September 24, 2018

Administrator Neomi Rao
Office of Information and Regulatory Affairs
Office of Management and Budget
725 17th Street NW
Washington, D.C. 20503

Re: US Department of Treasury Proposed Rules Under the Tax Cuts and Jobs Act of 2017 on Capital Gains Invested in Opportunity Zones (RIN: 1545-BP03)

Dear Administrator Rao,

As the Office of Information and Regulatory Affairs "OIRA" conducts its review of US Department of Treasury's proposed rules under the Tax Cuts and Jobs Act of 2017 on Capital Gains Invested in Opportunity Zones (RIN: 1545-BP03), the undersigned state economic development officials write to request that OIRA consider several comments and suggestions relating to the implementation of the Opportunity Zones incentive. These comments and suggestions have arisen via preliminary dialogue with one another. (Of course, we may have more feedback to offer once the regulations are issued.) Our initial input focuses upon the importance of ensuring that the proposed rules address the objectives of the law, including the tax treatment of rolled-over Opportunity Fund capital among Qualified Stock and Partnership Interests and the desire for the incentive to promote both real estate *and* business investments. We also ask that the proposed rules provide clarity on definitions, including the timeline for the 90 percent Qualified Opportunity Zone Property allocation test for new Opportunity Funds as well as the definition of "substantial improvement" of Qualified Opportunity Zone Business Property. This letter details these issues and asks that OIRA carefully consider them when making recommendations to the Department of Treasury as part of the regulatory review process.

The proposed rules should ensure that Opportunity Fund capital that is rolled over among Qualified Opportunity Zone Stock or Partnership Interests is eligible for the tax advantages of the Opportunity Zones incentive.

We are concerned that, under the current interpretation, Opportunity Fund capital that is invested in a Qualified Opportunity Zone Stock or Partnership Interest, subsequently divested from that Qualified Stock or Partnership Interest, and re-invested into a different Qualified Stock or Partnership Interest, would no longer qualify for tax advantages under the incentive. Rules that do not allow for the rollover of Opportunity Fund capital among Qualified Opportunity Zone Businesses could discourage investments in business ventures and entrepreneurship. The average time to exit from a business venture is approximately 6 years, and the median is closer to 5 years, much shorter than the 10-year length of investment required to realize the full benefits of the Opportunity Zones incentive.[1] As the Opportunity Zones incentive has a clear intention to focus on investment in businesses in Qualified Opportunity Zones, we emphasize the importance of the

[1] https://pitchbook.com/news/articles/us-venture-capital-activity-so-far-this-year-in-15-charts

rules being written in such a way that respects the Congressional objectives of the law. Allowing Fund capital to continually invest, divest, and reinvest in Qualified Opportunity Zone Stock and/or Partnership Interests will meet this intent and is permitted under the statute.

The proposed rules should provide for a grace period for new Opportunity Funds before being subjected to the 90 percent Qualified Property allocation test.

The law states that an Opportunity Fund must hold at least 90 percent of its assets in Qualified Opportunity Zone Property "Qualified Property," which is measured as the average holding over two periods: (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." Without clarification from appropriate rules, it is unclear whether an Opportunity Fund conceived on June 1, 2019 would have only 30 days (by June 30, 2019) before the Fund's allocation holdings are measured for the purposes of the 90 percent allocation test. This short timeline can be highly demanding for a newly-formed Opportunity Fund and could delay or discourage the formation of potential Opportunity Funds. We highly recommend that the proposed rules include provisions for a grace period for the 90 percent allocation test for new Opportunity Funds.

The proposed rules should clarify the definition of "Substantial Improvement" of Qualified Opportunity Zone Business Property.

The law states that the definition of "substantial improvement" to Qualified Opportunity Zone Business Property "Qualified Business Property" is met only if "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." We are concerned that it is not clear whether the definition of "substantial improvement" requires that an equity investor in a Qualified Business Property must put additional investment into the development of a property equal to: (A) the value of the initial equity investment, or (B) the overall value of the Qualified Business Property. The latter (B) interpretation would disincentivize many types of investment, such as building rehabilitation or brownfield development (which we believe are included in the original intent of the legislation), by making the standard for "substantial improvement" very high, as it would require significant investment beyond the initial equity stake. Instead, we ask that the proposed rules clarify this definition to be interpreted such that "substantial improvement" requires that the improved basis reflect, for example, a doubling of the equity investment value. As an illustrative example, if an investor purchases a $10,000 equity stake investment in a $100,000 Qualified Business Property, the proposed rules should clarify that "substantial improvement" requires the investor to make additions to basis equivalent to $10,000, not $100,000, within any 30-month period beginning after the date of acquisition. Further, the rules should clarify whether "additions to basis" is equivalent to the direct costs the investor incurs while improving the property, or the increased value the property accrues based on that improvement.

Additionally, for the purposes of understanding sufficient conditions that meet the definition of "substantial improvement" for operating businesses, if such conditions apply, proposed regulations should provide clarity on measuring the basis of these businesses.

We hope OIRA finds our observations and suggestions useful and that it will consider them in the review process of Department of Treasury's proposed rules under the Tax Cuts and Jobs Act of 2017 on Capital Gains Invested in Opportunity Zones. If your Office would like to better understand or clarify our comments, we would gladly welcome the opportunity for an extended discussion. Thank you for your consideration.

Sincerely,

Stefan Pryor
Secretary of Commerce
State of Rhode Island

Q. Val Hale
Executive Director
Utah Governor's Office of Economic Development

Joan Goldstein
Commissioner
Vermont Department of Economic Development

Brian Bonlender
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