

26 USC 1400Z-2: Special rules for capital gains invested in opportunity zones

Text contains those laws in effect on September 5, 2018

From Title 26-INTERNAL REVENUE CODE

Subtitle A-Income Taxes

CHAPTER 1-NORMAL TAXES AND SURTAXES

Subchapter Z-Opportunity Zones

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§1400Z–2. Special rules for capital gains invested in opportunity zones

(a) In general

(1) Treatment of gains

In the case of gain from the sale to, or exchange with, an unrelated person of any property held by the taxpayer, at the election of the taxpayer-

(A) gross income for the taxable year shall not include so much of such gain as does not exceed the aggregate amount invested by the taxpayer in a qualified opportunity fund during the 180-day period beginning on the date of such sale or exchange,

(B) the amount of gain excluded by subparagraph (A) shall be included in gross income as provided by subsection (b), and

(C) subsection (c) shall apply.

(2) Election

No election may be made under paragraph (1)-

(A) with respect to a sale or exchange if an election previously made with respect to such sale or exchange is in effect, or

(B) with respect to any sale or exchange after December 31, 2026.

(b) Deferral of gain invested in opportunity zone property

(1) Year of inclusion

Gain to which subsection (a)(1)(B) applies shall be included in income in the taxable year which includes the earlier of-

(A) the date on which such investment is sold or exchanged, or

(B) December 31, 2026.

(2) Amount includible

(A) In general

The amount of gain included in gross income under subsection (a)(1)(A) shall be the excess of-

(i) the lesser of the amount of gain excluded under paragraph (1) or the fair market value of the investment as determined as of the date described in paragraph (1), over

(ii) the taxpayer's basis in the investment.

(B) Determination of basis

(i) In general

Except as otherwise provided in this clause or subsection (c), the taxpayer's basis in the investment shall be zero.

(ii) Increase for gain recognized under subsection (a)(1)(B)

The basis in the investment shall be increased by the amount of gain recognized by reason of subsection (a)(1)(B) with respect to such property.

(iii) Investments held for 5 years

In the case of any investment held for at least 5 years, the basis of such investment shall be increased by an amount equal to 10 percent of the amount of gain deferred by reason of subsection (a)(1)(A).

(iv) Investments held for 7 years

In the case of any investment held by the taxpayer for at least 7 years, in addition to any adjustment made under clause (iii), the basis of such property shall be increased by an amount equal to 5 percent of the amount of gain deferred by reason of subsection (a)(1)(A).

(c) Special rule for investments held for at least 10 years

In the case of any investment held by the taxpayer for at least 10 years and with respect to which the taxpayer makes an election under this clause, the basis of such property shall be equal to the fair market value of such investment on the date that the investment is sold or exchanged.

(d) Qualified opportunity fund

For purposes of this section-

(1) In general

The term "qualified opportunity fund" means any investment vehicle which is organized as a corporation or a partnership for the purpose of investing in qualified opportunity zone property (other than another qualified opportunity fund) that holds at least 90 percent of its assets in qualified opportunity zone property, determined by the average of the percentage of qualified opportunity zone property held in the fund as measured-

(A) on the last day of the first 6-month period of the taxable year of the fund, and

(B) on the last day of the taxable year of the fund.

(2) Qualified opportunity zone property

(A) In general

The term "qualified opportunity zone property" means property which is-

- (i) qualified opportunity zone stock,
- (ii) qualified opportunity zone partnership interest, or
- (iii) qualified opportunity zone business property.

(B) Qualified opportunity zone stock

(i) In general

Except as provided in clause (ii), the term "qualified opportunity zone stock" means any stock in a domestic corporation if-

(I) such stock is acquired by the qualified opportunity fund after December 31, 2017, at its original issue (directly or through an underwriter) from the corporation solely in exchange for cash,

(II) as of the time such stock was issued, such corporation was a qualified opportunity zone business (or, in the case of a new corporation, such corporation was being organized for purposes of being a qualified opportunity zone business), and

(III) during substantially all of the qualified opportunity fund's holding period for such stock, such corporation qualified as a qualified opportunity zone business.

(ii) Redemptions

A rule similar to the rule of section 1202(c)(3) shall apply for purposes of this paragraph.

(C) Qualified opportunity zone partnership interest

The term "qualified opportunity zone partnership interest" means any capital or profits interest in a domestic partnership if-

(i) such interest is acquired by the qualified opportunity fund after December 31, 2017, from the partnership solely in exchange for cash,

(ii) as of the time such interest was acquired, such partnership was a qualified opportunity zone business (or, in the case of a new partnership, such partnership was being organized for purposes of being a qualified opportunity zone business), and

(iii) during substantially all of the qualified opportunity fund's holding period for such interest, such partnership qualified as a qualified opportunity zone business.

(D) Qualified opportunity zone business property

(i) In general

The term "qualified opportunity zone business property" means tangible property used in a trade or business of the qualified opportunity fund if-

(I) such property was acquired by the qualified opportunity fund by purchase (as defined in section 179(d)(2)) after December 31, 2017,

(II) the original use of such property in the qualified opportunity zone commences with the qualified opportunity fund or the qualified opportunity fund substantially improves the property, and

(III) during substantially all of the qualified opportunity fund's holding period for such property, substantially all of the use of such property was in a qualified opportunity zone.

(ii) Substantial improvement

For purposes of subparagraph (A)(ii), property shall be treated as substantially improved by the qualified opportunity fund only if, during any 30-month period beginning after the date of acquisition of such property, additions to basis with respect to such property in the hands of the qualified opportunity fund exceed an amount equal to the adjusted basis of such property at the beginning of such 30-month period in the hands of the qualified opportunity fund.

(iii) Related party

For purposes of subparagraph (A)(i), the related person rule of section 179(d)(2) shall be applied pursuant to paragraph (8) of this subsection 1 in lieu of the application of such rule in section 179(d)(2)(A).

(3) Qualified opportunity zone business

(A) In general

The term "qualified opportunity zone business" means a trade or business-

(i) in which substantially all of the tangible property owned or leased by the taxpayer is qualified opportunity zone business property (determined by substituting "qualified opportunity zone business" for "qualified opportunity fund" each place it appears in paragraph (2)(D)),

(ii) which satisfies the requirements of paragraphs (2), (4), and (8) of section 1397C(b), and

(iii) which is not described in section 144(c)(6)(B).

(B) Special rule

For purposes of subparagraph (A), tangible property that ceases to be a qualified opportunity zone business property shall continue to be treated as a qualified opportunity zone business property for the lesser of-

(i) 5 years after the date on which such tangible property ceases to be so qualified, or

(ii) the date on which such tangible property is no longer held by the qualified opportunity zone business.

(e) Applicable rules

(1) Treatment of investments with mixed funds

In the case of any investment in a qualified opportunity fund only a portion of which consists of investments of gain to which an election under subsection (a) is in effect-

(A) such investment shall be treated as 2 separate investments, consisting of-

(i) one investment that only includes amounts to which the election under subsection (a) applies, and

(ii) a separate investment consisting of other amounts, and

(B) subsections (a), (b), and (c) shall only apply to the investment described in subparagraph (A)(i).

(2) Related persons

For purposes of this section, persons are related to each other if such persons are described in section 267(b) or 707(b)(1), determined by substituting "20 percent" for "50 percent" each place it occurs in such sections.

(3) Decedents

In the case of a decedent, amounts recognized under this section shall, if not properly includible in the gross income of the decedent, be includible in gross income as provided by section 691.

(4) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including-

(A) rules for the certification of qualified opportunity funds for the purposes of this section,

(B) rules to ensure a qualified opportunity fund has a reasonable period of time to reinvest the return of capital from investments in qualified opportunity zone stock and qualified opportunity zone partnership interests, and to reinvest proceeds received from the sale or disposition of qualified opportunity zone property, and

(C) rules to prevent abuse.

(f) Failure of qualified opportunity fund to maintain investment standard

(1) In general

If a qualified opportunity fund fails to meet the 90-percent requirement of subsection (c)(1),² the qualified opportunity fund shall pay a penalty for each month it fails to meet the requirement in an amount equal to the product of-

(A) the excess of-

(i) the amount equal to 90 percent of its aggregate assets, over

(ii) the aggregate amount of qualified opportunity zone property held by the fund, multiplied by

(B) the underpayment rate established under section 6621(a)(2) for such month.

(2) Special rule for partnerships

In the case that the qualified opportunity fund is a partnership, the penalty imposed by paragraph (1) shall be taken into account proportionately as part of the distributive share of each partner of the partnership.

(3) Reasonable cause exception

No penalty shall be imposed under this subsection with respect to any failure if it is shown that such failure is due to reasonable cause.

(Added Pub. L. 115–97, title I, §13823(a), Dec. 22, 2017, 131 Stat. 2184 .)

Effective Date

Section effective on Dec. 22, 2017, see section 13823(d) of Pub. L. 115–97, set out as an Effective Date of 2017 Amendment note under section 1016 of this title.

1 So in original. This subsection does not contain a paragraph (8).

2 So in original. Probably should be "subsection (d)(1),".