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February 12, 2019

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Section 199A Deduction

Presented by:

Alice Varisano, CPA – *Partner*

General

- Section 199A deduction applies to years beginning after December 31, 2017 and ending before January 1, 2026 Even though it is not clearly stated; it seems reasonable to conclude that the owner of a fiscal year business would be able to claim the full deduction for QBI
- Eligible taxpayers: Individuals, Trusts, Estates, Partnerships, S Corporations and Sole Proprietors ***discuss the types of trusts that it does not apply to***
- Taxpayers are generally eligible to claim a deduction equal to the lesser of:
  - 20% of qualified business income earned in a qualified trade or business, subject to certain limitations

General

- The deduction is limited to the greater of (1) 50% of the W-2 wages with respect to the trade or business, or (2) the sum of 25% of the W-2 wages, plus 2.5% of the unadjusted basis immediately after acquisition of all qualified property

- Qualified trades and businesses include all trades and businesses except the trade or business of performing services as an employee and "specified service" trades or businesses: those involving the performance of services in law, accounting, financial services, and several other enumerated fields, or where the business's principal asset is the reputation or skill of one or more owners or employees

General

- Qualified business income is the net amount of qualified items of income, gain, deduction, and loss with respect to a qualified trade or business that are effectively connected with the conduct of a business in the United States. However, some types of income, including certain investment-related income, reasonable compensation paid to the taxpayer for services to the trade or business, and guaranteed payments, are excluded from qualified business income.

Specified Service Exclusion

- A qualified trade or business includes any trade or business except for a Specified Service Trade or Business (SSTB)
- QBI generated from a SSTB is subject to exclusion if the taxpayers taxable income is greater than $315,000 for joint filers and 157,500 for other files
- The SSTB exclusion is subject to phase out for taxable income between $315,000 - $415,000 for joint filers and $157,500-207,500 other filers

Specified Service Exclusion

Businesses

- Health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services
- New regulations just came out two weeks ago that further defines specific businesses that fall within and without SSTB (not all comprehensive, but a good start)
- Any trade or business where the principal assets are the reputation and skill of one or more of its employees or owners or
- Involves the performance of services that consist of investing and investment manager trading, or dealing in securities, partnership interests or commodities

Clarification in New Regulations on SSTB's

- Rental Real Estate activity as a §162 trade or business for purposes of §199A
- Notice 2019-07 is a proposed revenue procedure detailing a proposed safe harbor to treat rental real estate as a trade or business subject to the 20% QBI deduction
  - At least 250 hours of services are performed each year
  - This includes services performed by owners, employees and independent contractors
  - Time spent on maintenance, repairs, collection of rent, payment of expenses, provision of services to tenants and efforts to rent property
  - Hours spent by any person with respect to arranging financing, procuring property, reviewing financials, planning, constructing capital improvements, traveling--does not constitute hours of service eligible for the QBI deduction.

Continued

- The proposed safe harbor would also require separate books and records, and separate bank accounts, be maintained for the rental real estate enterprise
- Property leased under a triple net lease or used by the taxpayer as a residence for any part of the year would not be eligible

Special Rule for Renting Property to Related Party

- The rental or licensing of tangible or intangible property to a related trade or business is treated as a trade or business if the rental or licensing activity and the other trade or business are commonly controlled.
- Related Party is defined under § 267(b) or § 707(b)
- This rule also allows taxpayers to aggregate their trades or businesses with the leasing or licensing of the associated rental or intangible property if all of the requirements of § 1.199A-4 are met.

Computational Rules

- The proposed regulations provide that if an individual's QBI from at least one trade or business is less than zero, the individual must offset the QBI attributable to each trade or business that produced net positive QBI with the QBI from each trade or business that produced net negative QBI in proportion to the relative amounts of net QBI in the trades or businesses with positive QBI
- The aggregation rules provided in § 1.199A-4 are optional and are intended to assist taxpayers in applying the W-2 wage and UBIA of qualified property limitations

W-2 Wages

- Revenue procedure 2019-11 provides three methods for calculating W-2 wages, for purposes of §199A(b) and the regulations thereunder. The first method (the unmodified Box method) allows for a simplified calculation while the second and third methods (the modified Box 1 method and the tracking wages method) provide greater accuracy.
- W-2 wages calculated under this revenue procedure are not necessarily the W-2 wages that are properly allocable to QBI and eligible for use in computing the §199A limitations. As mentioned above, only W-2 wages that are properly allocable to QBI may be taken into account in computing the § 199A(b)(2) W-2 wage limitations. Thus, after computing W-2 wages under this revenue procedure, under § 1.199A-2(b)(3), the taxpayer must determine the extent to which the W-2 wages are properly allocable to QBI. Then, the properly allocable W-2 wages amount is used in determining the W-2 wages limitation under § 199A(b)(2) for that trade or business as well as any reduction for income received from cooperatives under § 199A(b)(7).

Compensation

- The Treasury and IRS stated in the preamble to the proposed regulations payments under guaranteed payments, reasonable compensation and wages none of which are includible in QBI.
- Treasury and IRS clearly excludes reasonable compensation paid to a taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business from QBI.
- Guaranteed payments and payments to independent contractors are not W-2 wages and cannot be counted for purposes of the W-2 wage limitation

Aggregation Rules

- The proposed regulations provide rules that allow a taxpayer to aggregate trades or businesses based on a 50% ownership test, which must be maintained for a majority of the taxable year.
- The majority of the taxable year must include the last day of the taxable year.
- To determine whether trades or businesses may be aggregated, the proposed regulations provide that multiple trades or businesses must, among other requirements satisfy two of three listed factors:
  - The businesses provide products and services that are the same
  - The businesses share facilities or share significant business elements
  - The businesses are operated in coordination with, or related to other businesses

Aggregation

- The proposed regulations require consistent reporting of aggregated trades or businesses. Each individual who chooses to aggregate must attach a statement to their return annually identifying each trade or business to be aggregated.
- Final regulations do not generally allow for an initial aggregation to be made on an amended return as this would allow aggregation decisions to be made with the benefit of hindsight.
- A taxpayer who fails to choose not to aggregate in Year 1 can still choose to aggregate in Year 1 but cannot amend to choose to aggregate.

Aggregation

- The IRS allows initial aggregations to be made on amended returns for 2018 because of the lateness of the forms.
- However the final regulations retain the annual disclosure requirement and in order to provide flexibility as forms and instructions change, allow the Commissioner to require disclosure of information on aggregated trades or businesses as provided in a variety of formats.
- The proposed regulations permit the Commissioner to disaggregate trades or businesses if a taxpayer fails to attach the annual disclosure.

Specified Service Trade or Business

- Further clarified certain specific ones in the regulations:
  - Health—skilled nursing, assisted living, and similar facilities provide multi faceted services to their residents.
  - Outpatient surgical center is not a SSTB
  - Sale of pharmaceuticals and medical devices by a retail pharmacy is not by itself a SSTB; there are some examples in the final regs whereby a pharmacist is performing services in the field of health
  - Treasury and IRS believe it is appropriate to continue to treat veterinary services as the performance of services in health.

SSTB

- Physical therapists are within the health related SSTB
- Accounting
  - Includes the common understanding of accounting, tax returns, bookkeeping services, attest functions, review functions
- Actuarial Science
  - The preamble to the proposed regulations, the field of actuarial science, does not include the provision of services by analysts, economists, mathematicians and statisticians not engaged in analyzing or assessing the financial cost of risk or uncertainty of events

SSTB

Performing Arts

- To the extent that a writer is paid for written material, such as a song or screenplay, this is integral to the creation of the performing arts, the writer is performing services in the field of performing arts.

Consulting

- Personnel agencies are not a SSTB

Consulting

- The performance of services in the field of consulting means the provision of professional advice and counsel to clients to assist the client in achieving goals and solving problems.
- Excludes the performance of services other than providing advice and counsel from the field of consulting.
- At issue is whether advice and counsel is provided in the context of the provision of goods or services….that is a question of facts and circumstances.
- Consulting services that are separately billed are generally not considered to be provided in the context of the provisions of goods and services.

Financial Services

- Insurance cannot be considered a financial service for purposes of §199A
- Managing wealth, advising clients with respect to finances and other advisory services, even if provided by insurance agent, can be considered a SSTB. However if these services are ancillary to the commission based sale of the insurance policy, it will not be considered financial services for the purposes of § 199A.
- Financial services does not include taking deposits or making loans.
- Banking for the most part will be treated as a SSTB

Reputation/Skill

- Final regulations limits the meaning of reputation and skill clause to fact patters in which an individual or RPE is engaged in the trade or business of receiving income from endorsements, the licensing of an individual's likeness or features and appearance fees.

De Minimus Rule

- A trade or business with gross receipts of 25 million or less is not an SSTB if less than 10 percent of the gross receipts of the trade or business are attributable to a SSTB
- The percentage is reduced to 5 percent if gross receipts are greater than 25 million

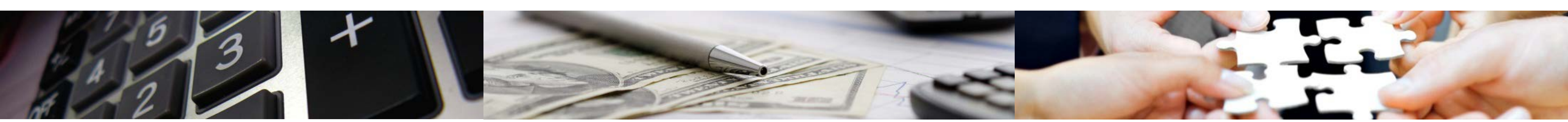
Services or Property Provided to an SSTB

- A trade or business that provides more than 80 percent of its property of services to an SSTB is treated as an SSTB if there is 50% or more common ownership of the trades or businesses

C Corp vs. S Corp

Presented by:

Jeffrey G. Cohen, CPA – *Partner, Tax Services Leader*



C Corp vs. S Corp

- Questions:
  - Do you have substantial taxable income?
    - If yes, continue
  - Are you selling within 5 years? If yes, don't convert to C
  - Are you holding the stock until you pass away? C Corp and step up in basis to make equivalent to being an S corp.
  - Have you already done estate planning: If yes, then using Martins Ice Cream case to sell goodwill outside of the company (C Corp double tax) will increase your estate tax liability.
  - Are you growing your company? If not you will run into accumulated earnings and profits tax.
  - ESOP?
  - Do you have foreign competition coming into the USA due to the tax law change?

C Corp vs. S Corp Tax Rates

- C Corp tax rate 21% vs effective flow through rate of 29.6%
- C Corp Double tax on Qualified Dividends to federal and state
- C Corp zero step up in basis on undistributed income vs S Corp
- C to S Built in Gains tax of 18% for 5 years after new S Election(21% highest C Corp rate less federal deduction for Built in gains taxes paid)
- C Corp accumulated earnings tax on undistributed retained earnings. Need a growth plan or IRS will have deemed dividends
- NYS one factor allocation (sales) for C Corps
- State taxes deductible to C Corps, not S Corp Shareholders

Excess Business Losses

Presented by:

Jeffrey G. Cohen, CPA – *Partner, Tax Services Leader*

Excess Business Losses for Noncorporate Taxpayers– New Law

- Excess business losses of noncorporate taxpayers are not allowed for tax years beginning after December 31, 2017, and before January 1, 2026. Any excess business loss that is disallowed is treated as a net operating loss (NOL) carryover to the following tax year
- Noncorporate taxpayers must apply the passive activity loss rules before application of the rules for excess business losses
- An "excess business loss" is the excess, if any, of:
  - The taxpayer's aggregate deductions for the tax year from the taxpayer's trades or businesses, determined without regard to whether or not such deductions are disallowed for such tax year under the excess business loss limitation; over the sum of the taxpayer's aggregate gross income or gain for the tax year from such trades or businesses, plus $250,000, or 500,000 MFJ
- For partnerships and S corporations, the limit on excess business losses is applied at the partner or shareholder level – HENCE if MFJ, then can only deduct 500K loss in any given year.

Excess Business Losses for Noncorporate Taxpayers– New Law

Example:

For 2018, Ned has $1 million of gross income and $1.4 million of deductions from a retail business that is not a passive activity. His excess business loss is $150,000 ($1,400,000 − ($1,000,000 + $250,000)). Brown must treat his excess business loss of $150,000 as an NOL carryover to 2019.

NOL Deduction

- The Act limits the NOL deduction to 80% of taxable income and provide that amounts carried to other years be adjusted to account for the limitation for losses arising in tax years beginning after December 31, 2017
- The Act eliminates carrybacks and allows unused NOL's to be carried forward indefinitely
- The act Bifurcates NOL's into two components:

1. Pre 2018 NOL's in which you carryover without the 80% taxable income limitation (20 years). No Change
2. Post 2018 NOL's which are limited to 80% of taxable income but carryover in perpetuity.

Current Tax Developments in Estates & Trusts

Presented by:

Jeffrey G. Cohen, CPA – *Partner, Tax Services Leader*



Estate & Gift Tax Basics

- Tax on Transfer of Assets-through gifting or at death
- Cumulative tax base
- Generation Skipping Tax
- Annual per person exclusions $15,000
- Splitting Gifts
- Permanent exclusions for Dynasty Trusts

Tax Reform Changes

- Exemption increased- approximately $11,180,000 per person per year
- Increase sunsets after 2025, reverts back in 2026
- Step up in basis not changed
- Cost of living adjustment calculation change

Estate Tax Changes Made by 2001 Tax Act

ESTATE TAX	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Exclusion	675,000	1,000,000	1,000,000	1,500,000	1,500,000	2,000,000	2,000,000	2,000,000	3,500,000	repealed	1,000,000
Top Rate	55%	50%	49%	48%	47%	46%	45%	45%	45%		

GIFT TAX	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Exclusion	675,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Top Rate	55%	50%	49%	48%	47%	46%	45%	45%	45%	35%	

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Federal Exclusion Compared to New York

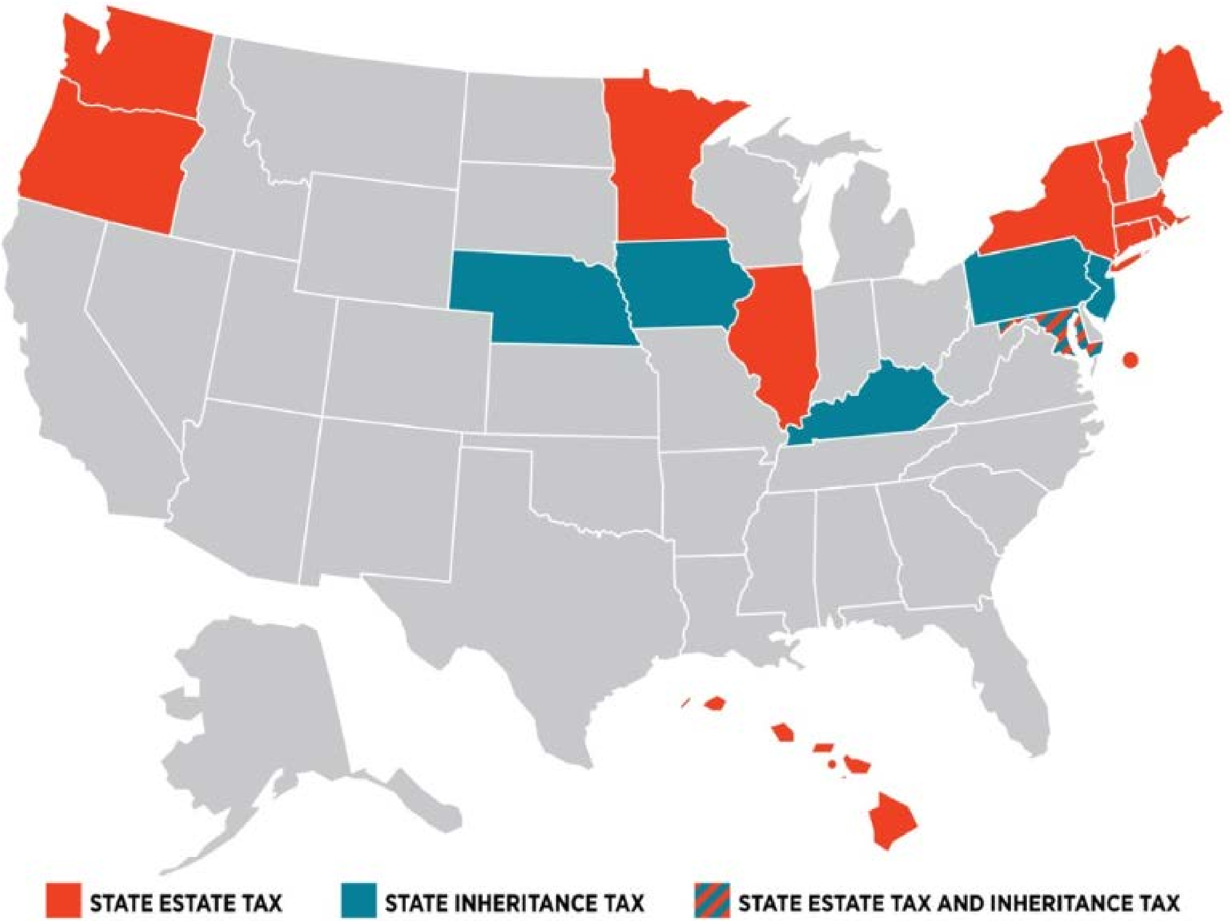
Date of Death	Federal Exclusion		NY Exclusion	Difference
1/1/17 - 4/1/17	5,490,000		4,187,500	1,302,500
4/1/17 - 12/31/17	5,490,000		5,250,000	240,000
1/1/18 - 12/31/18	11,180,000	*	5,250,000	5,930,000
1/1/19 - 12/31/2025	11,180,000	*	5,600,000	5,580,000
1/1/2026 +	5,600,000	*	5,600,000	-

- Inflation adjustments unknown at this time
- NYS exemption phases out when estate is105% of exemption

New Jersey Estate and Inheritance Tax

- New Jersey Estate Tax Repealed Effective 1/1/2018
- New Jersey Retains Inheritance Tax
- Inheritance Tax is Tax on transfer of Assets to certain Beneficiaries still living in NJ
- Inheritance Tax rate 11% - 16% based on beneficiary class
- No Inheritance Tax due for assets passing to surviving spouse or lineal descendent

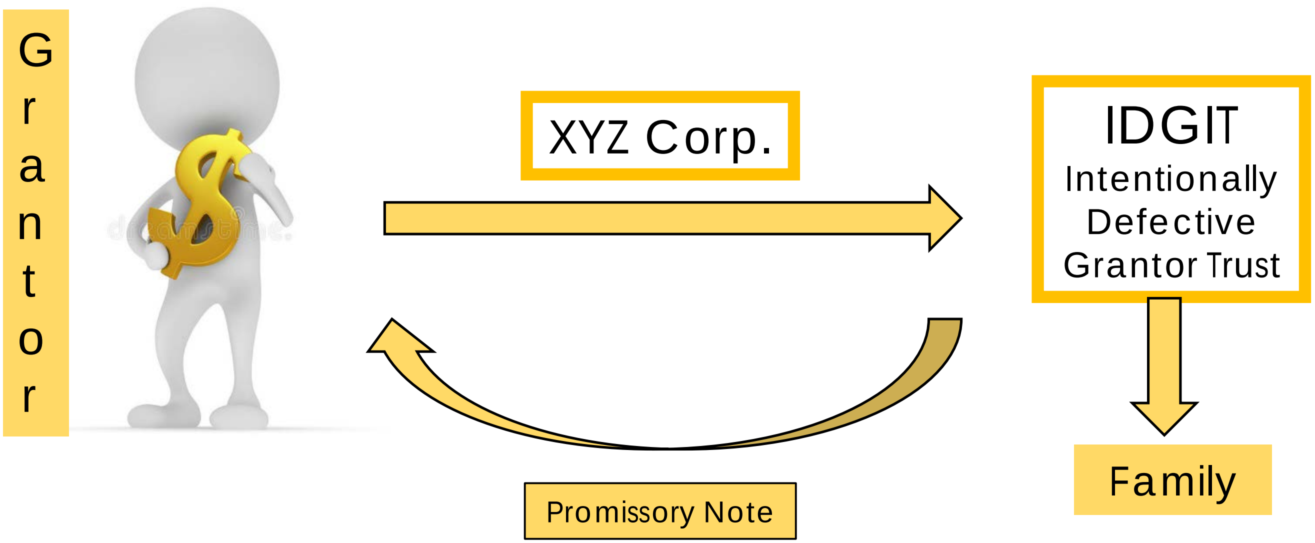
State Estate and Inheritance Taxes in 2018



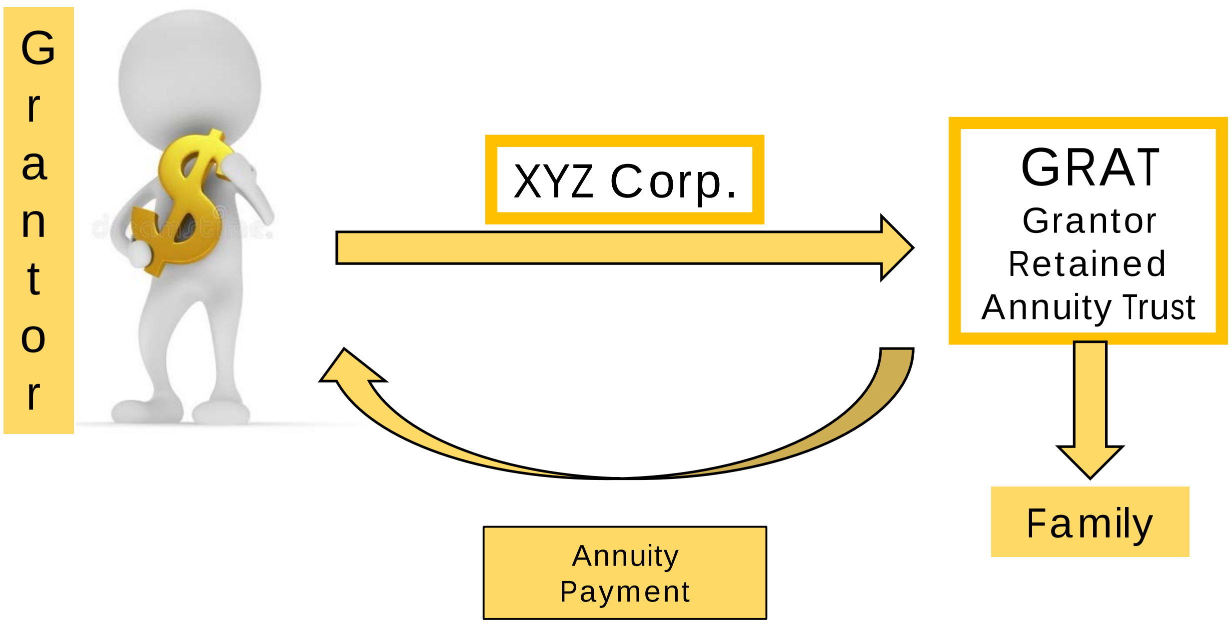
Planning Tools

- Intentionally Defective Grantor Trusts- "IDGIT"
- Grantor Retained Annuity Trusts "GRAT"
- Decant existing trusts for estates < than $11 or 22 million

Intentionally Defective Grantor Trust



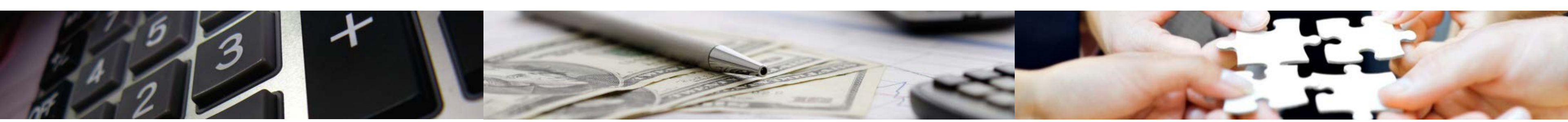
Grantor Retained Annuity Trust



Qualified Opportunity Zones

Presented by:

Raymond Haller, CPA – *Tax Partner*



Opportunity Zone Program

- The Opportunity Zone program was created by the Tax Cuts and Jobs Act in 2017 (TCJA) to stimulate economic development and job growth in low income communities across the US, DC and the five US territories by providing tax breaks to investors in the qualified zone areas.
- Localities qualify as Opportunity Zones if they have been nominated by the head of each state, district or possession and have been certified by the Secretary of the U.S. Treasury via their delegation of authority to the Internal Revenue Service
- Qualified Opportunity Zones can be found in the Federal Register at IRB Notice 2018-48
- Another valuable resource that provides access to the lists of all the designated opportunity zones and an interactive map of these zones can be found at https://www.cdfifund.gov/Pages/Opportunity-Zones.aspx
- This could be a game changer for distributors and manufacturers as well as investors

Tax Incentives Offered by the Program

- Tax Deferral of Reinvested Capital Gains for Federal Income Tax Purposes
- Potential Step-up in Basis/Permanent Exclusion of a Portion of the Deferred Gain
- Potential Permanent Exclusion of Post-Acquisition Appreciation in Investment
- Related Party rules put in place to prevent potential for abusive strategies in creating capital gains to be used as capital invested in Opportunity Zones

Tax Deferral

- Most capital gains can be deferred with tax savings to the taxpayer until 12/31/2026 or until the investment in the Qualified Opportunity Fund (QOF) is sold, whichever is earlier, if the original capital gains are invested in a QOF within 180 days of the sale of the asset.
  - Gain from sale or exchange of assets between related parties as provided in the proposed regulations does not qualify
  - Investment in QOF must be an equity interest and cannot be a loan or another debt instrument
  - The deferred gain retains its attributes, special rules for IRC Sec 1256 contracts

Tax Deferral

- With respect to owners of a pass-through entity where the entity does not make the election, the entity owners make elect to treat its 180-day period as beginning on the pass-through's 180 day period OR the 180-day may begin on the last day of the pass-through entity. There is further discuss to possibly changing this to the date the pass-through entity return is filed with the IRS.

Step-Up in Basis

- The basis in the capital gains invested in the QOF is increased by –
  - 10% if the taxpayer holds the QOF investment for at least 5 years
  - 15% if the taxpayer holds the QOF investment for at least 7 years
- Thus, the taxpayer can defer and effectively exclude up to 15% of the original capital gains from taxation.

Permanent Exclusion

- The capital gain on the sale or exchange of the investment in the QOF can be permanently excluded from taxation if the QOF investment is held for at least 10 years.

- Since designated QOZ's will expire at the end of 2028, the proposed regulations provide a provision that the taxpayer may make an election to adjust the basis in the property to fair market value upon a sale of a Qualified Opportunity Fund interest at any time on or before December 31, 2047, even if the designation of the QOZ has ceased to be in effect.

Permanent Exclusion

- Proposed Regulations state that it is possible to invest other capital, not from capital gains, into a QOZ, but these funds must be kept separate from the funds invested from capital gains. Also in connection with the permanent exclusion from gain for investments held over 10 years, the capital invested with funds not from capital gains, will NOT qualify for the permanent exclusion. This means that investors are only eligible for the step-up in basis to the extent the appreciation on a QOF investment is attributed to deferred gain.

Example

- John has a capital gain of $ 100,000 from sale of Apple stock as on 7/1/18
- He invests $100,000 in QOF on 11/1/18 (within 180 days of 7/1/18) - Does not pay any tax on the entire gain for 2018
- Holds the QOF investment until 11/30/23 (past 5 years) and sells the QOF investment at a gain of $15,000
  - Gets a step-up in basis of 10% or $10,000 on the original gain and pays tax only on the remainder of the original gain of $90,000. The $15,000 gain (115K sales price) on the sale of QOF investment is also subject to tax in 2023.
- Holds the QOF investment until 11/30/25 (past 7 years) and sells the QOF investment at a gain of $25,000 (same 125K sales price)
  - Gets a step-up in basis of 15% or $15,000 on the original gain and pays tax only on the remainder of the original gain of $ 85,000. The $ 25,000 gain on the sale of QOF investment is also subject to tax in 2025.
- Holds the QOF investment until 11/30/28 (past 10 years) and sells the QOF investment at a gain of $85,000
  - The $85,000 gain on the sale of QOF investment is permanently excluded from taxation. Must pay tax on the deferred gain of $85,000 (100K apple deferred gain less 15% step up for holding 7 years) in 2026.

Sec 1031 Exchange for Real Estate

- Tax deferral to the extent of sales proceeds invested
- Considerations of taxable boot
- Step-up in basis only upon death of the investor. Older investors may want to use sec 1031 exchange vs QOF investments.
- Investment restricted to like - kind property
- 1031 does not have a geographic limitation area like the QOZ does

QOF Investments

- Tax deferral available on investment of the capital gains instead of the sales proceeds. Better cash flow available to the taxpayer.
- Incremental step-up in basis available after 5/7/10 year holding period
- Investment needs to be in a QOF
- Proposed regulations have briefly considered the impact regarding the reinvestment of gain from the sale or exchange of a QOF into another QOF. In this situation it is believed that the taxpayer must completely dispose of their interest in the first QOF and reinvest all the proceeds into the next QOF within 180 days in order to be able to maintain the deferral on the original deferred capital gain. Further guidance is expected on this topic from the IRS.

Qualified Opportunity Zones (QOZ)

- An Opportunity Zone is a low-income census tract with an individual poverty rate of at least 20% and median family income no greater than 80% of the area median.

- Online Resources to find Qualified Opportunity Zones
  - https://eig.org/opportunityzones

Qualified Opportunity Funds (QOF)

- Must be formed as a partnership or a corporation for the purpose of investing in QOZ property
- Must hold average of 90% of its assets in QOZ measured semiannually. Provision for Working Capital Safe Harbor for QOF investments in QOZ businesses that acquire, construct or rehabilitate real or other tangible QOZ business property.
- Cannot invest in another QOF
- Self-certify as a QOF by filing Form 8996 with its tax return
- Must hold property in designated zone area and avoid the pitfall of being outside the zone even if slightly

Pre-Existing Entities

- Pre-existing entity may qualify as a QOF or as the issuer of a QOZ stock or partnership interest subject to certain requirements of sec 1400Z-2(d).

- It seems difficult for pre-existing entities to qualify due to tangible property acquired prior to 12/31/17 since the definition of qualified opportunity zone business property requires property to be used in a QOZ and also requires new capital to be employed in a QOZ.

Qualified Opportunity Zone Business (QOZB)

A trade or business that satisfies the following requirements is considered a QOZB-

- Acquires QOZ business property by purchase from unrelated parties
- Acquires (original use) or substantially improves the QOZ business property in the QOZ
- During substantially all of the holding period of the tangible property substantially all of the use of the property is in the QOZ – substantially all has been defined as 70% of the business property
- Derives at least 50% of its gross income from an active trade or business in the QOZ
- Substantial portion of intangible property is used in the active trade or business in the QOZ

Qualified Opportunity Zone Business (QOZB)

- Less than 5% of the average aggregate unadjusted bases of the entity's property is attributable to non-qualified financial property (NQFP includes debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, notional principal contracts, annuities and other similar property).
- The business is not described in Sec 144(c)(6)(B) (Excluded "Sin" Businesses)
- A trade or business of an entity is treated as satisfying the substantially all requirement above if at least 70% of the tangible property owned or leased by the trade or business is qualified opportunity zone business property

Excluded “Sin” Businesses

- Liquor stores
- Gambling facilities
- Golf Courses
- Country Clubs
- Massage parlors
- Hot tub facility
- Suntan facility
- Racetracks

Qualified Opportunity Zone Property (QOZP)

- QOZ stock acquired after 12/31/17 if an entity is classified as a corporation or partnership and is a QOZ business

Qualified Opportunity Zone Business Property (QOZBP)

Tangible property used in a trade or business of the QOF if:

- Such property was acquired by the QOF by purchase after December 31, 2017
- The original use of such property in the QOZ commences with the QOF or the QOF substantially improves the property
- During substantially all of the QOF's holding period for such property, substantially all of the use of such property was in a QOZ

Substantial Improvement

- Tangible property is treated as substantially improved by a QOZ business only if, during any 30-month period beginning after the date of acquisition of such tangible property, the QOZ business makes an additional investment of at least it's original basis in the QOZBP. Land on which the building is situated is excluded from the substantial improvement requirement.
- **Tactical move:** if investing 1MM, invest 500K on day one and another 500K within 30 months, know your own personal cash flow prior to jumping in.

Risks

- Market fluctuations
- Liquidity issues
- Business risk
- Potential decline in property values due to investors selling their investments all at once at the end of the 10 year period "rush to the exit"
- Unresolved issues regarding penalties for the 90% test of the Fund
- Unresolved partnership tax issues which hopefully the next round of tax regulations will address
- QOF may need to consider whether its operating agreement should provide for tax distributions at the end of 2026 to account for the deferred gain that will be recognized by investors that year or at least potential investors should be made aware of the tax consequences of investments

QOZ Examples

- **Example**: James bought unimproved property in Utah during 2000 for $1 million. On April 1, 2018, James sold the same property in Utah for $2 million. James will recognize $1 million of long-term capital gain. James can make an election with respect to the $1 million of long-term capital gain realized on the sale if James invests $1 million in a QOF within 180 days of April 1, 2018. The remaining $1 million of proceeds received by James in the sale of the property in Utah is not eligible for the tax incentives.

QOZ Examples

- **Example**: Same as example above, except James invests the entire $2 million of proceeds received from the sale of property in Utah in a QOF before the expiration of the 180-day period and makes an election with respect to the $1 million of gain. James is treated as making two investments in the QOF: one investment of $1 million of capital gain for which the election to defer the gain is made and that is eligible for the tax incentives, and another investment of $1 million that is treated like any other investment with no incentives.

QOZ Examples

- **Example**: On January 1, 2019, a calendar year Partnership realizes a capital gain, and the Partnership decides not to make an election to defer the gain. If any individual partner in the Partnership wants to make an investment in a QOF to defer their distributive share of the Partnership's eligible gain, they can either make the investment within the 180-day period beginning on January 1, 2019, or within the 180-day period beginning on December 31, 2019.

QOZ Examples

- **Example**: James sells stock in investment portfolio on January 1, 2019, and recognizes $1 million of long-term capital gain. James makes an equity investment in a QOF of $1 million and makes the election with respect to the $1 million of long-term capital gain. James's initial basis in the QOF is zero. On January 1, 2024, James's tax basis in the investment in the QOF increases to $100K, and on January 1, 2026, James's tax basis in its investment increases to $150K. On December 31, 2026, James still holds his investment in the QOF when his investment in the QOF is valued at $3 million. James recognizes $850K of long-term capital gain on December 31, 2026. James's tax basis in his investment in the QOF is increased by $850 to $1 million.

QOZ Examples

- **Example**: The same as the immediately preceding example, except on December 31, 2047, James sells his interest in the QOF for $10 million and makes an election to adjust the tax basis in his interest in the QOF to fair market value on the date of sale, or to $10 million. Taxpayer recognizes no gain on the sale.

QOZ Examples

- **Example**: John invests his capital gain from the sale of portfolio securities of $600K into a QOF on January 1, 2018, and also invests $400K of other cash not from capital gains into the same QOF for a total of a $1 million investment. After the 10 years John's investment in the QOF appreciates to $2 million. Assuming the tax on 85% of the deferred gain of $600K is paid by December 31, 2026; John would only be eligible for permanent exclusion on $600K of the $1 million appreciation and would pay taxes on $400K of appreciation.

Qualified Opportunity Zones:

Non-Tax Discussion Regarding this Provision

- The Joint Committee on Taxation estimates the Opportunity Zones program will cost $1.6B and will not generate revenue until 2026 and 2027 – the year the tax on the deferred gains are due
- These Zones operate in areas that face high unemployment, have many vacant buildings, as well as populations with low income and/or low education levels
- Governments use "Place-Based" incentive programs to subsidize companies and/or investors who operate in these specific areas in order to revitalize economically depressed communities, which also helps businesses offset the higher cost of doing business in these areas

Qualified Opportunity Zones:

Non-Tax Discussion Regarding this Provision

- Unfortunately many times with these programs, there is a skills mismatch problem, where many of the skills required of the company operating in the distressed area cannot be provided by the residents of the community and, therefore, people from outside the area must be brought in to perform those jobs--which in turn further displaces the low-income residents that the program was meant to help
- There is currently no reliable data available to measure the effectiveness of place-based incentive programs and as of today there are no requirements in the current tax law for gathering data to determine the success rate of this Opportunity Zone Program

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