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Pay Zero Tax on Sale of Your Business/Stock/Other Assets!?

New Law

Created by the Tax Cuts and Jobs Act (TCJA), Opportunity Zones were designed to increase investment in low income communities throughout the country. In June of 2018 over 8,000 communities in all 50 states, the District of Columbia and five U.S. territories were designated as Qualified Opportunity Zones (QOZ).

What is a Qualified Opportunity Fund (QOF)?

Any gain from a sale or exchange of property by a taxpayer, to an unrelated person, that is invested in a QOF are any investment vehicle, organized as domestic corporations or partnerships, that holds at least 90 percent of its assets in QOZ property. Disregarded entities are not, however, eligible to be QOZs.

QOZ property includes: QOZ stock, QOZ partnership interest, or QOZ business property. QOZ Property is tangible property used in a trade or business. QOZ Partnership Interests and Stock are equity interests in certain businesses that operate in QOZs.

Who can invest?

C Corporations (including RICs and REITs), individuals, partnerships, S corporations, and trust and estates can invest.

How does a taxpayer defer the gain?

Any gain from a sale or exchange of property by a taxpayer, to an unrelated person, that is invested in a QOF within 180 days of a sale is excluded from income until the earlier of the date the investment is sold, or December 31, 2026. Only the gain needs to be reinvested, not the proceeds from the sale.

To elect to defer gain, the taxpayer makes a deferral election by attaching Form 8949 to their Federal income tax returns in the – year of sale. It should be noted that, when a partnership elects to defer gain it is done at the partnership level. However, if the partnership does not elect to defer the gain; the gain is allocated to the partner and the partner can defer the gain individually.

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The 5, 7 and 10-year rule

Once a taxpayer holds an investment in a QOF for five years his or her basis in the property is stepped up by 10 percent of the deferred gain. Additionally, once investments are held for seven years the basis is increased by another 5 percent of the original gain. Finally, if the investment in the QOF is held by the taxpayer for at least ten years and the taxpayer makes a basis adjustment/ permanent exclusion election,the basis of the property equals the fair market value of the investment when the investment is sold or exchanged. Since the basis equals the FMV there is no gain or loss realized on the sale or exchange.

Example

Taxpayer is an individual who purchased land for $1,000,000 in 2014. The land has appreciated to $1,200,000 in 2018 and is disposed/sold. Before 180 days expire, the $200,000 gain is invested in a QOF which is invested in QOZ property. As such, the taxpayer owes no tax in 2018 with respect to the $200,000 gain.

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Please reach out if you need further assistance with this matter!

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