goulston&storrs

Qualified Opportunity Zones: Final Regulations Provide Clarity

February 10, 2020
Tax Notes Federal

This article highlights changes made to the qualified Opportunity Zone provisions by the final regulations issued in December.

Reprinted with permission from Tax Notes Federal, February 10, 2020, p. 907

Treasury released the final regulations on the qualified Opportunity Zone (QOZ) provisions under section 1400Z-2 at the end of 2019.

The real estate industry has been awaiting final guidance on the Tax Cuts and Jobs Act's new QOZ provisions since the IRS's release of proposed regulations in October 2018 and May 2019. The final regulations, released December 19, 2019, clarify various issues raised by the proposed regulations and make several key changes to the previously proposed rules.

The final regulations and accompanying preamble exceeds 540 pages, mainly because the preamble contains the drafters' responses to many of the more than 300 comments received by Treasury on the proposed regulations. The vast majority of comments were rejected by the drafters, many because they were not authorized by the statutory provisions under which the regulations were issued. However, the final regulations do make several changes to the proposed rules, many of which are taxpayer-friendly.

Key guidance in the final regulations provides increased flexibility regarding the disposition of assets by subsidiaries of a qualified opportunity fund, which will facilitate the creation of multi-asset QOFs, and the addition of a new cure period for QOF subsidiaries that violate the strict qualification requirements for subsidiaries.

I. Effective Date and Applicability

The final regulations are effective 60 days after publication in the *Federal Register* and apply prospectively. For periods before the effective date, taxpayers can elect to rely on either the final regulations or the proposed regulations.[1] Regardless of the taxpayer's choice, the 10-year holding period basis step-up election under reg. section 1.1400Z2(c)-1 can only be made under the final regulations.[2]

II. Eligible Gains

The QOZ regime encourages taxpayers who have recognized eligible capital gains to invest those gains to defer recognition and to benefit from basis step-ups. The proposed regulations set forth

detailed rules regarding the determination of what constitutes eligible capital gains. The final regulations make some important changes to those rules, as outlined later.

A. Section 1231 Gains

The QOZ rules for section 1231 gains (from the sale of real property or other depreciable property used in a trade or business) have been completely revamped from those set forth in the proposed regulations, which is unsurprising considering how heavily those proposed rules were criticized. First, unlike the proposed rule that limited the eligible gain from section 1231 gains to the net section 1231 gain for the year, the final rule treats the gross amount of section 1231 gain as eligible gain (similar to other capital gains that are not required to be netted).[3] Further, that the taxpayer's gain would have been characterized as ordinary under section 1231 if it had not been deferred through a QOF investment (that is, if the taxpayer's section 1231 losses for the year exceed section 1231 gains) does not prevent the section 1231 gain from being treated as eligible gain. The final rules also eliminate the proposed regulations' special timing rule for measuring the 180-day period for section 1231 gains, which was proposed to begin the last day of the tax year. Under the final regulations, the 180-day period begins on the date of the sale, like any other capital gain.[4] The final regulations also clarify that when the deferred section 1231 gain is triggered (for example, in 2026 if the taxpayer has not disposed of the QOF investment before then), the determination of whether the section 1231 gain is ordinary or capital is made by just including it in the section 1231 gains for the year of the inclusion and applying the normal netting rule to determine if the section 1231 gains exceed the section 1231 losses for the inclusion year.[5]

B. Sale to QOF

The preamble to the final regulations clarifies that gains resulting from a sale of property to a QOF in connection with a plan to reinvest the proceeds into the same QOF may be recharacterized under general step transaction principles as if the property had been sold to the QOF, in which case the gain from the sale will not be eligible gain. Also, the QOF would not be treated as purchasing the property for cash, and therefore the property would not be treated as qualified property for purposes of meeting the 90 percent qualifying property test.[6]

C. Foreign Investors

Foreign investors (nonresident aliens and foreign corporations) can make eligible investments only using gains that are subject to U.S. tax (for example, treated as effectively connected income) and that are not eligible for a treaty exemption.[7] Foreign taxpayers will be required to certify that they are waiving any applicable treaty benefits for the gain they are investing into the QOF.[8] For reasons of practical administration (because partnerships often don't know if their partners' gains are subject to U.S. tax), the final regulations except partnerships from the requirement that gain be subject to federal income tax to constitute eligible gain.[9] However, under an antiabuse rule in the final regulations, a partnership formed or availed of for a "significant purpose" of avoiding the taxable eligible gain requirement will be disregarded.[10]

The final regulations clarify that a foreign seller of real property cannot use a nonrecognition certificate under the 1980 Foreign Investment in Real Property Tax Act to notify the purchaser that no withholding should be required because the seller intends to defer the gain through an eligible

investment in a QOF.[11] The preamble indicates that Treasury and the IRS are still considering how to address the mechanics of applying the QOZ regime to sales subject to FIRPTA withholding tax.[12] For now, a seller could consider applying for a withholding certificate from the IRS (which would likely grant relief only in a situation in which the qualifying investment is made before the end of the 20-day filing period for the withholding certificate request) or just paying the withholding tax and applying for a refund.

D. Hedged Positions

The final regulations include several taxpayer-favorable changes to the limitations on gain from a position that was or had been at any time in the past part of a straddle. First, under the final rules, the restriction on deferring gain from hedged positions only applies to actively traded property that is part of a straddle described in section 1092.[13] Second, under the final rules, the restriction only applies if the hedged position was part of a straddle during the current year or if there is a loss carryover to the current year from another position in the straddle, but there is otherwise no restriction on positions that were part of a straddle in a prior year.[14] Further, even if the position was part of a straddle in the current year, as long as the taxpayer disposes of all the positions in the straddle, the net gain is an eligible gain.[15] Finally, the broad restriction on hedged gains from section 1256 contracts (like regulated future contracts and traded options) in the proposed regulations, which disallowed all of the taxpayer's section 1256 gains if any of the taxpayer's section 1256 contracts were part of a straddle, is narrowed to disallow only the gain from the specific section 1256 positions that were part of the straddle.[16]

III. The 180-Day Reinvestment Period

Taxpayers are permitted a 180-day period in which to reinvest eligible gain into a QOF. The 180-day period generally runs from the date the gain being deferred was recognized.[17]

A. New 180-Day Period for Partners

The proposed regulations included special rules for measuring the 180-day period for gains recognized by a passthrough entity, giving owners of these entities additional flexibility to select a 180-day period running either from the date of the sale or from the last day in the entity's tax year.[18] The final regulations include a new election for partners, S corporation shareholders, and trust beneficiaries to measure the 180-day period for reinvesting an eligible gain realized by the passthrough entity from the date the federal tax return for the entity is timely filed.[19] This gives partners three bites at the apple (one beginning on the date the partnership realizes the gain, a second beginning at the end of the partnership's year, and a third when the return is filed).

B. Installment Sales

A special timing rule is provided for installment sales under which the taxpayer can elect either to start a separate 180-day period for each installment payment on the date the payment is received or to start the 180-day period on the last day of the year in which the gain would be recognized absent the QOZ investment.[20] It appears that under either method there is a separate 180-day period for each year in which installment payments are received. Presumably, a taxpayer who elects out of the installment method would treat the gain as recognized on the date of the sale and begin counting 180 days from that date.

The final regulations confirm that gain realized after the effective date of the TCJA from an installment sale completed before the effective date is eligible for deferral under the QOZ regime.[21]

IV. Inclusion Events

The final regulations largely adopt the rules in the May 2019 proposed regulations regarding some events (like disposition of the taxpayer's interest in a QOF or specified distributions) that result in the deferred gain being triggered and causing a termination of the QOF investment as an eligible investment ("inclusion events"). However, the final regulations make several changes to those rules.

A. Spousal Transfers

The final regulations state that a transfer between spouses or former spouses incident to a divorce is an inclusion event.[22]

B. QOF Mergers

The final regulations permit QOF partnership mergers to occur without triggering an inclusion event.[23]

C. Inclusion Event Consequences

Inclusion events generally cause a QOF investment to cease being an eligible investment and thus to not benefit from any basis step-up after 10 years. However, inclusion events resulting from partnership distributions in excess of basis (or from corporate distributions) do not prevent the taxpayer from getting the benefits of the basis step-up after 10 years under section 1400Z-2(c), as long as the taxpayer continues to hold the eligible investment in the QOF.[24]

The final regulations also allow the gain triggered by an inclusion event to be deferred through a new investment in a QOF within 180 days.[25] (The proposed regulations required a complete disposition of the QOF investment in order for a new deferral election to be made.[26])

V. Basis Step-Up After 10 Years

Section 1400Z-2 allows taxpayers who hold an eligible investment in a QOF for 10 years to elect, immediately before a sale of the eligible investment, to increase the basis of the investment to its fair market value at that time.[27] This election effectively eliminates the taxable gain from appreciation of the investment over the taxpayer's holding period.

A. Sales by a QOF or QOF Subsidiary

The proposed regulations allowed a partner who held an eligible investment in a QOF partnership for 10 years to elect to exclude gain from a sale of qualified Opportunity Zone property (QOZP) by the QOF. This gain exclusion election was not available for sales by a subsidiary of the QOF, however. The omission of the exclusion for sales by subsidiaries was heavily criticized by commentators because most QOFs hold their investments through qualified Opportunity Zone business (QOZB) subsidiaries.[28]

The final regulations extend the election to exclude gains from asset sales by QOZBs and sales by a QOF or QOZB of property that is not QOZP.[29] The election is, however, not available for inventory

(even though the statutory basis step-up at the QOF level would apparently be available even to the extent the QOF holds inventory assets).[30]

Under the final regulations, the election to exclude gain from asset sales can be made for multiple asset sales occurring in different years. This flexibility will facilitate the formation of QOFs by investment managers that hold multiple investments through one or more QOZBs. To avoid a double benefit for gain from a reinvestment of proceeds that benefited from the gain exclusion election in a prior year, the final regulations treat any net proceeds from a sale that are not distributed within 90 days as having been distributed and then as recontributed to the QOF (resulting in a "mixed fund investment").[31] Because the regulations do not adopt a tracing approach or apply section 704(c) principles to allocate existing gains on the date of a new investment to the earlier qualifying investments in the QOF, this rule effectively penalizes taxpayers on future gains that are not actually attributable to the reinvestment of the proceeds from a prior sale (because in the future a portion of those gains would be allocated to the deemed mixed fund investment). Accordingly, well-advised taxpayers will consider causing the QOF to promptly distribute the net proceeds from sales of property for which a gain exclusion election was made. Note that the final regulations treat proceeds used to pay nonqualified liabilities (that is, incurred within two years of the sale outside the ordinary course) as part of the net proceeds deemed distributed and recontributed.[32]

B. Amount of Basis Step-Up

The final regulations clarify that the basis step-up in a QOF partnership interest after 10 years is equal to the net FMV plus the partner's allocable share of the debt (even if the debt exceeds the gross FMV).[33]

VI. The QOF 90 Percent Asset Test

Section 1400Z-2(d) requires that a QOF meet a semiannual asset test under which at least 90 percent of the QOF's assets are held in QOZP.

A. Exclusion of Newly Contributed Cash

To alleviate the pressure on a QOF to deploy cash proceeds from eligible investments before the first semiannual testing date (because cash is not treated as QOZP), the proposed regulations allowed a QOF to exclude from the numerator and denominator of the 90 percent test any property held in the form of cash, cash equivalents, or short-term debt instruments that was received by the QOF within the last six months before the testing date.[34]

The final regulations adopt this safe harbor and further extend it to other contributed property that is converted into cash, cash equivalents, or short-term debt within five days of being received by the QOF.[35] However, the preamble identifies a question raised by a commentator about whether the safe harbor can be used by a newly formed QOF that has no assets apart from the cash that is being excluded from the 90 percent test. The commentator pointed out that excluding the cash from both the numerator and the denominator of the fraction results in a "divide by zero" undefined mathematical value. Unfortunately, the preamble does not provide any comfort that the safe harbor would be available in that situation.[36]

B. QOZ Partnership Interests

Most QOFs seek to satisfy the 90 percent asset test by holding interests in partnership interests in subsidiary QOZB partnerships. For an investment in a partnership to qualify as a QOZP for purposes of the QOF's 90 percent test, the QOZB partnership has to be a QOZB for substantially all (that is, 90 percent) of the QOF's holding period in the partnership.[37] The final regulations provide that this "substantially all" test is applied at the end of each semiannual testing period of any QOF that holds an interest in the QOZB and that it has to be met as of that testing date.[38] Because QOZB status is tested on a calendar-year basis, the final regulations permit the QOF to test the status of its QOZB subsidiaries for just the period beginning with the QOF's holding period for the QOZB interest and ending at the end of the last tax year of the QOZB on or before the QOF's relevant semiannual testing date (so an interest in a calendar-year QOZB that qualifies for a tax is treated as qualifying for any testing dates before the last day of the following year).[39] However, it is unclear whether the foregoing safe harbor applies for purposes of testing whether each QOZB subsidiary satisfies the requirement that substantially all its tangible personal property be used in a QOZ for substantially all the holding period of that property (the qualified Opportunity Zone business property (QOZBP) use requirement), as this particular test is required to be applied semiannually on the testing dates of the QOF owner(s) of the QOZB rather than at the end of the QOZB subsidiary's tax year.

Six-Month Cure Period

The final regulations include a new six-month cure period (until the next testing date) if a QOZB does not qualify on a testing date.[40] During the six-month cure period, the QOF can treat the QOZB as satisfying the substantially all requirement, so long as the failure is cured by the next testing date.[41] However, because the QOZB qualification is generally tested on the last day of the QOZB's tax year, it appears that the cure period is only intended to be available when the subsidiary QOZB's failure to qualify is a result of the QOZB's failing to satisfy the QOZBP use requirement described in the preceding paragraph. As noted earlier, this particular test is applied semiannually on the testing dates of the QOF owner(s) of the QOZB, so a failure on one testing date could be cured on the next semiannual testing date even if it falls in the middle of a tax year.

VII. Original Use Requirement

For property to qualify as QOZBP, the property is required to meet an original use test, under which the property generally cannot have been used in the QOZ before it was purchased by the QOF or by the QOZB. Property that does not meet the original use requirement can qualify under an alternative test if the property is "substantially improved" (defined as improved by expenditures equal to at least 100 percent of the cost of the property) in any 30-month period following the property's purchase.[42]

A. Prior Nonbusiness Use

The preamble to the final regulations asserts that property used for a nonbusiness use in the QOZ (even by a prior owner) does not satisfy the original use requirement and is required to be substantially improved to qualify as QOZBP.[43] However, this assertion appears to be unsupported by the text of the regulations themselves, which define original use as commencing "on the date any person first places the property in service in the qualified opportunity zone for purposes of

depreciation or amortization, or first uses it in a manner that would allow depreciation or amortization if that person were the property's owner."[44] Personal use property wouldn't be eligible for depreciation even though the person using the property is the owner.

B. Newly Constructed Buildings

The final regulations confirm that an investment in a completed newly constructed building that has not yet been placed into service satisfies the original use test and is consistent with the legislative purpose of the QOZ regime.[45] Treasury declined to adopt the issuance of a certificate of occupancy as a bright-line test for when a new building is considered to be placed in service.[46]

C. Improvements to Nonqualifying Property

The final regulations clarify that improvements made to qualifying property, including leased property or substantially improved property that does not meet the original use test, are treated as qualifying property.[47] However, improvements made to nonqualifying property (for example, property purchased before January 1, 2018) are not treated as qualifying property. Thus, there is no amount of improvement that allows nonqualifying property to become qualifying.[48]

D. Vacant Property

The proposed regulations treat property that has been vacant for five years as satisfying the original use test.[49] The final regulations reduce the period for which property is required to have been vacant from five years to one year for a property that was vacant on the date the census tract in which the property is located was designated as a QOZ (and remained vacant through the date of purchase), and three years in all other cases.[50] Vacancy is defined as the property being 80 percent unused.[51]

E. Government and Brownfield Sites

All property purchased from a local government that acquired the property through an involuntary transfer (like foreclosure for failure to pay real property taxes) is deemed to meet the original use test without regard to whether the property is actually in use.[52] Also, all brownfield sites are deemed to meet the original use test if, within a reasonable period, investments are made in the property to ensure that it meets basic health and environmental safety standards.[53]

VIII. Substantial Improvement

As mentioned earlier, property that does not meet the original use test is required to be substantially improved by expenditures equal to at least 100 percent of the cost of the property in any 30-month period following the property's purchase.[54]

A. Status of Property During Improvement

The final regulations clarify that property that is undergoing the substantial improvement process is treated as qualifying property during the 30-month improvement period if it is reasonably expected that the substantial improvement requirement will be met by the end of the 30-month period.[55]

B. New Property Aggregation Rules

For purposes of measuring whether the 100 percent substantial improvement threshold has been met for purchased property that does not satisfy the original use requirement, the final regulations

provide that property used as part of an integrated business can be aggregated.[56] Under this rule, original use property that is purchased for use in the same business as a non-original-use property and that improves the functionality of the non-original-use property counts toward satisfying the 100 percent substantial improvement threshold for the non-original-use property.[57] For example, new linen purchased for a hotel counts toward the substantial improvement threshold for the building in which the hotel is located. However, this rule does require that the non-original-use property itself be improved "by more than an insubstantial amount."[58]

The final regulations allow contiguous buildings to be aggregated for purposes of the 100 percent substantial improvement threshold if they are contained either within a parcel described in a single deed or in contiguous parcels involving separate deeds if (1) the buildings are operated exclusively by the QOF or QOZB; (2) the buildings share facilities or significant centralized business elements (personnel, accounting, and so on); and (3) the buildings are operated in coordination with or reliance on one or more of the trades or businesses.[59]

IX. Property Straddling a QOZ Census Tract

The proposed regulations provide that when real property straddles the borders of a QOZ census tract, if the square footage located within the QOZ census tract is substantial as compared with the square footage outside the QOZ, and the real property outside the QOZ is contiguous to part or all the real property located inside the QOZ, then all the property is deemed to be located within a QOZ.[60] The preamble to the proposed regulations somewhat confusingly suggested that for this purpose, property in the QOZ should be considered to be substantial if the cost of that portion is more than the cost of the real property outside the zone.[61]

The final regulations include two alternative tests, one based on square footage and one based on cost.[62] There is a presumption (presumably rebuttable) that cost is allocated based on square footage. The method chosen must be applied consistently throughout the holding period for the property.

The final regulations clarify that properties separated only by the interposition of a road, street, railroad, stream, or similar property are treated as contiguous for purposes of the rule regarding property that straddles a census tract.[63] On the other hand, parcels that touch only at a common corner are not contiguous.[64]

X. Working Capital Safe Harbor

A QOZB is generally prohibited from holding more than 5 percent of its assets in the form of cash or other nonqualified financial property, with a limited exception for working capital. The proposed regulations included a safe harbor that permitted a QOZB to treat as working capital cash held for a period of up to 31 months according to a written plan providing for the funds to be spent on the development of a trade or business in the QOZ including the purchase and construction of real property in the QOZ.[65] The proposed regulations provide that the 31-month safe harbor period could be extended if the delay in spending the funds was the result of delays caused by waiting for governmental approvals.[66]

The final regulations clarify that the extension of the 31-month working capital safe harbor for delays caused by governmental approvals generally only applies if governmental approval is still

pending at the end of the 31 months but it does not toll the period if the approval is obtained before the end of the 31 months.[67] A limited exception is available in situations in which no other action could be taken to improve the property or complete the project during the permitting process.[68] Also, an additional 24 months is available for projects in a federally declared disaster area if the delay is caused by the disaster.[69]

XI. New Trade or Business Safe Harbor

A QOZB is required to be engaged in a trade or business that meets several requirements regarding the degree of nexus between the QOZB and the QOZ(s) in which it operates. These requirements include that 50 percent of the gross income of the QOZB be derived from its trade or business[70] and that substantially all (defined as 70 percent) of the tangible property owned or leased by the QOZB be used in the trade or business of the QOZB for substantially all of the property's holding period.[71] There had been some concern from commentators that a QOZB that is in a startup phase, like a QOZB that has purchased a property and is in the process of substantially improving the property, could have difficulty satisfying the trade or business requirement.

The final regulations add a new trade or business safe harbor for start-ups that is tied to the 31-month working capital safe harbor introduced by the proposed regulations and adopted with some modifications by the final regulations. Income (for example, interest income) that is earned on the working capital during the 31-month period is treated as having been earned in the QOZB's trade or business for purposes of the 50 percent gross income test.[72] Also, tangible property that is purchased, leased, or improved with the working capital and intangible property purchased or licensed with the working capital is treated during the safe harbor period as meeting the 70 percent substantially requirement (that is, treated as used in the trade or business of the QOZ).[73]

Further, the final regulations allow the startup safe harbor to be extended beyond the 31-month period following an initial injection of working capital if there are subsequent injections of working capital with their own 31-month working capital safe harbors, for a total of up to 62 months.[74] The subsequent capital injections must occur as an integral part of the plan covered by the initial 31-month working capital safe harbor.[75]

XII. Triple Net Leases

The proposed regulations provide that for purposes of section 1400Z-2, the ownership and operation (including leasing) of real property is generally treated as a trade or business, but that merely entering into a triple net lease does not constitute a trade or business.[76] The final regulations continue to provide that merely entering into a triple net lease does not constitute a trade or business.[77] An example intended to clarify this rule shows that when a building is triple net leased to a single tenant, the landlord is not treated as engaged in the active conduct of a trade or business even if the landlord maintains a staff of employees "to address any issues that may arise with respect to the triple-net-lease."[78] The example does not explicitly answer the question of whether the result would be different if the employees were actually engaged in operating the property, as would be typical in a multi-tenant office building when leases commonly require the tenants to pay all taxes, insurance, and common area maintenance. However, the reference to addressing "issues that may arise" suggests that the employees in the example are not actually

operating the property. Another example is in the final regulations to illustrate that when only a portion of the property is triple net leased, the whole property may be treated as held in the trade or business.[79]

XIII. Sin Business Limitation

Section 1400Z-2 prohibits a QOZB from operating any "sin business," like a private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack or other facility used for gambling, or any store the principal business of which is the sale of alcoholic beverages for consumption off premises.

The final regulations do not prohibit QOFs from engaging in sin businesses (the prohibition only applies to QOZBs). However, the final regulations do prohibit QOZBs from leasing more than 5 percent of their property to a sin business.[80]

XIV. Antiabuse Rule

Section 1400Z-2(e) authorizes Treasury to issue regulations to prevent the abuse of the QOZ regime. The final regulations include a broad antiabuse rule stating that if a significant purpose of a transaction is to achieve a tax result that is inconsistent with the purposes of section 1400Z-2 and the final regulations, the transaction will be recast to achieve a tax result consistent with the statute and regulations including, if appropriate, treating an investment as other than a qualifying investment.[81] The final regulations articulate the purpose the QOZ regime as providing specified federal tax benefits to owners of QOFs to encourage the making of longer-term investments, through QOFs and QOZBs, of new capital in one or more QOZs and to increase the economic growth of QOZs.[82]

One area of focus for Treasury and the IRS is to prevent QOFs from being used to purchase land (which is not subject to the 100 percent substantial improvement requirement) for speculative purposes without any intention of using the land to significantly increase economic activity in a QOZ. The final regulations confirm that those investments violate the antiabuse rule even if they are structured to comply with the technical requirements of the final regulations.

Two examples in the final regulations illustrate the operation of the antiabuse rule in the context of those transactions. One of those examples indicates that if a tract of land in a QOZ is purchased with a significant purpose of selling the land at a profit and excluding the gain from tax, and if the only use planned for the land is to pave it and use it as an outdoor parking lot (to be staffed by a single parking attendant), then the land will not qualify as a QOZB under the antiabuse rule.[83] The second example indicates that if the purchased land will be used for agricultural purposes requiring significant capital improvements to the land, including improvements to and construction of farm structures and installation of a new irrigation system, then the antiabuse rule does not apply.[84]

XV. Consolidated Group Rules

The final regulations permit a QOF C corporation to be a subsidiary member of a consolidated group if two conditions are met: (1) the corporation(s) making the eligible investment(s) into the QOF maintain a direct equity interest in the QOF; and (2) all the other subsidiary members of the consolidated group that are QOF investors are wholly owned by the parent of the consolidated

group (not just 80 percent owned, which would be sufficient for them to be part of the consolidated group).[85]

The final regulations include several special rules to ensure that the single-entity principles of the consolidated group regime are preserved without frustrating the purposes of the QOF rules:

- On a disposition of the QOF stock, any excess loss account regarding the QOF stock has to be taken into account before the 10-year step-up eliminates it.[86] (In contrast, in the QOF partnership context the final regulations ordinarily permit the basis step-up to reverse basis reductions from depreciation and eliminate the recapture of the depreciation.)
- Distributions in excess of basis (which give rise to an excess loss account) trigger inclusions just like section 301(c)(3) distributions by a QOF outside a consolidated group.[87]
- Transactions between a QOF or its subsidiaries and other members of the affiliated group are not treated as intercompany transactions.[88]
- The qualification tests for QOFs and QOZBs are applied on a separate-entity basis.[89]
- A special transition rule allows preexisting QOF consolidated subsidiaries to elect among a host of alternatives: partnership treatment, nonaffiliated QOF corporate treatment, or non-QOF treatment (or to continue consolidated QOF subsidiary treatment).[90]
- Intercompany gain can be treated as eligible gain under the matching rule (when the property is then sold to an unrelated party outside the group).[91]

XVI. Conclusion

The final regulations eliminate some of the technical barriers that were inhibiting taxpayers from making investments in QOFs and address many of the uncertainties that were raised by the proposed regulations. However, the final regulations do leave some important questions unanswered. This article only describes selected highlights from the final regulations. In particular, it focuses on the changes from the proposed regulations and only touches on the many rules that were incorporated from the proposed regulations without significant change. Accordingly, readers are cautioned to read the final regulations in full.

© 2020 Tax Analysts. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

Copyright 2020 Abraham Leitner. All rights reserved.

1 T.D. 9889, at 2.
2 See id.
3 Reg. section 1.1400Z2(a)-1(b)(11)(iii)(A).
4 Reg. section 1.1400Z2(a)-1(b)(11)(iv)(B).
5 Reg. section 1.1400Z2(a)-1(c)(1)(ii).
6 T.D. 9889, at 22-24.
7 Reg. section 1.1400Z2(a)-1(b)(11)(ix)(A)(1).
8 Reg. section 1.1400Z2(a)-1(b)(11)(ix)(A)(2).

9 Reg. section 1.1400Z2(a)-1(b)(11)(ix)(B).
10 Reg. section 1.1400Z2(f)-1(c).
11 See reg. section 1.1400Z2(a)-1(e).
12 T.D. 9889, at 59.
13 Reg. section 1.1400Z2(a)-1(b)(11)(vi)(A)(2).
14 Reg. section 1.1400Z2(a)-1(b)(11)(vi)(A).
15 Reg. section 1.1400Z2(a)-1(b)(11)(vi)(C).
16 Reg. section 1.1400Z2(a)-1(b)(11)(vi)(B).
17 Reg. section 1.1400Z2(a)-1(b)(7).
18 Reg. section 1.1400Z2(a)-1(c)(8)(iii); reg. section 1.1400Z2(a)-1(c)(9).
19 Id.
20 Reg. section 1.1400Z2(a)-1(b)(11)(viii)(B).
21 Reg. section 1.1400Z2(a)-1(b)(11)(viii)(A).
22 Reg. section 1.1400Z2(b)-1(c)(3)(ii).
23 Reg. section 1.1400Z2(b)-1(c)(6)(ii)(C)(2).
24 Reg. section 1.1400Z2(c)-1(b)(1)(v).
25 Reg. section 1.1400Z2(a)-1(b)(11)(iv).
26 See T.D. 9889, at 43.
27 Reg. section 1.1400Z2(c)-1(b)(1)(i).
28 T.D. 9889, at 320.
29 Reg. section 1.1400Z2(c)-1(b)(2)(ii)(A).
30 Id.
31 Reg. section 1.1400Z2(c)-1(b)(2)(ii)(B).
32 Reg. section 1.1400Z2(c)-1(b)(2)(ii)(B)(3).
33 Reg. section 1.1400Z2(c)-1(b)(2)(i).
34 T.D. 9889, at 140.
35 Reg. section 1.1400Z2(d)-1(b)(2)(i)(B).
36 T.D. 9889, at 141-142.
37 Reg. section 1.1400Z2(d)-1(c)(2)(i)(C).
38 Reg. section 1.1400Z2(d)-1(c)(2)(i)(C)(2).
39 Reg. section 1.1400Z2(d)-1(b)(2)(i)(C).
40 Reg. section 1.1400Z2(d)-1(d)(6).
41 Id.
42 Reg. section 1.1400Z2(d)-2(b)(2).
43 T.D. 9889, at 176.
44 Reg. section 1.1400Z2(d)-2(b)(3)(i)(A).
45 Reg. section 1.1400Z2(d)-2(b)(3)(i)(D)(1).
46 T.D. 9889, at 175-176.
47 Reg. section 1.1400Z2(d)-2(b)(2).
48 T.D. 9889, at 178-179.
49 Id. at 180-181.
50 Reg. section 1.1400Z2(d)-2(b)(3)(i)(B).

51 Reg. section 1.1400Z2(d)-2(b)(3)(iii).
52 Reg. section 1.1400Z2(d)-2(b)(3)(v).
53 Reg. section 1.1400Z2(d)-2(b)(3)(iv).
54 Reg. section 1.1400Z2(a)-1(b)(1).
55 Reg. section 1.1400Z2(d)-2(b)(4)(ii).
56 Reg. section 1.1400Z2(d)-2(b)(4)(v).
57 Reg. section 1.1400Z2(d)-2(b)(4)(v)(D).
58 Reg. section 1.1400Z2(d)-2(b)(4)(iii)(B).
59 Reg. section 1.1400Z2(d)-2(b)(4)(v).
60 Reg. section 1.1400Z2(d)-1(d)(3)(ix).
61 T.D. 9889, at 251.
62 Reg. section 1.1400Z2(d)-1(d)(3)(ix)(E).
63 Reg. section 1.1400Z2(d)-1(d)(3)(ix)(F).
64 Id.
65 T.D. 9889, at 241.
66 Id. at 242.
67 Reg. section 1.1400Z2(d)-1(d)(3)(v)(C).
68 See T.D. 9889, at 244.
69 Reg. section 1.1400Z2(d)-1(d)(3)(v)(D).
70 Reg. section 1.1400Z2(d)-1(d)(3)(i).
71 Reg. section 1.1400Z2(d)-1(d)(2)
72 Reg. section 1.1400Z2(d)-1(d)(3)(vi).
73 Reg. section 1.1400Z2(d)-1(d)(3)(viii)(A).
74 Reg. section 1.1400Z2(d)-1(d)(3)(v)(F).
75 Id.
76 T.D. 9889, at 235-236.
77 Reg. section 1.1400Z2(d)-1(d)(3)(iii).
78 Reg. section 1.1400Z2(d)-1(d)(3)(iii)(C)(1).
79 See reg. section 1.1400Z2(d)-1(d)(3)(iii)(C)(2).
80 Reg. section 1.1400Z2(d)-1(d)(4).
81 Reg. section 1.1400Z2(f)-1(c)(1).
82 Id.
83 Reg. section 1.1400Z2(f)-1(c)(3)(iv).
84 Reg. section 1.1400Z2(f)-1(c)(3)(v).
85 Reg. section 1.1400Z2(b)-1(c)(9)(i)(B).
86 Reg. section 1.1502-14Z(b)(1)(iii).
87 Reg. section 1.1502-14Z(b)(1)(i).
88 Reg. section 1.1502-14Z(b)(1)(iv).
89 Reg. section 1.1502-14Z(b)(1)(v).
90 Reg. section 1.1502-14Z(f).
91 Reg. section 1.1502-14Z(c)(5).