What tax incentives do Federal Opportunity Zones offer?

Federal opportunity zones offer three tax incentives to investors:

1. A temporary tax deferral for capital gains reinvested in an Opportunity Fund– the deferred gain is recognized on the earlier of the date on which the opportunity zone investment is sold or December 31, 2026.
2. A step-up in basis for capital gains reinvested in an Opportunity Fund– the basis of the original investment is increased by 10% if the investment in the qualified opportunity zone fund is held by the taxpayer for at least 5 years, and by an additional 5% if held for at least 7 years, excluding up to 15% of the original gain from taxation.
3. A permanent exclusion from taxable income of capital gains from the sale or exchange of an investment in a qualified opportunity zone fund, if the investment is held for at least 10 years.

How will the Federal Opportunity Zone Program Operate?

The US Treasury Department will certify who is a "Qualified Opportunity Fund" but the tax reform law defines this as a partnership or corporation formed for the purpose of making investments in businesses located in low-income communities designated as "Qualified Opportunity Zones." To gain the program benefits, an investor must invest proceeds from a sale or exchange of assets to an unrelated party into a Qualified Opportunity Fund within 180 days from the date of such sale or exchange. This investor may choose to reinvest only a portion of the proceeds from the original sale or exchange, in which case only a portion of the gain would be deferred. A Qualified Opportunity Fund is required to invest at least 90% of its assets in targeted businesses where substantially all of the tangible assets of each such business are used in a Qualified Opportunity Zone, and at least 50% of the gross income earned from each such business is from the active conduct of business in a Qualified Opportunity Zone. Opportunity Funds provide investors the chance to put that money to work rebuilding the low income communities.

Where will the Federal Opportunity Zone Program apply?

The tax reform law requires Governors' of each state to nominate qualifying census tracts to the Treasury Department by March 21, 2018. State Governors may nominate at least 25 census tracts but can only nominate 25% of a state's eligible census. Eligible census tracts must have a poverty rate of at least 20% or a median income that does not exceed 80% of the statewide income—following the New Market Tax Credit criteria. Up to 5% of census tracts that do not meet the definition of a low-income community can be designated under an exemption. Exempt census tracts must be contiguous with low-income community census tracts designated as Opportunity Zones, and the median family income of the exempt tract must not exceed 125% of the median family income of the designated low-income community census tract with which it is contiguous.