



City of Spokane & University District

CRITICAL OZ UPDATES

LEARN HOW THE NEW REGULATIONS OPEN OPPORTUNITIES FOR BUSINESSES,
INVESTORS, AND PROPERTY OWNERS.

Welcome – Today’s Agenda

- **Chris Green**, City of Spokane: Welcome & Logistic
 - Questions before we begin filming?
 - During presentations please hold questions until the filmed portion has ended.
- **Filming Begins**
 - **Lars Gilberts**, CEO – University District Welcome & Speaker Intros Speakers Presentations
 - Lars Gilberts Thank Everyone for the presentations and for participating -- **Filming Ends**
- Open up for questions





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Presentations and Q&A session by [Adam Sweet, JD, LLM, Principal, Eide Bailly, LLP](#); and [Bill Simer, CPA, Partner, Eide Bailly, LLP](#).





Bill A. Simer, CPA

Partner

INSPIRATION: I get up every morning thinking about how I'm going to help clients today, what I'm going to do better and how I'm going to help them achieve their goals. I do this because I love helping people find solutions to difficult challenges and helping them reach their goals, and I want to be on their team, not just an outside advisor.

509.789.9116

bsimer@eidebailly.com



Bill is a tax planning specialist who works with businesses and clients to plan for present needs and future goals. He also is an active member of the Spokane community who helped lead the effort to save and restore the Martin Woldson Theater at the Fox that now serves as the home of the Spokane Symphony.

When you work with Bill, you can expect a seasoned professional who will help your business or organization take charge of its tax planning and achieve new goals. He's worked with clients of all sizes, and he is ready to work with you to plan for a better future.

When he's not helping businesses run like a well-oiled machine, Bill likes to race other well-oiled machines of the vintage race car variety. He also likes to restore cars.

ADAM SWEET, J.D., LL.M.

Principal

509.252.4019 | asweet@eidebailly.com

Adam, a native of Spokane, is a Principal in Eide Bailly's National Tax Office, focusing on the taxation of pass-through entities.

Adam has a talent for distilling tax rules into concepts that can be understood by non-tax professionals. He has become a regular speaker on the subject of tax reform.

Outside of the office, Adam is a family man who enjoys everyday moments with his wife and kids. When he wants to unwind, he loves getting outdoors for a good run or a round of golf.



Memberships

Member of the California Bar

Published Tax Court cases

Education

Bachelor of Arts, History –
University of Washington, Seattle

Juris Doctor – Lewis and Clark
Law School, Portland, Oregon

Master in Tax (LL.M.) –
Georgetown University Law
Center, Washington, D.C.



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OPPORTUNITY ZONES

Understanding The Opportunity Part II

DISCLAIMER

These materials, and the accompanying oral presentation, are for educational purposes only and are not intended to be “written advice concerning one or more Federal tax matters” subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230.

This information is of a general nature and based on authorities that are subject to change.

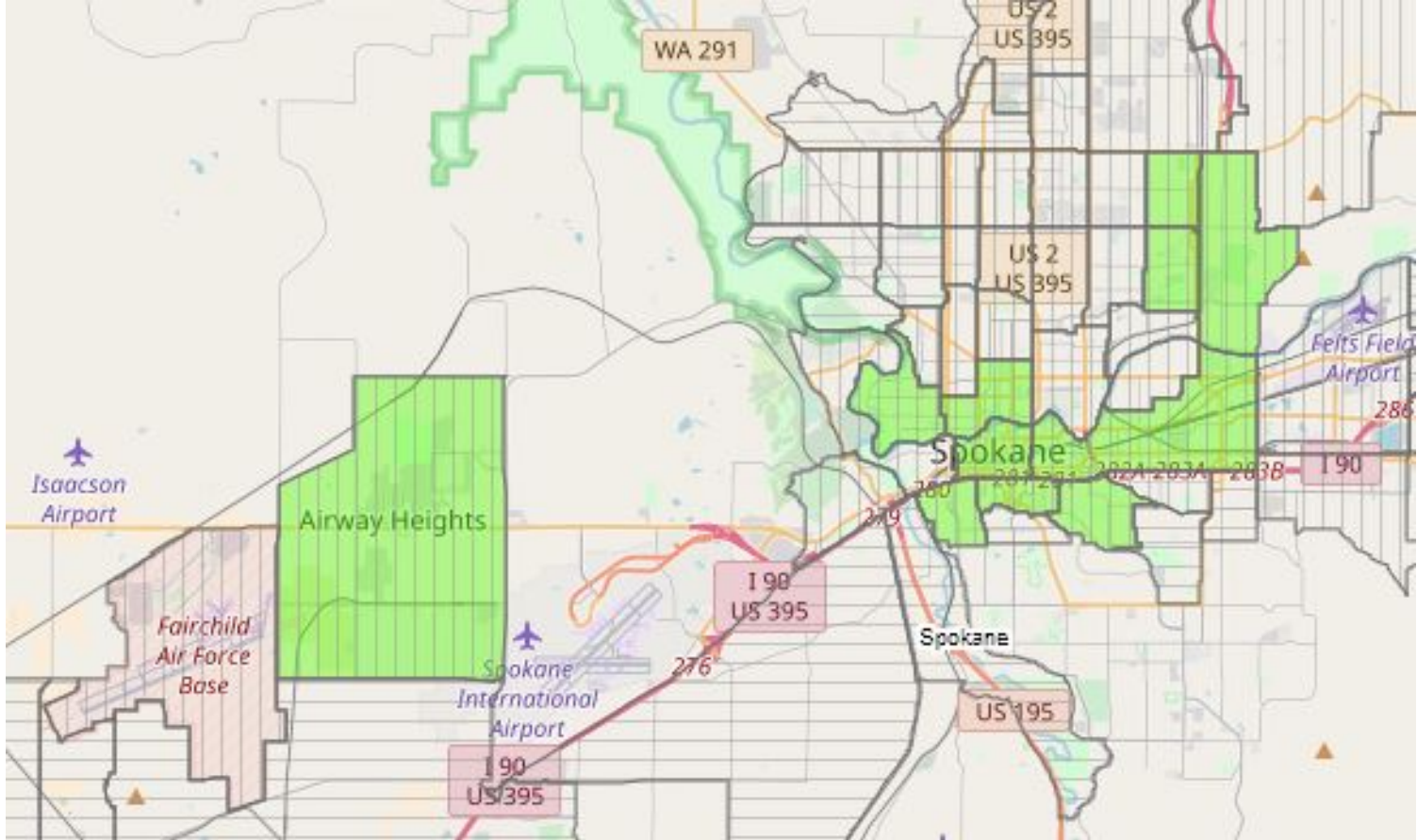


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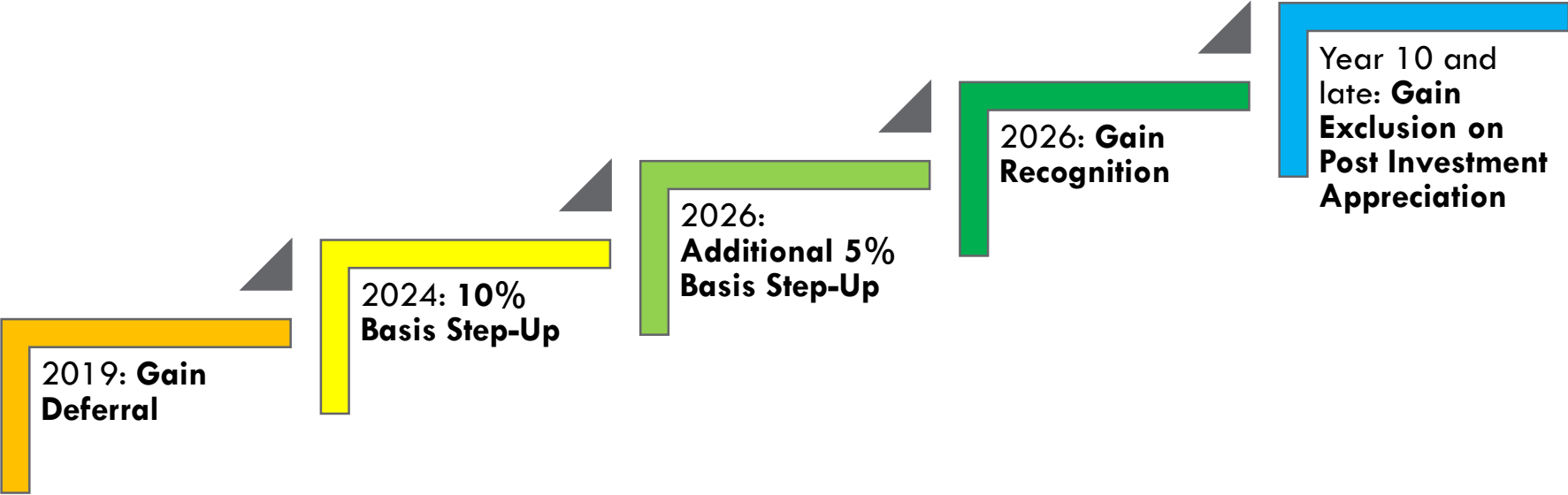
AGENDA

- Quick recap of the operative provisions
- Discussion of new guidance
- Current opportunities

OPPORTUNITY ZONE MAP SPOKANE COUNTY



TAX BENEFITS



KEY TERMS

- QOF= Qualified Opportunity Fund
 - Self certification
 - Can be state law LLC, very flexible
 - Holds at least 90% of its assets in “QOZ property”
- QOZ property= QOZ stock, QOZ partnership interest, or QOZ business property
- QOZ stock and QOZ partnership interest = acquired post 2017
 - During substantially all of the QOF’s holding period, the corporation/partnership qualifies as a QOZ business

KEY TERMS

- QOZ business property= tangible property used in trade or business purchased from unrelated party (20 percent threshold)
 - Need original use or substantial improvement
 - During substantially all of the QOF's holding period, substantially all of the use of the property in QOZ

KEY TERMS

- QOZB
 - Substantially all (70 percent) of tangible property owned or leased by the business is QOZB property
 - 50 percent or more gross income from active conduct of business in QOZ
 - Substantial portion (40%) of intangible property used in trade or business
 - Can't hold 5% or more of assets as certain financial assets
 - Not a "sin business"= golf course, country club, massage, suntan, hot tub, racetrack/gambling, store with principal purpose of selling alcohol

KEY DATES AND TIMELINES

- If sell capital asset directly, taxpayer has 180 days to reinvest the gain
- If a partnership or S corporation sells the assets
 - 180 days to roll gain over
 - If entity does not do so, the owner can elect to reinvest the gains within 180 days of the close of the entity's tax year (end of June for calendar year partnerships) or within 180 days of the entity's sale (assuming the partner has the requisite information)

COMPLIANCE POINTS

- Individual
 - Form 8949- gain deferral election
- QOF self certifies with Form 8996
 - Testing dates on last day of the first 6 month period of the tax year and on the last day of the tax year
 - Can ignore certain recent capital contributions for the first test

UPDATES- 1231 GAINS

- Reminder- need eligible capital gains to make a qualified investment
- Section 1231 gains- from the sale of property (including real property) used in a trade or business
 - Net 1231 gains=capital
 - Net 1231 losses=ordinary
- New guidance- must wait until the end of the tax year to make a qualified investment (180 day reinvestment period starts then)

UPDATES- CASH OR PROPERTY

- New guidance- either cash or property can be contributed into a QOF, as long as taxpayer has eligible capital gains
- But, contributed property appears not to be qualified because it was not acquired by the QOF

UPDATES- QOF SALE OF ASSETS

- If QOF sells an asset, has 12 months to reinvest the cash into other qualifying property (cash will count as qualified property during that period)
- But the gain is still subject to tax- Government has asked for comments
- QOFs may consider section 1031 exchanges

UPDATES- LAND

- Land and real estate can qualify as good property, but beware of “land banking”
- Don’t need original use for land
- Leased real property can qualify as an active business
- Beware of a triple net lease

UPDATES- LEASES

- Lessee improvements can work and are considered purchased property
- Leased property is QOZBP if:
 - Lease entered after December 31, 2017
 - 70% of the use of the leased property in OZ during 90% of the time period
 - Market rate lease
- Can lease between related parties, but no prepayment and, if is tangible property, need to acquire other tangible property at least equal to the value of the leased property

UPDATES- GROSS INCOME REQUIREMENT

- At least 50% of a businesses gross income must come from the active conduct of a trade or business in an opportunity zone
- 3 new safe harbors
 - At least 50% of services performed by QOZB employees and contractors are in an OZ, measured by service hours
 - At least 50% of services performed by QOZB employees and contractors are in an OZ, measured by amounts paid for services
 - Both the tangible property of the QOZB in the OZ and the management/operational functions in the OZ are each necessary for generation of at least 50% of QOZB gross income

UPDATES- WORKING CAPITAL SAFE HARBOR

- Working capital safe harbor allows QOZB to treat working capital as “reasonable” for a period of up to 31 months if there is a:
 - Written plan to use capital
 - Written schedule consistent with ordinary start up of a business
 - Working capital used in a manner consistent with schedule
- Can exceed 31 months if due to permitting/regulatory issues

UPDATES- ORIGINAL USE AND SUB IMPROVEMENT

- Reminder- need original use or substantial improvement of qualified property if that property was previously placed in service in a OZ

UPDATES- ORIGINAL USE

- Purchased tangible property- original use begins on placed in service date
- Used property never placed in service in OZ- original use begins when placed in service in OZ
- Used property previously placed in service in OZ- need substantial improvement
- Also, if real estate has been vacant for at least 5 years, can satisfy original use requirement

UPDATES- SUBSTANTIAL IMPROVEMENT

- Substantial improvement to tangible assets- \$1 of improvement for every \$1 of cost (excluding land)
- Measured on an asset by asset basis, not in the aggregate- burden for businesses with lots of assets

UPDATES- EXIT CONSIDERATIONS

- Capital gain from a QOF's sale of its assets can be excluded by an owner who has held their qualifying interest for at least 10 years
- Owner can sell their qualified equity interest (provided have held for 10 years) and avoid all tax, including, apparently, depreciation recapture
- Taxpayer can make a qualified investment by acquiring an interest from another equity owner- may help with liquidity considerations
- Debt financed distributions can work so long as the cash distributed does not exceed basis (including debt)- may provide cash for tax payment due in 2026

UPDATES- INCLUSION EVENTS

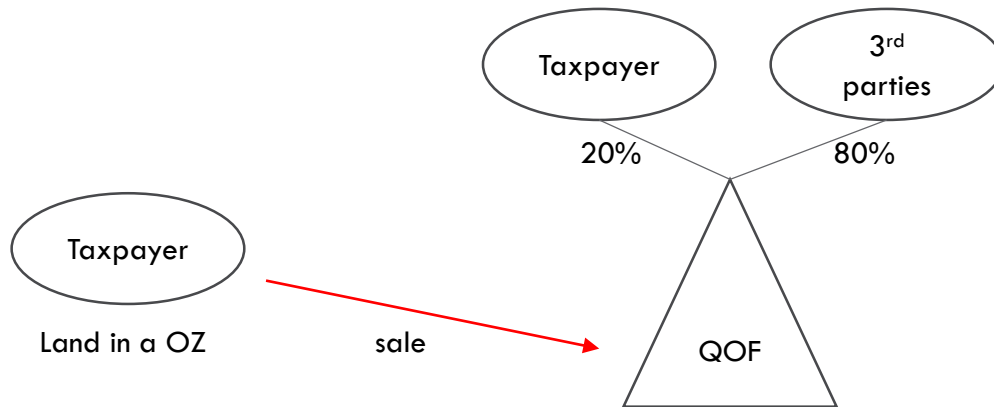
- Triggers deferred gain
- Events include
 - Disposing of all or a portion of a QOF interest
 - Distributions in excess of basis
 - Certain transfers

OWNING PROPERTY/BUSINESS IN A OZ

- Owning property and/or a business in a OZ may not provide any immediate tax benefits
- Just selling property and/or a business located in a OZ does not necessarily produce any tax benefits unless the owner decides to invest the qualifying capital gain into a QOF
- But the property and/or business may be an attractive investment for a QOF

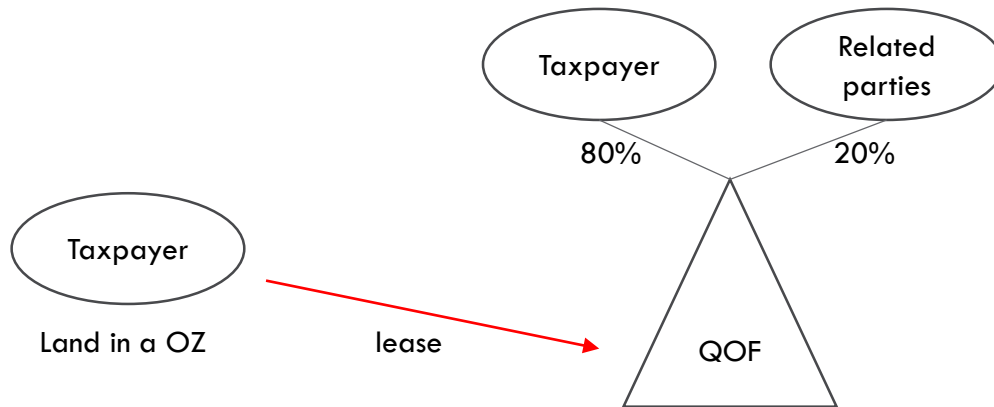
OWNING PROPERTY/BUSINESS IN A OZ

- Selling property to own fund and reinvest gain? Only if willing to give up control



OWNING PROPERTY/BUSINESS IN A OZ

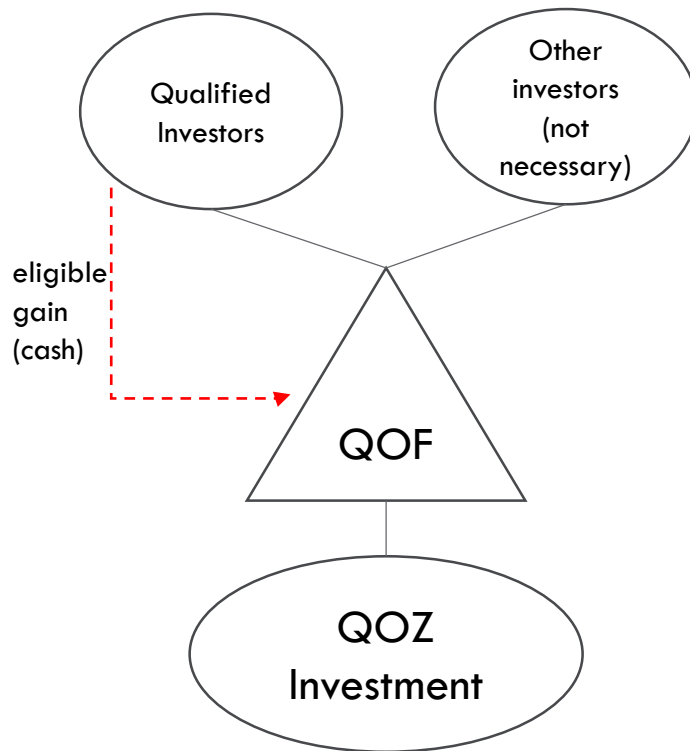
- Can also consider leasing property to QOF



EXISTING BUSINESS OWNER

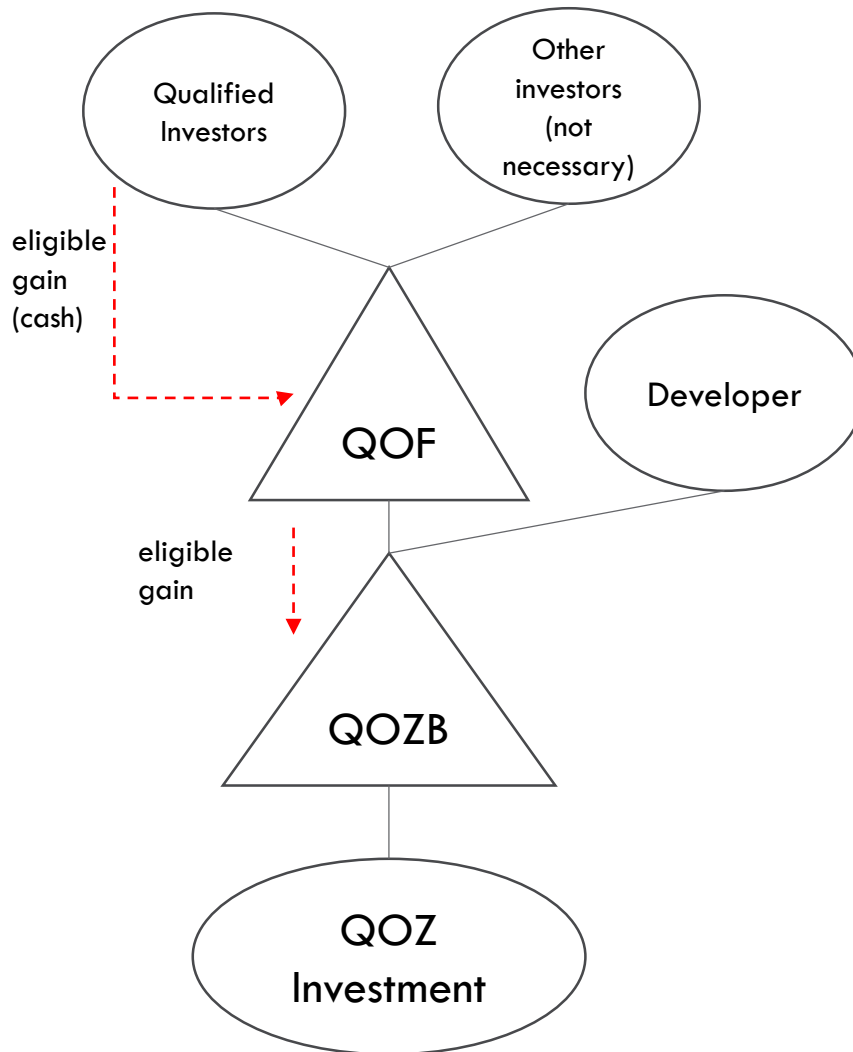
- Example
 - Spokane company sells land/building to unrelated party, generating capital gain
 - Owner, with family members, sets up QOF, and invests gain into QOF
 - QOF purchases land and builds new facility in an OZ (or makes substantial improvements to purchased property)
 - At end of 10 years, all appreciation could be realized tax-free

BASIC STRUCTURES- DIRECT INVESTMENT



- 90 percent of assets must be QOZB property
- May be hard to deploy cash within 6 months
- Led to focus on two tier structure (next slide)

BASIC STRUCTURES- INDIRECT INVESTMENT



- 70 percent of tangible property owned/leased by business is QOZB property
- 50% of gross income from trade or business within OZ
- Can use working capital safe harbor
- More flexible than direct investment structure (prior slide)

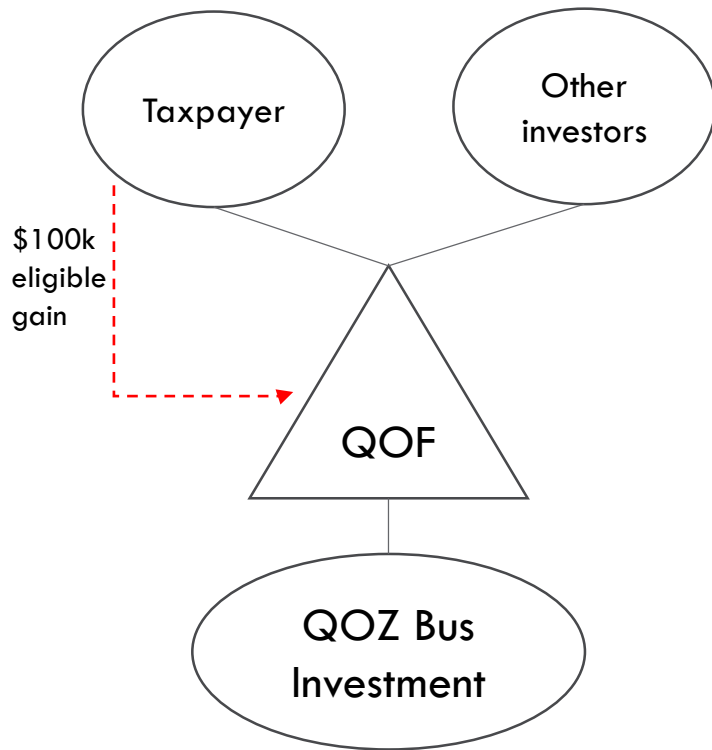
STATE AND LOCAL GOVERNMENTS

- Unclear what state and local governments may do to enhance the program, particularly in states with no income tax
- Possible Approaches
 - Tax incentives
 - Property tax abatements
 - Sales and use tax exemptions or refunds
- Non-tax incentives
 - Grants – cash / property
 - Discounts – utilities and other costs
 - Other assistance

OPPORTUNITY ZONE EXAMPLE

- Taxpayer sells publicly traded stock for \$200k in 2018 that was purchased for \$100k, triggering **\$100k of gain**
- Under new code section 1400Z-2, taxpayer elects to invest the **\$100k of gain** into a QOF (an LLC treated as a partnership for federal tax purposes) within 180 days of the sale of the stock

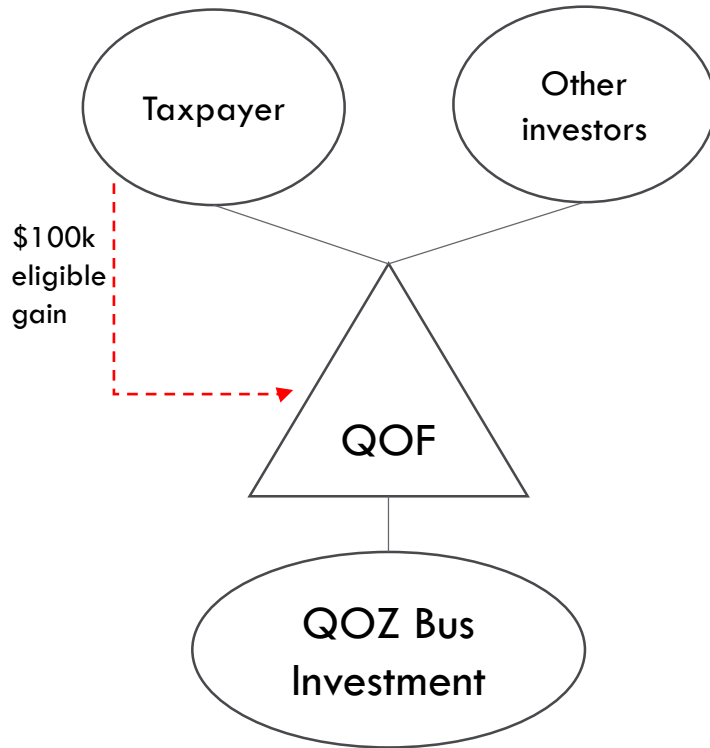
OPPORTUNITY ZONE EXAMPLE 2018



- Taxpayer defers the \$100k of gain in year 1 (meaning no tax recognized) by filing requisite **IRS Form 8949**
- QOF self-certifies with the IRS that it is initially qualified (**Form 8996**)
- QOF also files annual report certifying it meets all requirements
- Taxpayer takes a \$0 tax basis in its QOF interest

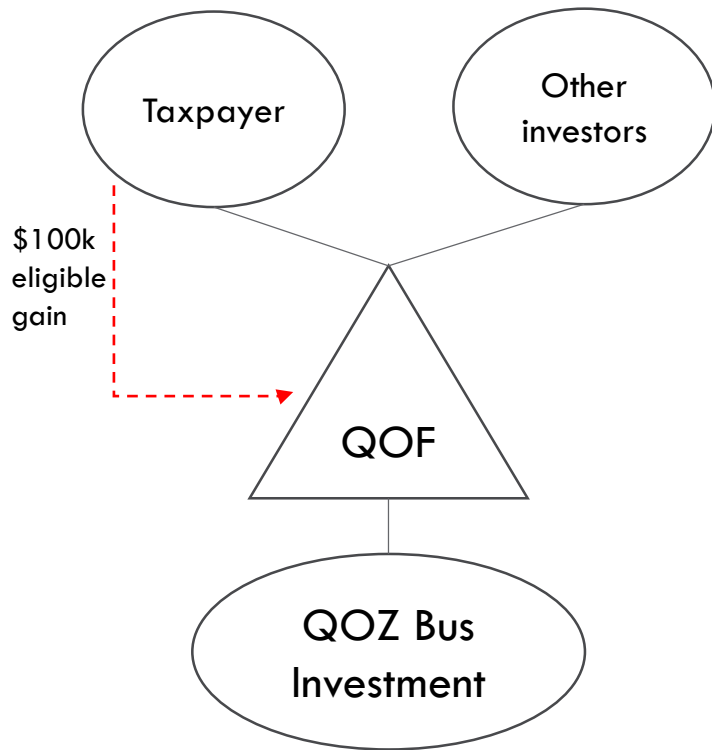
Important note: This is a simplified example for illustrative purposes and this example assumes all statutory and regulatory requirements are met

OPPORTUNITY ZONE EXAMPLE 2026



- Assume QOF interest now worth \$150k (\$50k appreciation)
- Taxpayer receives basis step-up of \$15k (\$10k at year 5 and additional \$5k at year 7)
- Taxpayer's 2026 basis= \$15k
- Deferred gain recognized in 2026= \$85k of original \$100k

OPPORTUNITY ZONE EXAMPLE 2028



- 2028- Assume QOF interest now worth \$200k and taxpayer sells interest
- Taxpayer's basis= \$100k (\$15k basis step-up plus \$85k of gain recognized in 2026)
- The \$100k of gain (\$200k proceeds minus \$100k of basis) permanently excluded from income

QUESTIONS

Contacts

Adam Sweet

Eide Bailly

asweet@eidebailly.com

509 252 4019

Bill Simer

Eide Bailly

bsimer@eidebailly.com

509 789 9116



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