



Opportunity Zone Program vs. 1031 Exchanges vs. IRC 453 Structures

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The Opportunity Zone program is a new investment vehicle created under a provision of the Tax Cuts and Jobs Act of December 2017. The program was developed to encourage investors to invest funds in economically distressed communities thereby stimulating economic development in these areas. When certain funds are invested in these communities, known as Qualified Opportunity Zones (QOZ), investors can enjoy immediate, as well as eventual tax benefits. Such benefits can include deferral of gain, partial forgiveness of deferred gain, and complete forgiveness of certain additional future gains if certain investment criteria are satisfied. On October 19th, the Treasury Department and the Internal Revenue Service issued proposed regulations and other published guidance for the new QOZ tax incentive. The proposed regulations can be found here:

<https://www.irs.gov/newsroom/treasury-irs-issue-proposed-regulations-on-new-opportunity-zone-tax-incentive>

Under the program, investors are able to temporarily defer some capital gains taxes and potentially eliminate certain other future capital gains taxes when they invest their realized gains in a Qualified Opportunity Fund (QOF), which is a corporation or partnership that invests at least 90% of its assets in QOZ property or interests. The realized gains must be invested in a QOF within 180 days of the realization- typically, the date of sale of the asset. The QOF may not simply purchase and hold the QOZ property or asset but must make substantial improvements to that property.

1. Deferral of gain. The taxpayer investing in a QOF will be able to take advantage of deferral of capital gains taxes invested until the sooner of December 31, 2026 or when the investor leaves the QOF.
2. Partial forgiveness of deferred gain. After holding the funds in the QOF for at least five years, the deferred capital gains will receive a 10% reduction, giving the investor a 10% step up in basis. After 7 years, the deferred gains will receive a 15% reduction, allowing for a 15% step up in basis.
3. Forgiveness of additional gains. If the investor keeps his funds in the QOF for at least ten years, any gains accrued by virtue of the appreciation of the QOF will be completely and permanently tax exempt.



The QOZ program differs from a 1031 exchange in several ways. A 1031 exchange can now only be used with real estate assets – the investor sells investment real estate and trades into replacement investment real estate. With the QOZ program, gain from the sale of any type of asset – real estate, stocks, bonds, etc. - can be placed into a QOF and receive the tax benefits. It is also important to note that the QOZ program requires that the money be placed into the QOF and the QOF then invests in the property. The investor does not invest in the property directly. Because of this, an investor cannot combine a 1031 with a QOZ investment. A QOF is not “like kind” to real estate and would not qualify as replacement property. Similarly, because the QOF is invested in the property rather than the individual, the individual investor cannot 1031 exchange out of a QOZ investment.

Failing/expired 1031 exchanges can be rescued two ways.

1. An amendment of a 1031 exchange into an IRC 453 deferral structure can be done as long as completed within 45/180-day requirements and the Qualified Intermediary allows the amendment which they have no legal basis to refuse by some QIs company policies do not allow. It is recommended to choose QI that will allow the amendment to give the Seller more options.
2. Utilize an QOZ investment. If you have a 1031 exchange expire, you have 180 days from 1031 expiration, your tax date, to roll your gains into one of several QOZ investments across the US.

IRC Section 453 deferral structures are by far the most flexible and can be used in conjunction with QOZ and 1031 exchanges to fit the investors unique circumstances and goals. The individual investor CAN defer tax with IRC Section 453 tax deferral structures to create tax deferred liquidity at close and then invest into a QOF within 180 days for all or part of their liquidity event. This allows full tax deferral, but investor can allocate the amount they want into the QOZ program while other funds can be invested in whatever they want.

Work with Tax Deferral Specialist: As with any tax deferral tool, investors should work with trusted advisors who specialize in tax deferral strategies to determine what vehicle is the best option based on their circumstances. Tax Deferral Services has a team of the nation’s foremost tax deferral experts ready to help conventional sales transactions as well as provides solutions for the most complex transactions. Tax Deferral Services acts in a fiduciary capacity to help fit the best tax deferral option to help the investor pursue their goals on their terms. Please feel free to contact Adam Ausloos at 414.269.2600 or send an email adam@defernow.com for more information or help to solve unique situations.

Comparison of IRC Section 453 Deferral Structures, Opportunity Zone Program and IRC Section 1031 Exchange.



	453 Deferral Structures	Opportunity Zone Program	1031 Exchange
Eligible asset classes	Any Asset Class completely flexible	Any Asset Class held in QOF	Only real property held for investment or business purposes
How much needs to be invested	Flexible, Any amount	Only capital gains, in any amount	All proceeds for full tax deferral
Investment deadline	NONE	180 days	180 days
Where can you invest	Anywhere in the WORLD	Only in QOZ's through a QOF	Anywhere in the U.S.
Is an intermediary required	YES	No	Yes
Tax benefits	Tax can be deferred indefinitely through perpetual Installment notes but each installment note is typically 10-30 years of deferral	Capital gains deferred until December 31, 2026	Tax can be deferred indefinitely through perpetual exchanges but capital gains fully taxable upon the sale of the final replacement property
	Upon death of Seller, heirs Do Not received stepped up basis to the property's market value	OZF investments receive 10% increase in basis after 5 years and 15% after 7 years	Upon death of exchangor, heirs received stepped up basis to the property's market value
		Zero capital gains tax on gains from QOF investment after 10 years	