Treasury & IRS Release Second Phase of Opportunity Zone Regulations

On Wednesday, April 17, 2019, the U.S. Treasury and IRS released its second tranche of proposed Opportunity Zone (OZ) regulations. Even though this second set of regulations is still “proposed,” Treasury has indicated that investors and Qualified Opportunity Funds (QOFs) may rely on them if they are applied consistently and in whole.

Click here for the second set of Treasury OZ regulations.

In this proposal, Treasury also invites outside parties to comment on outstanding issues (60-day comment period), in particular the need for reporting requirements, which USCM called for in our December comments to the first set of proposed regulations.

Of major concern in our December comments was the restrictive nature of the 50% gross income test, meaning that 50% of gross income of a qualified OZ business must be derived from business conducted in the OZ itself. The result of this proposed rule would have been to restrict an OZ business from significantly developing markets beyond the zone.

The rules released yesterday propose three safe harbors and a “fact and circumstance” test for OZ businesses, any one of which can be used to meet the 50% gross incomes requirement. Treasury believes these rules should allow for companies to conduct business outside the zone while at the same time investing in the OZ.

Click here for a Novogradic technical summary of the 50% gross income test and other issues.

On another major issue, the regulations allow for the extension of the 31-month safe harbor for working capital. Under the previous proposed regulations, OZ businesses could hold funds for 31 months, but many cities and responders had indicated that securing environmental approvals and other permitting requirements for large projects may not be feasibly obtained within that timeframe.

The new rules establish that the working capital safe harbor is not jeopardized if the delay is the result of failure to receive such approvals during the 31-month period as long as the application for such permits were made during that period.
The rules also clarify that an OZ business may use multiple or overlapping 31-month working capital funds. For example, on a major construction project, an OZ business (developer) could have a safe harbor working capital fund for site preparation, and another one for vertical construction. Again, Treasury’s intent is to bring OZ businesses flexibility in their efforts to invest in OZs. We will continue to analyze the proposed regulations to determine their impact on the formation and operation of QOFs.

In the near future, the Conference of Mayors and its Council on Metro Economies and the New American City will hold a conference call to further assess the impact of these regulations on Opportunity Zone development.

Please direct your questions or comments to USCM Staff Dave Gatton: dgatton@usmayors.org.