

Opportunity Zones Regulations Correcting Amendments

On April 1, 2020, the Treasury Department and the Internal Revenue Service (collectively the “government”) released correcting amendments to the opportunity zone regulations (the “corrections”). Although correcting amendments are typically used to correct typos and other minor errors, these corrections also clarify certain ambiguities in the regulations and even make some substantive changes. Below is a summary of the significant changes:

Reporting requirements – The corrections broadened the description of what must be reported by eligible taxpayers presumably to maintain flexibility to modify Form 8997 in the future.

Effective date – In the effective date provisions in all of the subsections of the regulations, the corrections provide that reliance on proposed regulation sections is disregarded for purposes of determining whether the final regulations are consistently applied. Thus, the corrections modify statements previously made by government representatives that the election to apply the final regulations was “all or nothing.” The corrections also remove some confusing language referring to taxable years ending after December 21, 2017 “that began on December 22, 2017.”

Cure rule

Date for filing – The corrections fix language that had required a QOF to file a tax return “not later” than when a cure is achieved for a QOZ business that failed to qualify as a QOZ business and replace it with “not earlier than.”

Trade or business – The corrections clarify that a QOZ business can receive only one cure per trade or business (rather than one cure per QOF).

Federally declared disasters

Working capital safe harbor – For a federally declared disaster, the language of the final regulations stated that a QOZ business may receive up to 24 months to consume its working capital assets. The corrections change the language “receive up to” to “receive not more than,” clarifying that a QOZ business can receive an extension for the duration of the disaster but not more than 24 months.

Reinvestment period – For the 12 additional months for a QOF to reinvest proceeds that is delayed due to a federally declared disaster, the language providing that a QOF may receive “up to” 12 months is replaced with language providing that a QOF may receive “not more than” 12 months.

Working capital safe harbor

62-month safe harbor – The corrections reorganize the working capital safe harbor to place the 62-month safe harbor rule with the remainder of the specific rules for applying the working capital safe harbor to the section 1397C requirements. In addition, the example illustrating the 62-month safe harbor was moved with the other examples, renumbered as example 4.

Working capital – The corrections clarify that working capital will not be treated as QOZ business property for any purpose. However, the corrections also provide that the QOZ business will be treated as meeting the QOZ business property requirements for the duration of the working capital safe harbor, which represents a taxpayer-favorable change from prior statements made by government representatives. Thus, for example, a QOZ business will not be disqualified during the safe harbor period if it has nonqualified property (e.g., land acquired from a related party).

Debt as working capital – The language of example 4 is modified to more clearly indicate that working capital includes debt as well as contributed equity.

Unadjusted cost basis valuation – The final regulations provided that the alternative valuation method using cost basis could only be used for property acquired by purchase or constructed; otherwise fair market value must be used. The correction clarifies that the acquisition by a QOF of qualified opportunity zone stock or a qualified opportunity zone partnership interest is treated as a purchase of the interest by the QOF solely for purposes of this rule.

Circular movement of consideration – The corrections add a new paragraph to example 3 of the anti-abuse examples to describe a circular flow of consideration between a QOF and its subsidiary QOZ business that will be disregarded, regardless of whether the investor is related to the QOF immediately following the acquisition.