

Opportunity Zone Funds



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**A Chance to Unlock
Unrealized Capital Gains
and Invest Where It's
Needed**

SEIZING (AND SIMPLIFYING) OPPORTUNITY ZONES

WITH HELP FROM RPR AND NAR,
YOU CAN GET IN THE ZONE



As a commercial practitioner, you may have heard about Opportunity Zones. It's one of the hottest topics in commercial real estate and something that should definitely be on your radar.

Here's the official definition: Created in 2017 as part of the Tax Cuts and Jobs Act, the purpose of the federal government's Qualified Opportunity Zone (QOZ) program is to drive economic growth through long-term investments in economically disadvantaged communities by offering tax incentives to investors.

In plain English? Opportunity Zones are areas that are ripe for redevelopment and they offer tax breaks to savvy commercial investors. They're also pretty easy to identify if you're an RPR user. Using the RPR Maps feature, REALTORS® can search a geographic area to display the Opportunity Zone areas that qualify. (More details on that later...)

Although Opportunity Zones are technically easy to find in RPR, it's the next step or two that may make them seem confusing or overwhelming. There's plenty of IRS tax code, legal mumbo-jumbo hoops to jump through and

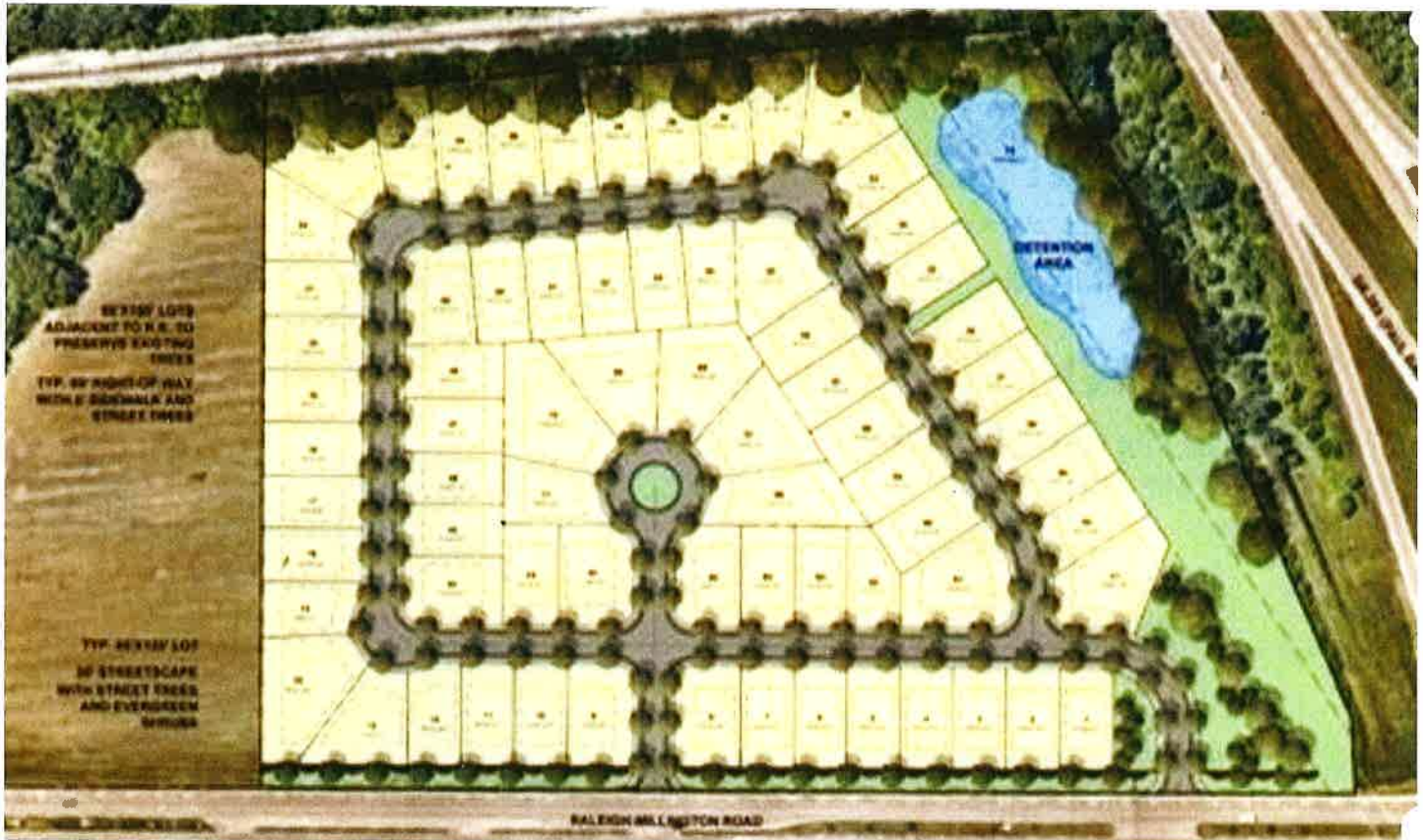
comprehend. However, with some help from RPR and NAR, you can understand them, how they work, and use them to you and your clients' advantage.

Which is why we've enlisted Bob Turner, ALC - 2019 NAR Commercial & Business Specialties Liaison, as our Opportunity Zones guide to help break down and explain how they work, where to look for them and what types of businesses are optimal examples. And why you shouldn't be afraid of them!

KNOCK-KNOCK? IT'S OPPORTUNITY.

Bob has been researching and utilizing Opportunity Zones since their inception. He has an expert understanding of the ins and outs of the program and his experiences and examples will help you grasp how they work.

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THE BARRET OAKS APARTMENT COMPLEX

Bob's most memorable piece of advice? To rip off the bandaid and dive right in. "The biggest hurdle may just be getting started. Keep in mind that this is simply tax law and you don't have to ask any governmental agency for permission. As long as you abide by the investment structure requirements, benchmarks and time frames, you simply treat it like any other tax law."

According to Bob, the first step you must take is to establish a Qualified Opportunity Fund. This is money that you are gaining from other investments or the sale of another property, similar to a 1031 Exchange. Then you need to identify the property, using RPR of course, and finally, purchase it.

It's important to keep in mind that only "gained" money can go into an Opportunity Fund from the sale of stocks or real estate to qualify for the tax gain benefits of the Opportunity Zone. The Opportunity Fund can be used to purchase the land for the new investment to start the process. This will ultimately allow you to receive three types of long-term tax benefits: 1) deferral of gains tax, 2) reduction of gains tax, and 3) exclusion of gains on the new investment.

The Barret Oaks Apartment Complex is Bob's most recent Opportunity Zones project. He used RPR to search for a designated OZ area, then he created his OZ Fund, and then he developed the land for use. Here are some specifics from this successful project:

- Includes 1, 2 and 3 bedroom units
- Rental rates range from \$800 - \$1,200
- Amenities include a water park and pool, walking trails, ponds and bike trails to the Millington Resilient Project
- Estimated costs: \$26,000,000
- Investors expect a 22% IRR

Although you shouldn't be intimidated by Opportunity Zone properties, you still have to view them as serious endeavors and stay on top of things accordingly. Bob sums this up by saying, "Development is like going to the casino, except with much more money! You can lose your tail if you don't know what you're doing. Land transactions and land development can be the most complicated transactions in the real estate business. Make sure you have expert tax and legal advisers on your team."

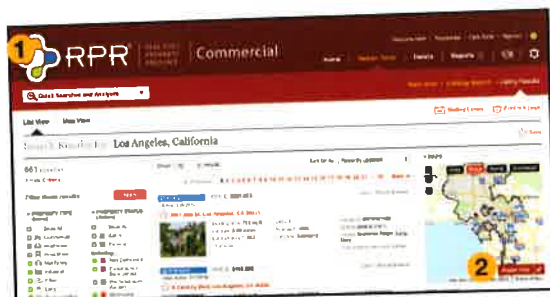
USING RPR TO FIND YOUR QOZ

Now that you know a little more about how these

investments work in the real world, let's discuss how you can use RPR, your REALTOR® benefit, to research and analyze properties.

The most basic thing you can do is select the Opportunity Zone map layer when you are looking for properties, or wanting to see if a property you are listing is in an OZ.

If you're unfamiliar with RPR, it is a benefit of REALTOR® membership and there is no cost for REALTORS® to create an account (www.narrpr.com). Once you log in, you have access to nationwide property data such listings, public records, economic/demographic stats and more.



How do I show the Opportunity Zone layer?

- 1 Log in to RPR at narrpr.com.
 - Or choose *Commercial* if you are on the *Residential* side of RPR.
- 2 From *Search Results*, *Property Details* and *Trade Area Summary* pages you'll select *Bigger Map*.
- 3 Select *Show Geographies* dropdown

OPP ZONE DEEP DIVE

Now that you know how to find and reveal Opportunity Zones in RPR, here's some other "drill down" type of scenarios to consider:

- Are there building owners that are unaware that their property is in an Opportunity Zone? Of course, and some of those owners may be at the end of their hold periods. RPR allows you to set up your search to look for properties that haven't sold since a specific date range.
- Keep in mind that just because a property is in an Opportunity Zone, doesn't mean that it's going to be a successful investment. So to help tip the scale you'll want to understand the community as much as possible and ensure the business idea matches that area's

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BOB TURNER'S STARTER IDEAS FOR OPPORTUNITY FUNDS:

- **Single Family Development**
You would need rental homes for the whole subdivision
- **Cannabis/Medical Marijuana Processing Facilities**
Ensure it's legal in your area
- **Warehousing**
Great for areas where buildings are not up-to-date
- **Create a Business**
You can operate a business in the OZ area
- **Mobile Home Parks**
The ultimate affordable housing
- **Land**
But you have to add improvements for it to qualify

OPPORTUNITY ZONES

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wants and needs. To do this you will want to run an RPR Custom Trade Area Report which will generate economic, demographic and tapestry segmentation data to help guide you in your due diligence.

- Finally, and probably the most important step in the process is to make sure that the project is capable of meeting or exceeding the Opportunity Fund's investment goals. Whether you are planning to renovate a multifamily building, refurbish an old industrial space for last mile delivery, or even look at a land development opportunities, RPR's Valuate® tool can be used to help you understand the potential returns and risks.

THE FINE PRINT OF OPPORTUNITY ZONES

Here we provide every last detail about the legalities and rules concerning Opportunity Zones, courtesy of Evan Liddiard, NAR's Director of Federal Tax Policy and CPA.

What Are Qualified Opportunity Zones?:

- Low-income census tracts designated by the governors of all 50 states to be eligible to receive private investment through Opportunity Funds.
- A total of 8,761 Opportunity Zones have been approved by the US Treasury, and every state has some.

Three Kinds of Capital Gains Incentives:

- Deferral of capital gain on the sale of old investment, the gain on which must be rolled over into an Opportunity Fund within 180 days, until the earlier of the date the Opportunity Fund investment is sold, or December 31, 2026.
- A 10% reduction of the capital gain deferred on the old investment if the Opportunity Fund is held for at least 5 years and a 15% reduction of deferred capital gain if the Opportunity Fund is held for at least 7 years.
- Zero capital gains tax on any post-investment gains in an Opportunity Fund that is held for at least 10 years and sold before Jan. 1, 2048.

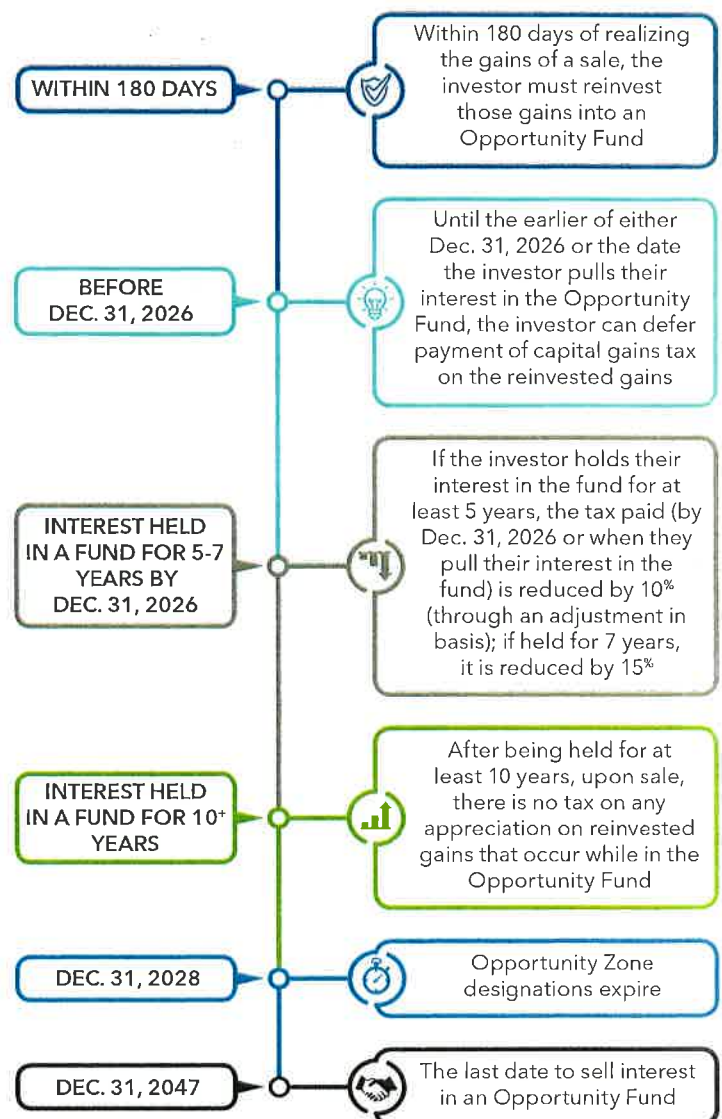
Investments in Opportunity Zones must be made via an Opportunity Fund and they must hold at least 90% of their assets in property within the Opportunity Zones. For real estate investments, properties must be "substantially improved" which means the Opportunity Fund spends at least as much to improve the property over any 30-month period as was paid for the non-land portion of the property.

QUALIFIED OPPORTUNITY ZONE PROGRAM

INVESTORS' TIMELINE

Qualified Opportunity Zones (QOZ) provide tax incentives for private investment into more than 8,700 under-served communities that have been designated as Opportunity Zones throughout the country. To qualify, investors must go through Opportunity Funds specifically set up for investing in a QOZ, and comply with the timing requirements set by the legislation, the IRS, and Department of Treasury.

PROGRAM DEADLINES



Opportunity Zone Funds



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**A Chance to Unlock
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You may have heard the term “Opportunity Zones” and wondered what that means for property investors. Opportunity Zones are designed to drive investment money to certain geographic areas – and they offer investors significant tax benefits for doing so.

Here in Winston-Salem, thanks in no small part to the hard work of Mayor Allen Joines and his staff, Governor Cooper has designated 10 Census Tracts as **Opportunity Zones**. These Opportunity Zones were designated under authority provided through the passage of The Tax Cuts and Jobs Act (H.R.1) earlier this year. H.R.1 places a new, robust tool in the toolbox of investors in the

form of Internal Revenue Code Section 1400Z-2. If certain rules are followed, the provision will delay recognition of capital gains *and* reduce them upon recognition.

Ideally, what this could mean for these designated areas is an influx of much-needed capital to revitalize a struggling neighborhood. For investors, it provides a way to invest with attractive tax incentives.

Until the passage of The Tax Cuts and Jobs Act earlier this year, **Internal Revenue Code Section 1031** has been the way for owners of investment property to delay recognizing capital gains on the sale of their properties. Boiled down to its most basic summary, in a

1031 exchange (or a “like kind” exchange), an owner of investment property can avoid paying capital gains tax on the sale of that property as long as it reinvests the money from that sale in a property or properties of “like kind,” and of equal or greater value within a certain timeframe.

While 1031 exchanges certainly aren’t going anywhere, Section 1400Z-2 promises to do what Section 1031 does and more.

How Opportunity Zones Work

First, the investor generates capital gains by selling an asset.

Second, within 180 days, the investor reinvests the gain (notice that this does not require reinvestment of the full proceeds) in an “Opportunity Zone Fund” – which is a corporation or partnership holding at least 90% of their assets in Opportunity Zones, either directly or through stock or partnership interests in “Qualified Opportunity Zone Businesses.” There are, of course, restrictions on what can be a Qualified Opportunity Zone Business.

Third, the investor holds the Opportunity Zone Fund interest until the “Recognition Date,” which is the earlier of the date the investor sells the investment or December 31, 2026.

- If the Recognition Date is at least five years after the date the investor made the investment, then its basis is stepped-up to 10% of the value invested.
- If the Recognition Date is at least seven years after the investment date, then its basis is stepped up again to a total of 15% of the value invested.

Fourth, at the Recognition Date, the investor recognizes the gain (the amount invested minus the basis, whether that is 10% or 15% of the value invested), which yields a new basis equal to the full amount of the value invested.

Finally, if the investor holds the Opportunity Zone Fund investment for at least 10 years, then it may elect to step-up the basis one more time to the then-fair market value. Doing so and selling the property at that amount would **eliminate all additional capital gains tax on disposition.**

Opportunity Zones (1400Z-2) Are More Flexible than 1031 Exchanges

While 1400Z-2 has the obvious geographical limitation that doesn't exist in a 1031 exchange, it is much more flexible in four significant ways:

- In 1031, the entire proceeds from the sale generating capital gains must be reinvested. **1400Z-2 requires only the gains be reinvested.**
- 1031 is only applicable to real property, **whereas 1400Z-2 applies to tangible property used in a trade or business, whether real or personal, as long as substantially all of it is located in an Opportunity Zone.** This brings in the possibility of using the tool in relation to partnership interests, stock in corporations, and personal property.
- In a 1031 exchange, replacement property must be identified within 45 days, with limits on the number of

properties that can be identified as replacement property. There are no such requirements in 1400Z-2.

- In a 1031 exchange, the replacement property must be like-kind. There is no such requirement in 1400Z-2.

How Opportunity Zone Investments Delay and Reduce Capital Gains Tax

Let's walk through an example. Let's say an investor generates \$1,000,000 in capital gains through a transaction on December 1, 2018. Within 180 days, the investor puts the full \$1,000,000 gain in an Opportunity Zone Fund, which purchases property in an

Opportunity Zone. On December 2, 2028, it sells the property for \$5,000,000. In this example, if done right, Section 1400Z-2 can allow the investor to recognize only \$850,000 in capital gains and delay paying tax on that \$850,000 for a little over 8 years, with the remaining \$4,150,000 in gain being realized without capital gains tax. The investor can do all of that without tying up the proceeds from the December 1, 2018 transaction, except that portion of the proceeds that were themselves capital gains.

Here's how: In this example, the two key dates are December 31, 2026 (the Recognition Date) and December 1, 2028

(the Disposition Date). On the Recognition Date, the Taxpayer receives a step-up in its income tax basis from \$0 to \$150,000 (15% of its \$1,000,000 investment).

Simultaneously, it recognizes \$850,000 in capital gains (its \$1,000,000 investment less its new \$150,000 basis), even though there has not yet been a sale. Upon such recognition, its basis increases again by the amount of the recognized gain, from \$150,000 to \$1,000,000. Then, on December 1, 2028, the investor can elect to step-up the basis one more time, to the properties then-fair market value of \$5,000,000, eliminating all remaining capital gains tax.

Where are These Opportunity Zones in Winston-Salem?

The **10 Opportunity Zones in Winston-Salem** are:

- Tracts 1 (37067000100) & 2 (37067000200) cover the downtown business district
- Tracts 3.01 (37067000301) & 3.02 (37067000302) cover the Boston-Thurmond and Kimberly Park neighborhoods
- Tract 7 (37067000700) is considered East Winston-Salem and includes sections of Wake Forest Innovation Quarter
- Tract 8.01 (3706700080) & 8.02 (37067000802) are south of Tract 7

and include Winston-Salem State University, the UNC School of the Arts and Happy Hill

- Tract 14 (37067001400) includes Whitaker Park and the Lawrence Joel Coliseum
- Tract 16.02 (37067001602) includes Smith Reynolds Airport and neighborhoods south of the airport
- Tract 17 (37067001700) is southeast of New Walkertown Road and includes the Winston Lake Golf Course area

[Click here for a map of the North Carolina Opportunity Zones](#)



Opportunity Zone Map of Winston-Salem

With 1400Z-2, Opportunity Zones promise to be a powerful tool to the right investor in the right circumstances. It has the potential to allow investors holding significant unrealized capital gains to deploy them in

communities in need an investment injection. We are looking forward to helping clients navigate this new investment vehicle.

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Leigh C. Bagley is an attorney at the Winston-Salem law firm of **Bell, Davis & Pitt**. Leigh focuses her practice on **commercial real estate law**, and **banking and financial services**. Leigh currently serves on the board of the Winston-Salem Business Inc. (WSBI). Until 2014, she served as an adjunct professor at the Wake Forest School of Law, where she also received her law degree.

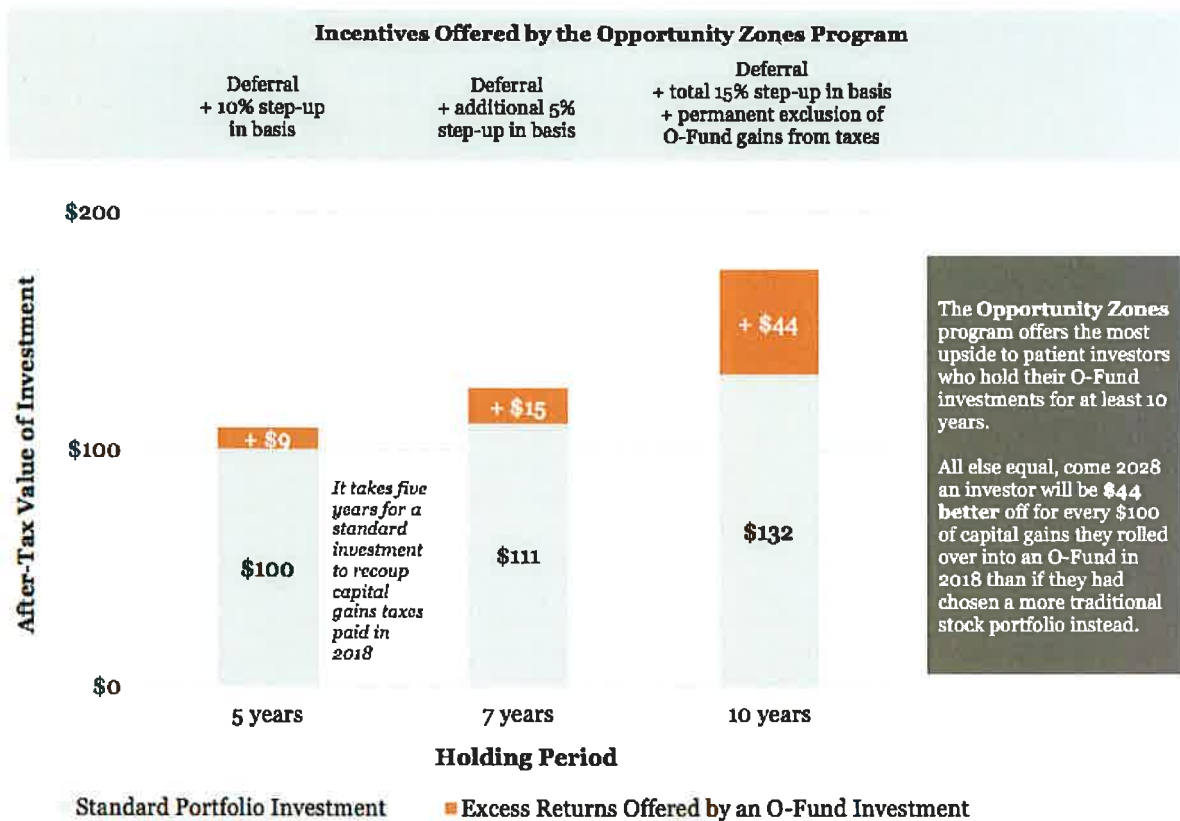
The Tax Benefits of Investing in Opportunity Zones

January 2018

The Opportunity Zones program offers three tax benefits for investing in low-income communities through a qualified Opportunity Fund¹:

1. A **temporary deferral** of inclusion in taxable income for capital gains reinvested in an Opportunity Fund. The deferred gain must be recognized on the earlier of the date on which the opportunity zone investment is disposed of or December 31, 2026.
2. A **step-up in basis** for capital gains reinvested in an Opportunity Fund. The basis is increased by 10% if the investment in the Opportunity Fund is held by the taxpayer for at least 5 years and by an additional 5% if held for at least 7 years, thereby 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 an Opportunity Fund if the investment is held for at least 10 years. This exclusion only applies to gains accrued *after* an investment in an Opportunity Fund.

Figure 1. Investing in an Opportunity Fund vs. a Standard Stock Portfolio Scenario: A Capital Gain of \$100 is Reinvested in 2018



* Note: Assumes long-term federal capital gains tax rate of 23.8%, no state income tax, and annual appreciation of 7% for both the O-Fund and alternative investment.

How does the incentive work in practice? Illustrative examples:

The figure above, along with the table and examples below, show how an investor's after-tax funds available compare under different scenarios, assuming various holding periods, annual investment appreciation of 7%, and a long-term capital gains tax rate of 23.8% percent (federal capital gains tax of 20% and net investment income tax of 3.8%). The table provides additional information on the tax liabilities and differences in the after-tax annual rates of return. As is clear, the incentives built into the Opportunity Zones program are designed to reward *long-term* investments in distressed communities the most.

Table 1. Investing in an Opportunity Fund (O-Fund) vs. a Standard Stock Portfolio
Scenario: A Capital Gain of \$100 is Reinvested in 2018

Holding Period	Appreciation Rate	Investment in a Stock Portfolio		Investment in an Opportunity Fund		Difference in After-Tax Annual Rate of Return
		Total Tax Liability	After-Tax Funds Available	Total Tax Liability	After-tax Funds Available	
5 years	7%	\$31	\$100	\$31	\$109	1.9%
7 years	7%	\$35	\$111	\$35	\$126	1.8%
10 years	7%	\$41	\$132	\$20	\$176	3.0%

Example 1: Investor holds the O-Fund stake for 10 years

Susie has \$100 of unrealized capital gains in her stock portfolio. She decides in 2018 to reinvest those gains into an O-Fund that invests in distressed areas of her home state, and she holds that investment for 10 years. Susie is able to defer the tax she owes on her original \$100 of capital gains until 2026. Further, the basis is increased by 15% (effectively reducing her \$100 of taxable capital gains to \$85). Thus, she will owe \$20 (23.8% of \$85) of tax on her original capital gains when the bill finally comes due. In addition, since she holds her O-Fund investment for at least 10 years, she owes no capital gains tax on its appreciation. Assuming that her O-Fund investment grows 7% annually, the after-tax value of her original \$100 investment in 2028 is \$176. Susie has enjoyed a 5.8% effective annual return, compared to the 2.8% an equivalent non-O-Fund investment would have delivered.

Total tax bill in 2028: \$20

After-tax value of investment in 2028: \$176

Effective after-tax annual return on \$100 capital gain in 2018: 5.8%

Example 2: Investor holds the O-Fund stake for 7 years

As in Example 1, in 2018 Susie rolls over \$100 of capital gains into an O-Fund. She holds the investment for 7 years, selling in 2025. As in Example 1, she temporarily defers the tax she owes on her original capital gains and steps-up her basis by 15%, so that in 2025 she will owe \$20 (23.8% of \$85) of tax on her original capital gains. Unlike Example 1, however, Susie will owe capital gains tax on the appreciation of her O-Fund investment, since she holds the investment for less than 10 years. Assuming that her O-Fund investment grows 7% annually, in 2025 Susie will owe \$15 (23.8% of \$61) of tax on the O-Fund investment's capital gain. Susie did not take full advantage of the Opportunity Zone program but nevertheless received a 3.3% effective annual return compared to the 1.5% an equivalent non-O-Fund investment would have delivered.

*Total tax bill in 2025: **\$35***

*After-tax value of investment in 2025: **\$126***

*Effective after-tax annual return on \$100 capital gain in 2018: **3.3%***

Example 3: Investor holds the O-Fund stake for 5 years

As in Example 1, in 2018 Susie rolls over \$100 of capital gains into an O-Fund. She holds the investment for 5 years, selling in 2023. As in Example 1, she can temporarily defer the tax she owes on her original capital gains, but her step-up in basis is only 10%, so that in 2023 she will owe \$21 (23.8% of \$90) of tax on her original capital gains. As in Example 2, Susie enjoys no exemption from capital gains tax on the appreciation of her O-Fund investment, since she holds the investment for less than 10 years. Assuming that her O-Fund investment grows 7% annually, in 2023 Susie will owe \$10 (23.8% of \$40) of tax on the O-Fund investment's capital gain. Susie did not take full advantage of the Opportunity Zone program but nevertheless received a 1.8% effective annual return on her initial capital gains compared to the -0.1% effective annual return an equivalent non-O-Fund investment would have delivered.

*Total tax bill in 2023: **\$31***

*After-tax value of investment in 2023: **\$109***

*Effective after-tax annual return on \$100 capital gain in 2018: **1.8%***

For more information visit eig.org/opportunityzones or email john@eig.org

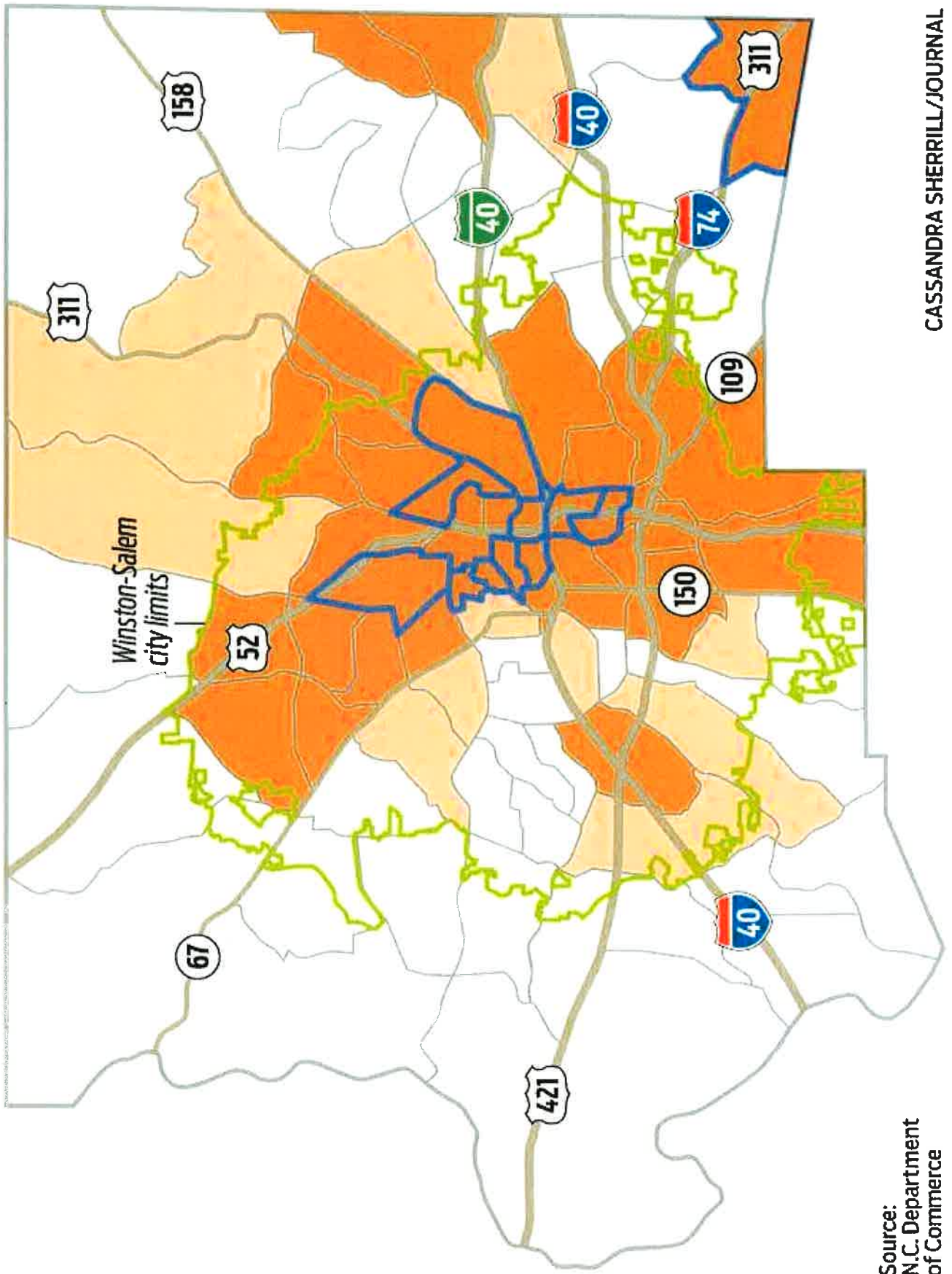
¹ A qualified Opportunity Fund is a privately managed investment vehicle organized as a corporation or a partnership for the purpose of investing in qualified opportunity zone property (the vehicle must hold at least 90 percent of its assets in such property). Governors (or the Mayor in the case of the District of Columbia) may designate 25 percent of their state's low-income census tracts as qualified opportunity zones, subject to certification by the U.S. Secretary of the Treasury. Low-income census tracts are defined in Internal Revenue Code Section 45D(d). If the number of low-income census tracts in a state is less than 100, then a Governor may designate a total of 25 tracts. Qualified opportunity zone property includes any qualified opportunity zone business stock, any qualified opportunity zone partnership interest, and any qualified opportunity zone business property. Only taxpayers who roll over capital gains of non-zone assets before Dec. 31, 2026, will be able to take advantage of the special treatment under the provision.



 Census tracts approved by the U.S. Treasury as opportunity zones

 Low-income census tracts that were eligible to be an Opportunity Zone

 Contiguous census tracts that were potentially eligible



Source:
N.C. Department
of Commerce

CASSANDRA SHERRILL/JOURNAL