HAYNSWORTH SINKLER BOYD

OPPORTUNITY ZONE PROGRAM

CONTACT

CHARLESTON

134 Meeting Street, 3rd Floor
Charleston, SC 29401
P 843.722.3366

COLUMBIA

1201 Main Street, 22nd Floor
Columbia, SC 29201-3226
P 803.779.3080

FLORENCE

135 S. Dargan Street, Suite 300
Florence, SC 29506-2533
P 843.669.6002

GREENVILLE

1 North Main Street, 2nd Floor
Greenville, SC 29601-2772
P 864.240.3200

MYRTLE BEACH

2411 North Oak Street, Suite 305
Myrtle Beach, SC 29577
P 843.626.5700

HSBLAWFIRM.COM

INTRODUCTION

The Tax Cuts and Jobs Act (the "Act"), signed into law on December 22, 2017, included a new tax incentive to encourage private investment in low-income communities. Under the program, a taxpayer can defer and potentially reduce capital gain on the sale of property to the extent that the taxpayer reinvests the gain into an Opportunity Zone through a "qualified opportunity fund" ("O-Fund"). In addition, taxpayers may permanently exclude any gain realized from the post-acquisition appreciation of the taxpayer's investment in the O-Fund if the taxpayer holds the investment for at least ten years. On October 19, 2018, the Treasury Department and Internal Revenue Service issued regulatory guidance containing several important taxpayer-friendly provisions that should make the Opportunity Zones incentives easier to utilize.

WHAT IS AN OPPORTUNITY ZONE?

Opportunity Zones are economically-distressed U.S. census tracts that have been nominated by the governor of each state and designated by the U.S. Treasury Secretary as a Qualified Opportunity Zone under the Act. The State of South Carolina has 135 Qualified Opportunity Zones which can be viewed at www.scopportunityzone.com.

WHAT ARE THE TAX INCENTIVES?

The Opportunity Zone program includes three key incentives:

1. Deferral of Gain for Proceeds Reinvested in an Opportunity Fund

   The first tax incentive allows a taxpayer to defer the capital gain from the sale of any appreciated property to an unrelated person to the extent that proceeds from the sale are reinvested in an "O-Fund" within 180 days. The taxpayer recognizes the deferred gain on the earlier of the date that the taxpayer sells its O-Fund investment or December 31, 2026.

2. Partial Exclusion of Deferred Gain for Fund Investments Held for 5 Years and 7 Years

   A second incentive provides for a partial exclusion of the deferred gain for O-Fund investments held for a required period of time. For O-Fund investments held for five years, the deferred gain is reduced by 10%, and for O-Fund investments held for seven years, the deferred gain is reduced by 15%.

3. Complete Exclusion of Gain on Appreciation of Fund Investments Held for 10 Years

For O-Fund investments held for ten years, a third tax incentive allows the taxpayer to make an election to have the taxpayer's basis the O-Fund investment equal to the fair market value of the investment on the date the investment is sold. The effect of this provision is to exclude from the taxpayer's gross income all of the post-acquisition gain on the appreciation of the taxpayer's opportunity fund investment when the investment is sold.

WHAT DID THE TREASURY REGULATIONS CLARIFY?

The Treasury Department and Internal Revenue Service released proposed regulations as well as a Revenue Ruling on October 19, 2018. This guidance addressed a broad range of open issues and questions regarding the implementation of the Opportunity Zone program. Most notably, the proposed regulations adopted a "working capital" safe harbor. An O-Fund may invest in certain qualifying corporations or partnerships that can hold cash for up to 31 months pursuant to a written working capital plan. This safe harbor alleviated significant concerns about the ability to complete an underlying Opportunity Zone investment within the statutory time periods. Further, the proposed regulations clarified that an O-Fund may "self-certify." In contrast to community development enterprises in the context of new market tax credits, this self-certification process is substantially simpler than a procedure requiring Treasury Department or other federal agency approvals. In addition, Revenue Ruling 2018-29 addressed the "substantial improvement" requirement, pursuant to which taxpayers purchasing existing real estate in an Opportunity Zone must improve existing property in a manner that doubles the adjusted basis of the property within any 30-month period following the purchased of the property. The Revenue Ruling clarifies that the increased basis requirement only applies to the improvements on real estate, not to the underlying land, thereby making it much simpler to satisfy the "substantial improvement" rule.

CONCLUSION

The new Opportunity Zone incentives present tremendous planning opportunities for tax savings for taxpayers who are able to qualify for these incentives under the Act, and recent Treasury guidance is consistent with the underlying goal of the program to facilitate taxpayer investment in economically challenged areas. Considering that no deferral elections are allowed after December 31, 2026, that Opportunity Zone designations expire on December 31, 2028, and that the tax incentives for qualified fund investments are enhanced at 5-year, 7-year, and 10-year holding periods, taxpayers interested in obtaining Opportunity Zone tax incentives should begin planning with their tax advisors as soon as possible.

For more information on how you can take advantage of Opportunity Zone tax incentives, please contact Will Johnson, 803.540.7945 or wjohnson@hsblawfirm.com, or Scott Barnes, 843.720.4458 or sbarnes@hsblawfirm.com.