Quick Qualified Opportunity Zones Rules

SINGLE-TIER STRUCTURE

INVESTORS

Contribution (qualifying gain)

QUALIFIED OPPORTUNITY FUND (QOF)

partnership or corporation for tax purposes

90% of *all* of the Fund's assets (average of two snapshot dates) must be Qualified Opportunity Zone Business Property (**QOZBP**).

Cash and accounts receivable are not good assets for purposes of the 90% test.

TWO-TIER STRUCTURE

INVESTORS

Contribution (qualifying gain)

QOF

partnership or corporation for tax purposes

90% of *all* of the Fund's assets (average of two snapshot dates) must be:

- Interests in subsidiaries that are corporations or partnerships for tax purposes and that meet the requirements to be a qualified opportunity zone business (Subsidiary **QOZB**); and/or
- **QOZBP**

Cash and accounts receivable are not good assets for purposes of the 90% test.

Any percentage owner *Cash contribution*

SUBSIDIARY QOZB

partnership or corporation for tax purposes

- 70% of its *tangible assets* (owned or leased) are **QOZBP**;
- At least 50% of its gross income is from the *active conduct of its trade or business in the zone;*
- At least 40% of its intangible property is used in the *active conduct of its trade or business in the zone;*
- Not a sin business; and
- Less than 5% of the tax basis of its assets is comprised of *nonqualified financial property,* although *reasonable working capital* is permitted.

DEFINITION OF QUALIFIED OPPORTUNITY ZONE BUSINESS PROPERTY (QOZBP)

- Tangible property
- Acquired by purchase from an unrelated party after December 31, 2017, or leased pursuant to a lease entered into after December 31, 2017 (with special rules for leases from related parties); and
- The original use of the property in the zone commences with the QOF or Subsidiary QOZB or the property is substantially improved by the QOF or Subsidiary QOZB. Qualifying leased property does not have to be substantially improved.
  - Substantial improvement means over any 30-month period the property is owned by a QOF or QOZB, the QOF or QOZP spends more than the adjusted basis of such property at the beginning of the 30-month period. But, land and a building, all of which is in a zone, may be substantially improved by spending more than the cost of the building only.
- During at least 90% of the QOF's or Subsidiary QOZB's holding period, at least 70% of the use of such tangible property was in a QOZ.

NOTES

- Both the QOF and the Subsidiary QOZB may be LLCs, but neither can be a disregarded entity.
- Different requirements apply at the QOF level as compared to the Subsidiary QOZB level, including:
  - the base for calculating the 90% and 70% tests; and
  - additional requirements the Subsidiary QOZB must satisfy.
- Subsidiary QOZB must have at least 50% of its gross income from the *active conduct* of a trade or business in the zone. A trade or business is defined generally under Section 162 of the Code. Less well-defined is what constitutes the *active conduct* of a trade or business. However, rental real estate is an active conduct of a trade or business, but merely entering into a triple net lease is not an active trade or business.
- There are three safe harbors for determining whether 50% of a Subsidiary QOZB's gross income is derived from the active conduct of a trade or business in the zone. These safe harbors are when: (1) at least 50% of the services performed for the business, measured by hours, are performed within the zone; (2) at least 50% of the services performed for the business, measured by amounts paid for such services, are performed in the zone; and (3) both the tangible property of the business that is in a zone and the management/operational functions performed for the business in the zone are necessary to generate 50% of the gross income of the trade or business. ("Services" include those provided by employees and independent contractors (and employees of independent contractor.)) A subsidiary QOZB that does not satisfy a safe harbor may meet the requirement based upon facts and circumstances.
- Safe harbor for *reasonable working capital* that may be held at the Subsidiary QOZB level:
  - designated as working capital for acquisition, construction and/or substantial improvement of tangible property or for developing a business in a zone;
  - written schedule for spending the working capital;
  - working capital spent consistent with the written schedule; and
  - each working capital infusion must be spent within 31 months of receipt, with extensions for certain delays caused by governments.
- Most QOFs will utilize the two-tier structure because the QOZB is then permitted to hold reasonable working capital.
- Original use for purposes of the substantial improvement test applicable to QOZBP means placed in service for depreciation purposes.

For questions about qualified opportunity zones, please contact:

Wendi Kotzen, *Partner*
215.864.8305 | kotzenw@ballardspahr.com

Linda Schakel, *Partner*
202.661.2228 | schakel@ballardspahr.com

Molly Bryson, *Partner*
202.661.7638 | brysonm@ballardspahr.com

Douglas Fox, *Partner*
410.528.5505 | foxd@ballardspahr.com

April Hamlin, *Partner*
612.371.3522 | hamlina@ballardspahr.com

or any member of Ballard Spahr's Qualified Opportunity Zone Team:
https://www.ballardspahr.com/practiceareas/initiatives/qualified_opportunity_zones.aspx

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