

COVID-19 Impact on Opportunity Zone Program Deadlines

PROFESSIONALS

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PRACTICE AREAS

Opportunity Zones

The IRS issued Notices 2020-18, 2020-20, and 2020-23 (“Notices” or “Notice”) in response to the COVID-19 crisis and CARES Act. These Notices are intended to provide some needed guidance, extended filing and compliance deadlines, and cash-flow relief to taxpayers struggling with this current economic environment. The following is a quick summary of these Notices and how Opportunity Zone investors may be able to benefit from:

1. an extended window for investing their capital gains into a Qualified Opportunity Fund (QOF),
2. an additional 24-month Federal Disaster extension of the standard 31-month working capital safe harbor and the “substantial improvement” period for a tangible property (if included in the written business plan), and
3. an extension of time to deploy Qualified Opportunity Zone Business (QOZB) funds into QOZB Property (QOZBP).

Notice 2020-18

- Postpones the due date from April 15, 2020, until July 15, 2020, for filing the vast majority of federal income tax returns and making Federal income tax payments otherwise due April 15, 2020

Notice 2020-20

- Provides additional relief by postponing specific Federal gift (and generation-skipping transfer) tax return filings and payments

Notice 2020-23

- Provides additional relief to affected taxpayers, as well as relief for specific time-sensitive actions and postponement of due dates in respect to specific

government acts

- Affected taxpayers are any persons (as defined in section 7701(a)(1) of the Code) with a Federal tax payment obligation, or a Federal tax return or other form filing obligation, which is due to be performed (initially or pursuant to a valid extension) on or after April 1, 2020, and before July 15, 2020, who are affected by the COVID-19 emergency
- For a detailed list of specific filing and payment obligations that have been extended by this Notice, see Section III, A. linked in the header
- Affected taxpayers with respect to Specified Filing and Payment Obligations, the due date for filing Specified Forms and making Specified Payments are **automatically** postponed until July 15, 2020
- Affected taxpayers who need additional time, can also file an extension form by July 15, 2020, but can not exceed the original statutory extension deadline (i.e., September 15 for pass-through entities and October 15 for Individuals, C Corporations, certain Trusts)
- Affected taxpayers have until July 15, 2020, to perform specified time-sensitive actions that did not expire before April 1, 2020, such as filing all petitions with the Tax Court, or for review of a decision rendered by the Tax Court, filing a claim for credit or refund of any tax, and bringing suit upon a claim for credit or refund of any tax
- For a detailed list of particular time-sensitive government actions please see Section III, D. linked in the header

Extension of 180-Day QOF Funding Deadline

IRS Notice 2020-23 provides a sliver of an extension for OZ investors who had a **direct** capital gain (e.g., that did not flow through on a K-1) that occurred after October 4, 2019. If the standard 180-day reinvestment period was set to expire between April 1, 2020, and July 14, 2020, Notice 2020-23 extends the deadline until July 15, 2020 – a small crumb for a handful of OZ investors. Various OZ trade groups and legislators are continuing to push for a longer extension.

Keep in mind that the final OZ regulations contain copious rules for when the 180-day period begins, and taxpayers should evaluate whether to apply the proposed regulations or elect the early application of the final regulations which can extend the QOF reinvestment period for capital gains that are reportable on December 31, 2019, until September 10, 2020. These rules are extremely complex and HCVT would be happy to answer any questions you may have.

Summary of Additional Working Capital Safe Harbor Relief Under the Final OZ Regulations

- While not addressed in the above mentioned IRS Notices, the final OZ regulations provided additional time and flexibility for OZ investors, making the OZ program even more attractive with the high volatility in the stock market, general economic uncertainty and a renewed focus on the long-term horizon

- The working capital safe harbor provisions are applicable at the QOZB subsidiary level, so managers of QOF's must generally drop 90% of their liquid assets held in the QOF down into the QOZB within the first 12 months of self-certifying the QOF
- Once the QOZB accepts these funds they have a minimum 31-month period to deploy the cash into QOZBP which can be either real estate, other tangible property, or active business. There is also a parallel 30-month period from the date the QOZB acquires **used** tangible property for the QOZB to make "substantial improvements" – generally met by doubling the cost basis in the asset values other than the land value.
- The 31-month working capital safe harbor period can easily extend to 62 months under the "start-up" business rules introduced in the final regulations

The preamble to the final regulations state:

- To qualify for a maximum 62-month working capital safe harbor period, a start-up business must receive multiple cash infusions during its start-up phase. Specifically, under the 62-month working capital safe harbor, a start-up business can qualify for a 31-month safe harbor period with respect to the business' first cash infusion. Taxpayers desiring this extra 31-month investment period should either drop funds from the QOF to the QOZB in at least two separate transactions or attempt to fund the QOF with two or more distinct funding steps
 - Upon receipt of a subsequent contribution of cash (subsequent cash infusion), the business can both (i) extend the original 31-month safe harbor period that covered the initial cash infusion, and (ii) receive safe-harbor coverage for the subsequent cash contribution for a maximum 31-month period, if the business satisfies the following two conditions
 - First, the subsequent infusions of working capital assets form an integral part of the plan covered by the initial working capital safe harbor period
 - Second, the working capital safe harbor plan for the subsequent cash infusion must form an integral part of the working capital safe harbor plan that covered the initial cash infusion.
- There is a reference to the secondary funding being more than a de-minimis capital infusion, but there are no specific thresholds provided. 10% would appear to meet the de-minimis test, but unclear at this point. The language in the regulations is as follows:
 - In addition, the 62-month working capital safe harbor features a minimum investment threshold for each subsequent cash infusion to ensure that a de minimis subsequent infusion does not unlock a subsequent 31-month period for previously covered tangible and intangible property.
- Even without the 62-month start-up provisions, there is also a provision in the second set of temporary regulations that will allow the 31-months to reset when you make secondary funding and document the expanded project. If you believe the project will be substantially completed within 31-months from the upcoming funding date, an investor could potentially be fine without meeting the 62-month test. The language in the regulations is as follows:

- The May 2019 proposed regulations also clarified that a business may benefit from multiple overlapping or sequential applications of the working capital safe harbor, provided that each application independently satisfies all of the requirements in proposed §1.1400Z2(d)-1(d)(5)(iv)(A) through (C) (multiple safe harbor rule). See proposed §1.1400Z2(d)-1(d)(5)(iv)(D). The Treasury Department and the IRS confirm that a QOZB may string together subsequent or overlapping working capital safe harbors with respect to the same tangible property.
- The combination of the minimum 180-day period for reinvesting the gain into a QOF, then the 12-month window for dropping funds into the QOZB, followed by the 31 or 62-month working capital safe harbor, certain OZ investors could have up to seven years to deploy all their QOF funds into OZ assets. **On top of that, the final regulations provide that, if an OZ project is Federally declared a disaster area [as defined in section 165(i)(5)(A)], the QOZB may receive up to an additional 24 months to deploy its funds for purposes of meeting the working capital safe harbors provided the project can be proven to be delayed due to the crisis.**
- It is also important to note that investors that sell their underlying QOZB investment have up to 12 months to reinvest all or a portion of their proceeds from the sale into the QOF and count that towards meeting the 90% qualified asset test. Any gain on sale will generally trigger tax in the year of sale.

As you can see, the OZ program is an amazingly flexible and long-term program that can provide investors extra time to make significant investment decisions. Its national footprint and broad economic development impact can offer both the public and private sectors an invaluable tool to assist with the upcoming economic recovery.

Various OZ trade groups and legislators are continuing to encourage Congress to enact further QOF funding extension, census tract modification, and a possible extension of the overall OZ program to deal with the unprecedented COVID-19 impact.

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