke

VERMONT
DEVELOPMENT
CONFERENCE

The

LATE SHOW

(it's not too)



(to incorporate OZs into your development project)



featuring...



SHANNON LENZINI

AND



DREW KERVICK

Our first guest...



CBS/Viacom

... the Tax Cuts and Jobs Act of 2017.

Misleadingly Overly General Summary of Sec. 1400Z-2

1. Taxpayer must reinvest capital gains in a Qualified Opportunity Fund within 180 days
2. The Fund must timely invest and hold at least 90% of its assets in Qualified Opportunity Zone Property
3. Qualified Opportunity Zone Property:
 - Equity interest in qualifying business (active business, in zone, owns enough qualifying tangible property), or
 - Qualifying tangible property (purchased after 12/31/17, in zone, original use or substantially improved within 30 months)

Benefits:

- The taxpayer can temporarily defer tax on rolled over gains until December 31, 2026
- The taxpayer can reduce the tax on the rolled over gains by up to 15%
- The gains on the investment in the Fund are not subject to tax if held for at least 10 years

**TOP TEN
OPPORTUNITY ZONE
UPDATES, PITFALLS AND
POINTERS**



TOP TEN OZ UPDATES

**10. NEW LIFE FOR PROPERTIES
ACQUIRED BEFORE 1/1/18**

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10. NEW LIFE FOR PROPERTIES ACQUIRED BEFORE 1/1/18

General Rule:

(Statute)

Qualifying property must meet the following criteria:

1. Acquired by purchase from an unrelated party after December 31, 2017
2. During substantially of the holding period, substantially all of the use is in a zone
3. Original use of the property commences with the fund/qualifying business or the property is substantially improved during any 30 month period after acquisition

Leased Property:

(April 2019 Proposed Regulations)

Can be qualifying property, even if property acquired before January 1, 2018, if:

1. Lease entered into after December 31, 2017
2. Substantially all the use of the leased tangible property must be in zone during substantially all of the lease period
3. Lease must be “market rate” lease

No original use or substantial improvement requirement!

10. NEW LIFE FOR PROPERTIES ACQUIRED BEFORE 1/1/18 (CONT'D)

No requirement that property be leased from an unrelated party

(April 2019 Proposed Regulations)

However, if the lease is with a related party, the following additional criteria must be met:

1. Lease cannot be prepaid more than twelve months in advance.
2. For leased tangible personal property: Lessee must acquire tangible property that is qualifying property and has a value not less than the value of the leased personal property. The acquisition must occur during a period that begins on the date of possession and ends on the earlier of the last day of the lease or the end of the 30-month period beginning on the date that the lessee receives possession.

Anti-Abuse Rule:

(April 2019 Proposed Regulations)

For real property (other than unimproved land): If, at the time the lease is entered into by a Fund, there was a plan, intent, or expectation for the property to be purchased by the Fund for an amount other than the FMV of the real property, the leased real property does not qualify.

TOP TEN OZ UPDATES

10. NEW LIFE FOR PROPERTIES ACQUIRED BEFORE 1/1/18



TOP TEN OZ UPDATES

**9. NEW SAFE HARBORS FOR
THE GROSS INCOME TEST**

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9. NEW SAFE HARBORS FOR THE GROSS INCOME TEST

General Rule:

(Statute)

A **QOZB** must derive at least **50%** of its total gross income from the active conduct of business within a qualified opportunity zone

Area of Concern:

How will this Gross Income Test be satisfied?

New Safe Harbors:

(April 2019 Proposed Regulations)

1. At least 50% of the services performed (**based on hours**) by QOZB employees and independent contractors are performed within the zone
 - Best for businesses located in a zone that primarily provide services
2. At least 50% of the services performed (**based on amounts paid**) by QOZB employees and independent contractors are performed within the zone
3. The **tangible property** of the QOZB located in the zone and the **management or operational functions** performed in the zone are each necessary for the generation of at least 50% of the gross income of the QOZB
4. Based on all **facts and circumstances**, at least 50% of the gross income of a QOZB is derived from active conduct of a T or B in the QOZ

TOP TEN OZ UPDATES

- 9. NEW SAFE HARBORS FOR THE GROSS INCOME TEST
- 10. NEW LIFE FOR PROPERTIES ACQUIRED BEFORE 1/1/18



TOP TEN OZ UPDATES

**8. NEW GUIDANCE ON UNIMPROVED
LAND AND VACANT BUILDINGS**

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8. NEW GUIDANCE ON UNIMPROVED LAND AND VACANT BUILDINGS

General Rule:

(Statute)

To count as qualifying property, the **original use** of the property must commence with the Fund or qualifying business or the property must be **substantially improved** within any 30-month period after acquisition.

Unimproved Land:

(April 2019 Proposed Regulations)

Land can be treated as qualifying property only if it is used in a **trade or business** (within meaning of Section 162 of the Code) of a Fund or qualifying business.

The land generally does not have to meet the original use or substantial improvement requirements.

BUT: If the land is unimproved or minimally improved and a Fund or qualifying business purchases the land with an expectation not to improve the land “by more than an insubstantial amount” within 30 months after the date of purchase, then this special rule does not apply.



Matt York, AP



<http://www.omafra.gov.on.ca/english/landuse/gis/censusmaps.htm>

8. NEW GUIDANCE ON UNIMPROVED LAND AND VACANT BUILDINGS

Vacant Property:

(April 2019 Proposed Regulations)

If real property (other than land) has been unused or vacant for an “uninterrupted” period of at least 5 years, then successive use can qualify as “original use.”



TOP TEN OZ UPDATES

8. NEW GUIDANCE ON VACANT LAND AND BUILDINGS
9. NEW SAFE HARBORS FOR THE GROSS INCOME TEST
10. NEW LIFE FOR PROPERTIES ACQUIRED BEFORE 1/1/18

A man with white hair and glasses, wearing a dark suit, white shirt, and striped tie, is speaking. He is positioned in the center of the frame. The background is a nighttime cityscape with illuminated buildings and streets. The entire scene is enclosed in a yellow border.

TOP TEN OZ UPDATES

**7. CASH AND CASH EQUIVALENTS
CAN PUT THE “NON” IN NQFP**

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7. CASH AND CASH EQUIVALENTS CAN PUT THE “NON” IN NQFP

What is NQFP?

Cash, debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, annuities and other similar property

NQFP does not include:

Reasonable amounts of working capital held in cash, cash equivalents, or debt instruments with a term of 18 months or less

Why is it important?

An entity can only be a QOZB if less than 5% of the average of the aggregate unadjusted bases of its property is attributable to non-qualified financial property (“NQFP”)

But wait, isn't there a safe harbor?

Yes. Drew will talk about it next.

Even with the safe harbor that Drew will talk about, can NQFP still be a challenge in my project?

Yes. For example:

1. Certain industries – banking, insurance
What are *reasonable amounts* of working capital?
2. Certain types of projects - NMTC
3. Leases viewed as financing arrangements
4. Safe harbor applies to QOZBs, NOT QOZ Funds

TOP TEN OZ UPDATES

7. CASH AND CASH EQUIVALENTS CAN PUT THE “NON” IN NQFP
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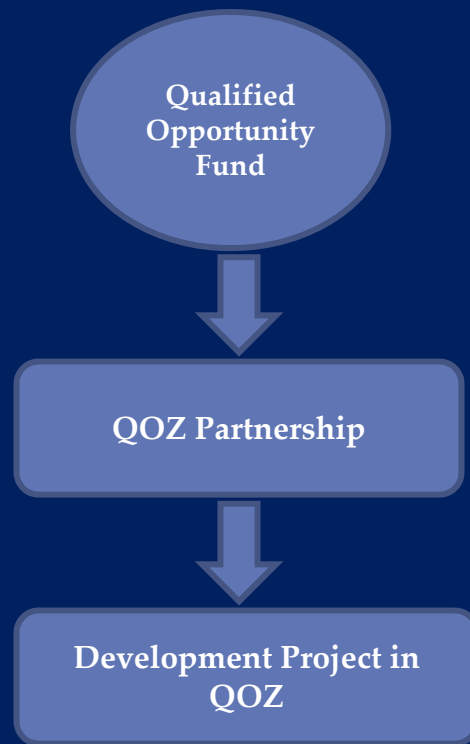


TOP TEN OZ UPDATES

**6. BEST PRACTICES FOR STRUCTURING
REAL ESTATE PROJECTS**

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6. BEST PRACTICES FOR STRUCTURING REAL ESTATE PROJECTS



Working Capital Safe Harbor: \$ held up to 31 months for the acquisition, construction or improvement of tangible property or the development of a trade or business, if the following is met:

- Intended uses are designated in writing
- Written schedule to spend funds within 31 months
- Used in a manner substantially consistent with the written plan/schedule

(October 2018 and April 2019 Proposed Regulations)

Less Stringent Asset Requirements:

A Fund must hold at least **90%** of its assets in qualifying property *(Statute)*

At least **70%** of a qualifying business's assets must be qualifying property *(October 2018 Proposed Regulations)*

Mixed OZ and Non-OZ Investor Projects:

Can improve administration, operation and efficiency in projects involving both OZ investors and non-OZ investors

TOP TEN OZ UPDATES

6. BEST PRACTICES FOR STRUCTURING REAL ESTATE PROJECTS
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TOP TEN OZ UPDATES



5. TRIPLE-NET IS A NO-NO

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QOZB as Landlord

(April 2019 Proposed Regulations)

- QOZB must be a T or B
- Active conduct
- Ownership and operation (including leasing) of real property is the active conduct of a T or B.
- “Merely” entering into a triple-net-lease with respect to real property owned by a taxpayer is not the active conduct of a T or B.

5. TRIPLE-NET IS A NO-NO



Possible fixes?

- Shift some operating responsibility and risk to the QOZB landlord.
- If multiple short-term leases on triple-net basis in multi-tenant building, might that be enough to demonstrate that landlord QOZB has active property management role and is not “merely” leasing?

TOP TEN OZ UPDATES

5. TRIPLE-NET IS A NO-NO
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TOP TEN OZ UPDATES

**4. NOW IS THE TIME TO THINK
ABOUT THE EXIT**

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4. NOW IS THE TIME TO THINK ABOUT THE EXIT

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2. Str

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<https://www.history.com/this-day-in-history/nixon-resigns>

Taxpayer

Partnership Interest in
Opportunity Fund

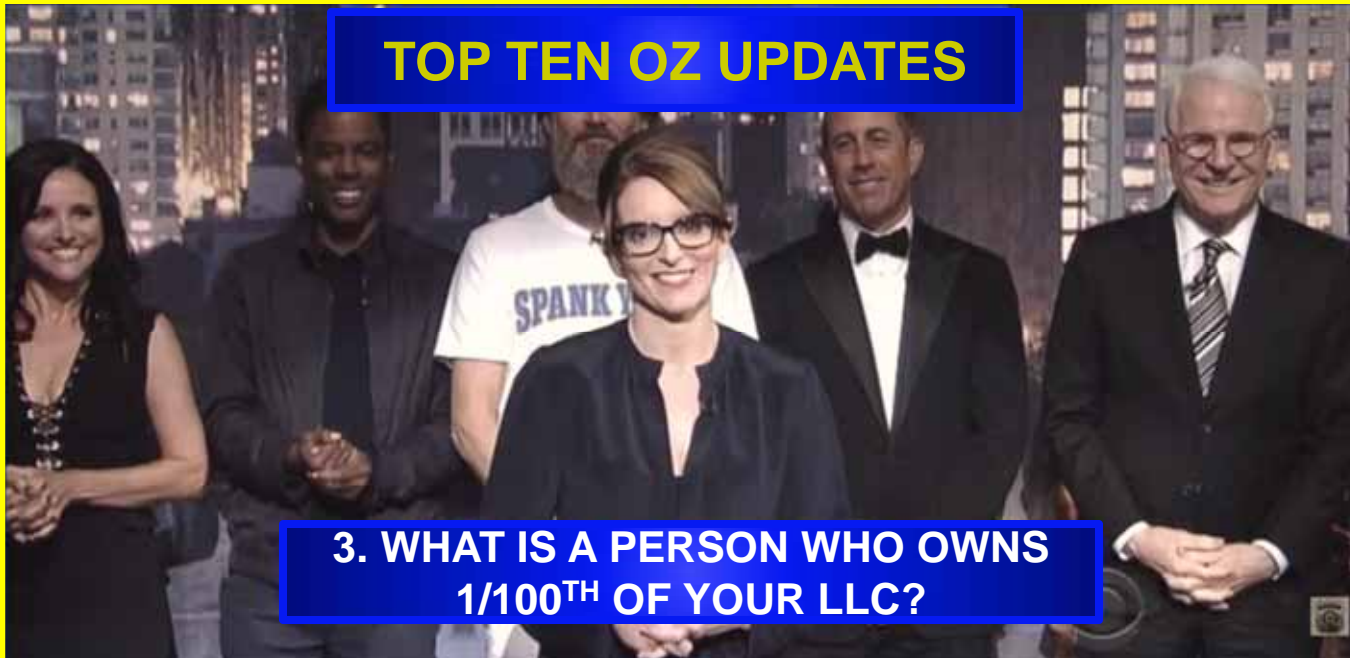
Partnership Interest in
QOZ Partnership

Assets in QOZ

TOP TEN OZ UPDATES

4. NOW IS THE TIME TO THINK ABOUT THE EXIT
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TOP TEN OZ UPDATES



3. WHAT IS A PERSON WHO OWNS
1/100TH OF YOUR LLC?

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3. WHAT IS A PERSON WHO OWNS 1/100TH OF YOUR LLC?

QOZF

Taxed as Corporation or Partnership

LLC – will have more than one member
(in order to be taxed as a partnership)

Operating Agreement should:

State that the entity is formed to be a
QOZF

Address control issues
Steve Jobs and Steve Wozniak

QOZB

Taxed as Corporation or Partnership

Control – how will this be handled?

In QOZB LLC, if QOZF is minority member – worry about the 10
years

In QOZB LLC, if QOZF is majority member – worry about minority
member

Build control provisions into the operating agreement to ensure that
the QOZB remains a QOZB for the 10-year compliance period
Bill Hewlett and Dave Packard

Ben

Jerry

TOP TEN OZ UPDATES

3. WHAT IS A PERSON WHO OWNS 1/100TH OF YOUR LLC?
4. NOW IS THE TIME TO THINK ABOUT THE EXIT
5. TRIPLE-NET IS A NO-NO
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TOP TEN OZ UPDATES

**2. SECURITIES LAWS
COMPLIANCE**

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2. SECURITIES LAWS COMPLIANCE

Whenever you solicit investors in a project, you must comply with federal and state securities laws. Most often this means identifying and complying with available exemptions from registration requirements.

Commonly utilized exceptions include:

Federal:

- Rule 506 (Preempts state law)
- Rule 504
- Regulation CF (Crowdfunding)
- Rule 147/147A (Intrastate Offerings)

Vermont:

- Accredited Investor
- Crowdfunding
- De minimis



Paramount Pictures

TOP TEN OZ UPDATES

2. SECURITIES LAWS COMPLIANCE
3. WHAT IS A PERSON WHO OWNS 1/100TH OF YOUR LLC?
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TOP TEN OZ UPDATES

1. TIMING IS EVERYTHING

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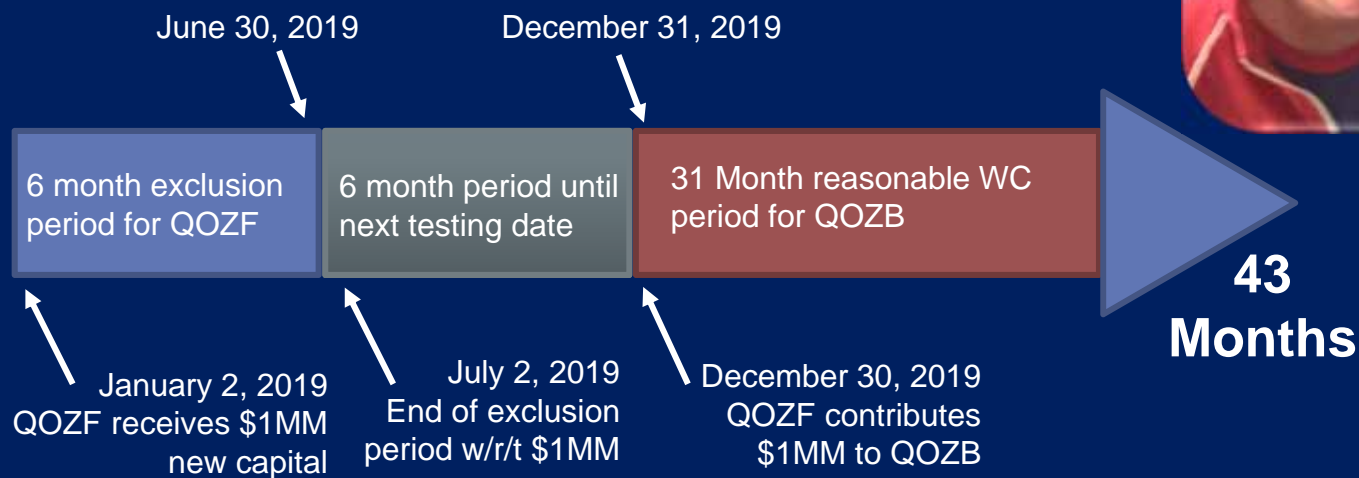
1. TIMING IS EVERYTHING

2. December 31, 2019

1. 6 Months

- OZ Fund can exclude contributed capital from the 90% test for 6 months after it is received
- Example:

90% Asset Testing Dates



TOP TEN OZ UPDATES

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QUESTIONS?

SPEAKERS

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