

# Opportunity Zones: Spurring Development In Indian Country

By **Nicole Elliott, Kristin DeKuiper and Katy Rossiter** August 21, 2018, 3:59 PM EDT

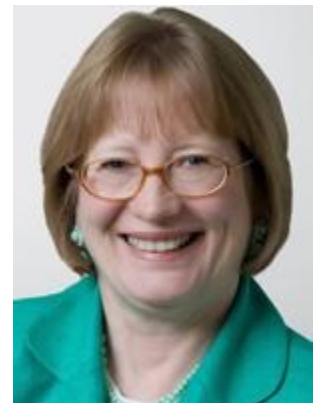
The tax reform approved by Congress and signed by President Donald Trump late last year contained an important incentive designed to spur economic development in low-income communities — the new opportunity zone incentive. Taxpayers who invest under the new law can reap significant tax benefits. Among those who should be interested in the new opportunity zone incentive are tribes who can leverage this incentive to attract investment.



Nicole Elliott

## The New Opportunity Zone Incentive

The Tax Cuts and Jobs Act of 2017 moved through Congress and was signed into law at breakneck speed. While much of its content built off existing tax law, the new incentive for investments in opportunity zones was not contained in existing tax law. The idea, however, was pushed in a stand-alone bill earlier in the 114th and 115th Congress on a bipartisan basis by Sen. Cory Booker, D-N.J., and Sen. Tim Scott, R-S.C. The timing aligned and the stand-alone bill made its way into the 2017 tax reform bill.



Kristin DeKuiper

The new opportunity zone incentive continues a successful history of using the tax code to spur investment in communities that need it — examples include the Low-Income Housing Tax Credit (1986), the Empowerment Zone provisions (1993, now defunct) and the New Markets Tax Credit (2000). Unlike these provisions, however, the new opportunity zone incentive is unique in that it can be used to fund a larger variety of businesses and projects and it has no limits in the amount that can be channeled into these business and projects.



Katy Rossiter

## The New Terms

The statute and this article contain a number of defined terms. Orientation to the terms and their simple definitions is helpful:

- Opportunity Zone — [U.S. Department of the Treasury](#) designated low-income community census tract;
- Qualified Opportunity Zone Fund — the investment vehicle;
- Qualified Opportunity Zone Property — the property that must be held by the fund and can be one of three things:
  - Stock in a Qualified Opportunity Zone Business;
  - Partnership Interest in a Qualified Opportunity Zone Business; or
  - Qualified Opportunity Zone Business Property.

## What Are the Benefits of Investing in a Qualified Opportunity Zone Fund?

Thanks to the new statute, contained in new Internal Revenue Code Sections 26 U.S.C. 1400Z-1 and 1400Z-2, taxpayers (whether they are individuals or corporations) who invest their realized capital gains in qualified opportunity zone funds benefit in three distinct ways.

First, taxpayers can temporarily defer recognizing gain on their tax return until they either divest their interest in the qualified opportunity zone fund or until Dec. 31, 2026, whichever comes first.

Second, taxpayers can receive some forgiveness of the gain that ultimately needs to be recognized (through a step up in basis). If they stay invested in the qualified opportunity fund for at least five years, 10 percent of the deferred gain is forgiven and an additional 5 percent of the deferred gain is forgiven if they stay invested for seven years.

Third, if taxpayers stay invested for at least 10 years, the basis of their investment in the qualified opportunity zone fund jumps to fair market value when their interest in the fund is sold, meaning taxpayers will not pay tax on the gain resulting from appreciation of the investment in the qualified opportunity zone fund itself.

### **What Is a Qualified Opportunity Zone Fund?**

To be a qualified opportunity zone fund, i.e., the investment vehicle, the fund must hold at least 90 percent of its assets in qualified opportunity zone property. Per the statute, a qualified opportunity zone fund must meet the 90 percent test by reviewing its holdings at two points during the fund's tax year — at the end of the first six months of the fund's tax year and then at the end of the tax year. If the average is less than 90 percent, the fund will have to pay a penalty to the [IRS](#) based on how much it missed the 90 percent mark.

As noted above, qualified opportunity zone property means an interest (stock or partnership interest) in a qualified opportunity zone business or directly in a qualified opportunity zone business property. The terms qualified opportunity zone business and qualified opportunity zone business property are defined by the statute in a way that, while restrictive, is designed to spur real economic growth in the designated opportunity zones by, for example, triggering the renovation of existing structures and adding jobs to communities.

Although there are chances to leverage the new opportunity zone incentives in a wide variety of industries — including real estate projects, energy projects and tech startups — one significant limitation in the law is that a qualified opportunity zone business cannot be a certain type of designated business such as a golf course, country club, racetrack or other facility used for gambling.

### **How Can Indian Country Benefit from the New Opportunity Zone Incentive?**

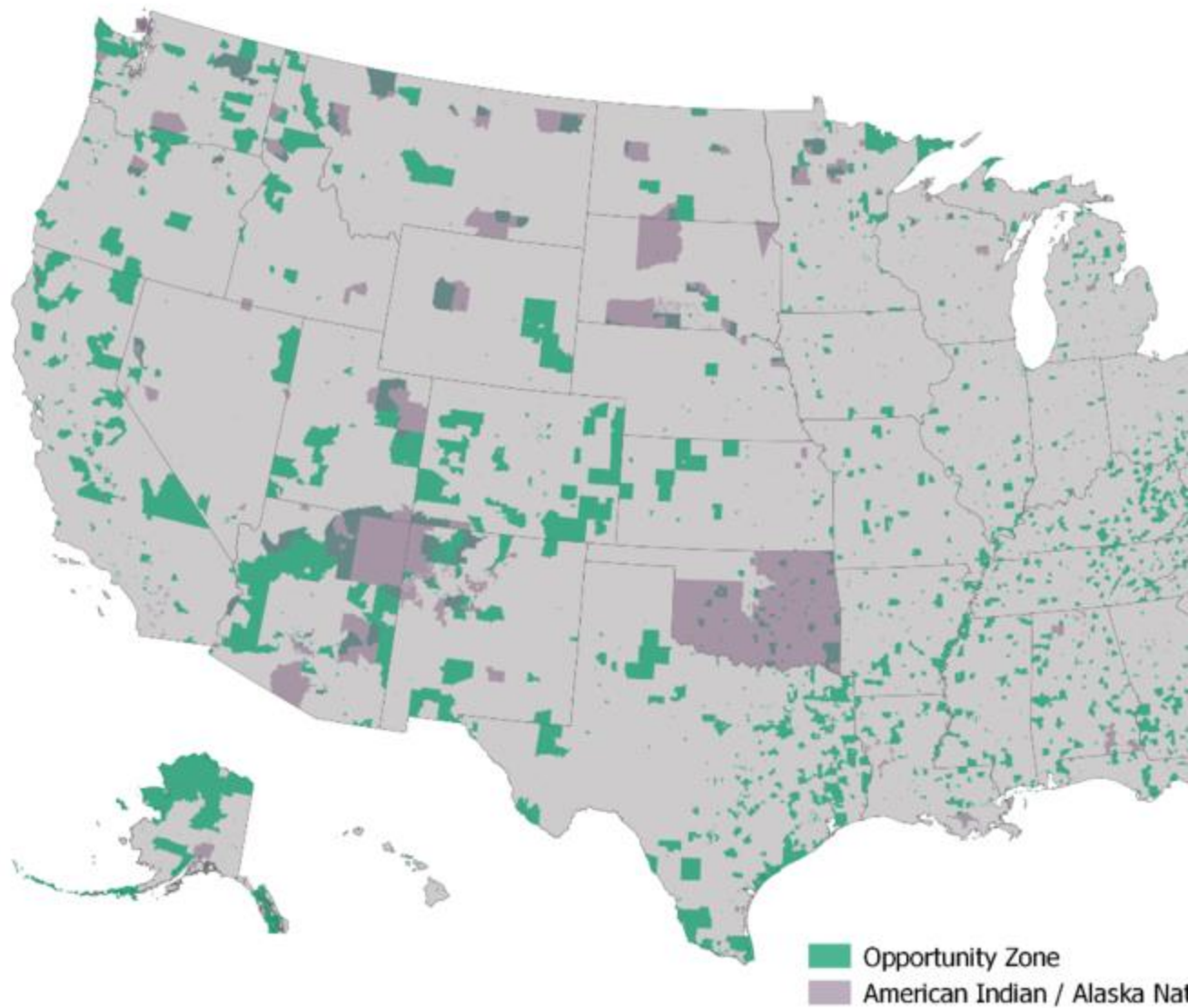
Many are excited by this new tax incentive — including taxpayers who want to reap the benefits of investment, those who want to set up or manage a qualified opportunity zone fund either to defer their own personal tax gains or to solicit outside investors and those who want to start or ensure they are a qualified opportunity zone business in order to raise needed capital. Indian Country should also be interested and prepared to take advantage of the incentive.

Tribes and tribal economic enterprises are in a unique position to harness the new opportunity zone incentive. As shown below, there is a significant overlap between Indian Country and the designated opportunity zones. Tribes who want to leverage the new opportunity zone incentive should work to make investment in tribal areas or tribal businesses attractive to qualified opportunity zone funding or may wish to set up or manage their own qualified opportunity zone fund.

### **Where Are Opportunity Zones?**

At the core of the new opportunity zone incentive are the communities that the law intends to benefit. Earlier in the year, the U.S. Department of the Treasury, with the input of state governors, designated certain low-income community tracts as opportunity zones.

The below map shows the new opportunity zones and the current American Indian, Alaska Native and Native Hawaiian areas. These tribal lands include legal entities, such as state and federally recognized American Indian reservations and trust lands, as well as statistical areas, such as Alaska Native villages and tribal areas in Oklahoma. A review of the overlap reveals that 362 opportunity zones cross into tribal areas. (If one considers opportunity zones adjacent to tribal areas, this number increases.) While this represents a small portion of opportunity zones (4 percent), a larger number of tribal entities are represented (38 percent).



### Further Information

Although there is a lot of excitement about the new opportunity zone incentive, there remain many unknowns on how the law should be interpreted and implemented. As with any change in the tax law, the Treasury Department and the IRS must provide further legal guidance to taxpayers and those who want to harness the new incentive.

Currently, the official places to find updates and information on the new opportunity zone incentive are the IRS and Treasury Department websites.

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**Disclaimer: Holland & Knight's Native American law practice actively represents several tribes.**

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