IN-DEPTH TAX PLANNING IN 2019
(QBI, CHOICE OF ENTITY AND QOZ FUNDS)

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OVERVIEW FOR TODAY

- Discuss QBI Planning
  - Address revised regulations
  - Practical planning for QBI including cash balance plans
- Choice of Entity
  - Comparison of tax in different entities
- Qualified Opportunity Zones
  - Qualifications and practical issues
QUALIFIED BUSINESS INCOME DEDUCTION
Qualified Business Income is all domestic business income other than:

- Guaranteed Payments
- Reasonable compensation paid to the taxpayer for owners of an S corporation
- Investment income (dividends - other than REIT and Co-op), investment interest, STCG, LTCG, commodities, foreign currency, bitcoin, etc.
QBI – PLANNING AFTER THE FIRST YEAR – OVERVIEW

▸ QBI available to:
  ▶ Sole proprietorships
  ▶ Partnerships
  ▶ S corporations
  ▶ Trusts
  ▶ Estates
QBI – PLANNING AFTER THE FIRST YEAR – OVERVIEW

- Taxpayer may deduct the lesser of
  - 20% of taxable income less net capital gain and REIT and co-op dividends
  - 100% of qualified business income
  - Or the greater of (i) 50% of allocable share of qualified wages or (ii) 25% of allocable share of qualified wages plus 2.5% of the UBIAQP
- 20% deduction also allowed for
  - Qualified REIT dividends
  - Qualified publicly traded partnership income
  - Qualified cooperative dividends
**QBI - PLANNING AFTER THE FIRST YEAR - OVERVIEW**

- QBI determined based on **taxable income**

- Which means we can deduct

<table>
<thead>
<tr>
<th>Educator Expenses</th>
<th>HSA contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retirement contributions</td>
<td>Alimony</td>
</tr>
<tr>
<td><strong>Deductible part of self employment tax</strong></td>
<td></td>
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<tr>
<td>Itemized deductions or standard deduction</td>
<td></td>
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</tbody>
</table>
What do we focus on with our tax planning?

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Deductible part of self employment tax

Itemized deductions or standard deduction
QBI – PLANNING AFTER THE FIRST YEAR – OVERVIEW

- Specified Service Trade or Business have a limitation
  - Health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal assets of such trade or business is the reputation or skill of one or more of its employees.
  - Services that consist of investing and investment management, trading, or dealing in securities, partnership interests or commodities.
QBI - PLANNING AFTER THE FIRST YEAR - OVERVIEW

- Specified Service Trade or Business have a limitation
  - The limitation for SSTBs does not apply unless the taxable income exceeds the threshold amounts:
    - $157,500
    - $315,000 married filing jointly
    - Phase out for MFJ over next $100,000 and next $50,000 for all other filing statuses.
EXAMPLE 1 – QBI PLANNING

▸ CPA, married filing jointly with QBI of $325,000 (sole prop)

▸ Taxable income of $315,000

▸ No capital gains

▸ Deduction is the lesser of 20% QBI or 100% taxable income

▸ 20% of QBI = $63,000

▸ Value of deduction - 24% of $63,000 or $15,120 in tax

▸ Note - if single, and income is 1/2, then tax benefit is $7,560
EXAMPLE 2 - QBI PLANNING - S CORP

- CPA, married filing jointly with business income of $325,000. In an S corp, so has to take reasonable compensation of $200,000.

- QBI now limited to $125,000

- Deduction is the lesser of 20% QBI or 100% taxable income
  
  - 20% of QBI = $25,000 or $6,000 in tax (assuming 24%)
  
  - QBI benefit if a sole proprietor? $15,120 in tax
EXAMPLE 3 – QBI PLANNING – PARTNERSHIP

- CPA, married filing jointly win a partnership. CPA is paid based on production primarily, so receives guaranteed payments of $300,000 plus $25,000 of flow-through income

- QBI now limited to $25,000

- Deduction is the lesser of 20% QBI or 100% taxable income
  - 20% of QBI = $5,000 or $1,200 in tax (assuming 24%)
  - QBI benefit if a sole proprietor or no GP? $15,120 in tax
QBI PLANNING IN 2019 – PLANNING OPTIONS

- Cash method taxpayers deferring income to next year
- Consider accelerating income if over the threshold
- Retirement contributions
- Health savings accounts
- Purchase of needed business equipment
- Bunching itemized deduction (directed giving acct)
QBI PLANNING IN 2019 - PLANNING OPTIONS

- Partnership Planning Options
- Restructuring Compensation to avoid guaranteed payments
  - What is the definition of guaranteed payments?
  - Old law vs new law
- Risk of loss
QBI PLANNING IN 2019 – PLANNING OPTIONS

- S corporations
  - How do we restructure to benefit from the QBI?
  - Must pay reasonable compensation, no way to avoid
- Best options?
- Related entities?
S CORPORATION EXAMPLE
IRS Issues Final 199A Regs on 1/18/2019

Extensive and not exactly taxpayer friendly

- 1.199A-1 - Covers calculation of 199A, definitions, loss carryover rules and trade or business requirement.

- 1.199A-2 - W-2 wages rules and unadjusted basis immediately after acquisition rules

- 1.199A-3 - QBI, REIT dividends and PTP income

- 1.199A-4 - aggregation of non-SSTB and SSTB

- 1.199A-5 - definitional guidance on SSTB

- 1.199A-6 - computational guidance on beneficiaries of RPE, PTP and trusts and estates
Final QBI Regulations address 3 ways that a taxpayer can ensure that rental real estate qualifies for the QBI deduction:

- Qualifies as a Section 162 trade or business
- Rents to specific related parties
- Satisfies the safe harbor
Case law for trade or business discusses profit motive and requires considerable, regular and continuous activity.

Regulations look at several factors, including:

- Type of property rented (commercial vs residential)
- Number of properties rented
- Owner’s (or agent’s) day to day involvement
- Any ancillary services provided under the lease
- Terms of the lease (tripe net, etc)
RENTAL REAL ESTATE AND QBI DEDUCTION – RELATED PERSON

▸ Final QBI Regulations address related person leases
  ▶ Deemed a trade or business if rented to a related person
  ▶ Must be rented to individual or entity that is commonly controlled (50% and not C corp)
  ▶ Related to SSTB cannot aggregate
Final QBI Regulations provide safe harbor

- Separate books and records can be kept
- Prior to January 1, 2023, at least 250 of services must be performed each year by owners, employees, agents or independent contractors
- Must keep contemporaneous records of services performed
- Triple net leases are not eligible under the safe harbor
- Cannot use a personal residence as defined in 280A
- Signed statement (penalties of perjury) that safe harbor has been satisfied
DE-MINIMIS RULES

- If a trade or business has gross receipts of $25 million or less or a taxable year, the business will NOT be treated as an SSTB if less than 10% of the gross receipts are attributable to the performance of SSTB services.

- Any services treated as incidental are included in the gross receipts the SSTB for purposes of the 10% test.

- If the trade or business has gross receipts of more than $25 million, the applicable percentage is 5%.
DISQUALIFYING BUSINESSES

▸ An SSTB will include a trade or business that provides 80% or more of its property or services to an SSTB if there is 50% or more common ownership.

▸ If trade or business provides less than 80% of property or services to an SSTB with common ownership, the portion of business property providing property or services to the SSTB is treated as part of the SSTB.

▸ An incidental qualified trade or business is treated as part of an SSTB with common ownership if gross receipts of non-SSTB represents 5% or less of the total combined gross income.
AGGREGATING TRADES OR BUSINESSES

- Proposed Regs allow (but only mandate in certain circumstances) the aggregation of multiple QTBs owned directly by individuals and/or the individual’s share of QBI, W-2 wages and UBIA of qualified property from trade or business operated through Relevant Pass-through Entities ("RPE")

- RPEs themselves cannot aggregate, just the owners
AGGREGATING TRADES OR BUSINESSES – 2

Four Factors to Aggregate

1) same person, or group of persons, must directly or indirectly, own 50% or more of each trade or business to be aggregated are included in income

2) all the items attributable to each trade or business to be aggregated must be reported on returns within the same taxable year, not considering short taxable years

3) None of the aggregated trades or businesses may be an SSTB
AGGREGATING TRADES OR BUSINESSES – 3

Four Factors to Aggregate

4) two out of three of the following factors demonstrate that the businesses are in fact part of a larger, integrated trade or business MUST exist:

- The trades or businesses provide products and services that are the same or customarily offered together;

- The trades or businesses share facilities or share significant centralized business elements, such as personnel, accounting, legal, manufacturing, purchasing, human resources or IT services;

- The trades or businesses are operated in coordination with, reliance upon, one or more of the businesses in the aggregated group (for example, supply chain interdependence).
AGGREGATING TRADES OR BUSINESSES – 4

▸ Additional Operational Rules

▸ If an individual chooses to aggregate, it must combine the QBI, W-2 wages, and UBIA of qualified property for all aggregated trades or business for purposes of applying the wages and property limitations

▸ Owners of RPE do not have to aggregate in the same manner - it’s an owner by owner assumption/calculation

▸ Once aggregated, must consistently report aggregated trades or businesses in all subsequent tax years, but can add a new business. And a change in facts can cause disaggregation
Additional Operational Rules

- If aggregation is chosen, must attach statement to return with required information from the IRS

- IRS can disaggregate for failure to provide information.
CASH BALANCE PLANS
PLANNING FOR QBI WITH CASH BALANCE PLANS

- Cash balance plan is a form of a defined benefit plan
- Popularity started around 2008
- The plans have been growing in popularity since 2012
- CBP pairs with a 401(k) profit sharing plan
- Requires a gateway minimum around 8% (including contributions to DC plan)
- Requires a 4-5% growth rate
- Contribution is not discretionary
- Has to be in place 3-5 years
PLANNING FOR QBI WITH CASH BALANCE PLANS

- CBP has increased contribution limits
  - Age 35 - $66,000
  - Age 40 - $87,000
  - Age 45 - $113,000
  - Age 50 - $148,000
  - Age 55 - $194,000
  - Age 60 - $254,000
EXAMPLE - PLANNING FOR QBI WITH CASH BALANCE PLANS

- Partnership with 2 married partners having combined K-1 compensation of $630,000
- Combined DC contributions of approximately $100,000
- Other deductions of approximately $50,000
- Taxable income is approximately $480,000 and is ineligible for the QBI deduction (for multiple reasons)
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## Example - Planning for QBI with Cash Balance Plans

- **Employee #1** age 71
- **Employee #2** age 38
- **Employee #3** age 38
- **Employee #4** age 70

<table>
<thead>
<tr>
<th>Name</th>
<th>K-1 Comp</th>
<th>401(k)</th>
<th>Match</th>
<th>Non Elect Safe Harbor</th>
<th>Profit Sharing</th>
<th>Cash Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employee #1</td>
<td>630,000</td>
<td>24,500</td>
<td>11,000</td>
<td>8,250</td>
<td>0</td>
<td>220,000</td>
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<tr>
<td>Employee #2</td>
<td>315,000</td>
<td>18,500</td>
<td>5,920</td>
<td>4,440</td>
<td>26,140</td>
<td>81,000</td>
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<tr>
<td>Employee #3</td>
<td>315,000</td>
<td>18,500</td>
<td>5,920</td>
<td>4,440</td>
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<td>81,000</td>
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<tr>
<td>Employee #4</td>
<td>59,000</td>
<td>21,300</td>
<td>2,360</td>
<td>1,770</td>
<td>19,104</td>
<td>500</td>
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</tbody>
</table>
EXAMPLE - PLANNING FOR QBI WITH CASH BALANCE PLANS

- Addition of CBP
  - Total contributions for partners - $535,750
  - Total cost for employees - $23,734
  - Efficiency - 96%
  - Tax savings at 35% (for illustration purposes)
    - Approximately $196,000
EXAMPLE – PLANNING FOR QBI WITH CASH BALANCE PLANS

Now, consider partners 2 and 3 with $630,000 combined income (with changes so income is not guaranteed payments)

- $630,000 of income
- $272,000 of DC and DB contributions
- $50,000 of other deductions

Equals $308,000, with a QBI deduction of $61,600 and tax savings of $14,640 at a 24% bracket.
# Choice of Entity in 2019

<table>
<thead>
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<th></th>
<th>C Corp</th>
<th>S Corp</th>
<th>Sole Prop/Pship</th>
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</thead>
<tbody>
<tr>
<td>Income</td>
<td>$100</td>
<td>$100</td>
<td>$100</td>
</tr>
<tr>
<td>Initial tax</td>
<td>$21</td>
<td>$18</td>
<td>$37</td>
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<tr>
<td>Net to owner</td>
<td>$32</td>
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<td>$63</td>
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<tr>
<td>Net to corp</td>
<td>$79</td>
<td>$50</td>
<td></td>
</tr>
<tr>
<td>Dividend</td>
<td>$79</td>
<td>$50</td>
<td></td>
</tr>
<tr>
<td>Shareholder tax</td>
<td>-$19</td>
<td>$12</td>
<td></td>
</tr>
<tr>
<td>Net Shareholder</td>
<td>$60</td>
<td>$38</td>
<td></td>
</tr>
<tr>
<td>Plus QBI</td>
<td>$70</td>
<td>$70</td>
<td></td>
</tr>
</tbody>
</table>

**What did I not include (hint - S Corp is wrong)**
QUALIFIED OPPORTUNITY ZONE FUNDS
OVERVIEW

▸ Background

▸ Definitions

▸ Benefits

▸ Examples

▸ Penalties

▸ Fund Certification
As part of the recently enacted Tax Cuts and Jobs Act, new Code section 1400Z-2 provides for the temporary deferral of tax on capital gains that are reinvested in a "qualified opportunity fund," the potential to receive partial exclusion on such gain if held for a minimal amount of time and the permanent exclusion from tax of the gains from the sale or exchange of an investment held for at least 10 years in a qualified opportunity fund.
BENEFITS
DEFERRAL OF GAIN

- By election, a taxpayer can elect to have the gain from the sale or exchange of property excluded from gross income to the extent that the gain is invested in a Fund within 180 days from the date of the sale or exchange.

- The election cannot be made for any sale or exchange after December 31, 2026.

- The gain that is invested in a Fund is deferred until the investment in the Fund is sold or until December 31, 2026, whichever is earlier, I.R.C. 1400z-2(b)(1).

- Observation the benefit of the statue lessens as the date of investment gets closer to the end of 2026.

- Investors will likely not be able to get same benefits for the investment of non-capital gain funds in a Fund.
DECLINING BENEFIT OF INVESTING IN FUND
STEPPED UP BASIS

- If a taxpayer holds an investment in a Fund for at least 5 years, the basis of the gain is increased by 10% of the original amount of gain deferred

- If the investment in a Fund is held for at least 7 years, the basis of the gain is increased by an additional 5% of the original amount of gain differed

- Investors can get up to 15% reduction in capital gains tax for investments held more than 7 years
By election, gains from the sale or exchange of an investment in a Fund are permanently excluded from tax if the investment in the fund is held for at least 10+ years, so long as the investment in the fund is sold or exchanged in an arm's length transaction.

The mechanism for the exclusion from tax is the step up basis of the investment to its fair market value upon disposition.

Thus a sale of the investment to an affiliate may qualify for the exclusion so long as the sale price of the investment is consistent with the price that would be paid by an independent third party.
The legislative history makes it clear that taxpayers can continue to recognize losses associated with investments in Funds.
DEFINITIONS
QUALIFIED OPPORTUNITY ZONE

- Low income census track or a census tract contiguous with a low income census tract that has been nominated by the chief executive of a state or possession and certified by the Treasury Department
  - All tracts have been certified by Treasury
  - Nationwide tracts
  - Taxpayer does not have to be located in a tract to invest in one

- The designated Opportunity Zones are available here:
  - [https://www.cdfifund.gov/Documents/Designated%20QOZs.4.18.18.xlsx](https://www.cdfifund.gov/Documents/Designated%20QOZs.4.18.18.xlsx)
QUALIFIED OPPORTUNITY ZONE
QUALIFIED OPPORTUNITY FUND - DEFINED

- Corporation or partnership (can be structured as an LLC):
  - Organized for the purposes of investing in "qualified opportunity zone property"
    - As simple as establishing a new entity with a dedicated bank account
    - Need formal partnership/LLC operating agreement or shareholder agreement
  - Capital gains must be placed in Qualified Opportunity Zone within 180 days of realization
    - Gains must be deposited in Fund account, or at least a binding commitment to transfer cash is made
  - General Rule - Fund must be hold at least 90% of its assets in qualified opportunity zone property, measured twice (once 6 months into the taxable year, and once at the end of the taxable year), meaning default rule is that capital proceeds must be invested within 6 months
    - Proposed regulations provide some flexibility here
QUALIFIED OPPORTUNITY FUND — CAPITAL GAINS

- Proposed Regulations allow to defer any income that is treated as capital gain for federal income tax purposes, whether short term or long term capital gain
- Includes Section 1231 gain
- The capital gains must have occurred as a result of a sale to an unrelated party (as defined under Section 267 and 707 with the threshold percentage reduced to 20%)
- Under the Proposed Regulations, partnership can make an election to defer capital gain and the partnership itself can contribute the gains to a Fund
- Partners of a partnership receiving capital gains can treat rollover that capital gain into a fund if they invest within 180 days after the last day of the partnership’s tax year
Observations

- The 90% testing places time pressure on investments, but are reduced by the provisions of the Proposed Regulations

- IRS recently issued guidance on Funds in the form of Proposed Regulations

- Observation: Since the 90% test is done six months into and at the end of the Fund's taxable year, Fund established on December 1 may have to deploy 90% of its cash by December 31 unless I fall under the provisions of the Proposed Regulations
QUALIFIED OPPORTUNITY ZONE PROPERTY

- Stock acquired by a Fund after December 21, 2017 (for cash) at its original issue in a corporation that is qualified opportunity zone business

- A partnership interest acquired by a Fund after December 31, 2017 (for cash) in a partnership that is qualified opportunity zone business

- Tangible property used in a trade or business of the Fund if the property was acquired after December 31, 2017 and the original use of the property in the qualified opportunity zone commences with the Fund or if the fund substantially improves the property.
QUALIFIED OPPORTUNITY ZONE BUSINESS

- A trade or business in which substantially all (defined as 70%) tangible property owned or leased by the business was acquired by purchase after December 31, 2017.

- The original use of the property commences with the business or the business substantially improves the property.

- Substantially all of the use of the property is in a qualified opportunity zone.

- At least 50% of the total gross income of the business must be derived from the active conduct of the business.
QUALIFIED OPPORTUNITY ZONE BUSINESS

► A substantial portion of the intangible property of the business must be used in the active conduct of the business

► Less than 5% of the average of the aggregate adjusted bases of the property of the business can be attributable to certain financial property (debt stock, partnership interests, options, future contracts, forward contracts, warrants, national principal contracts, annuities, and other similar properties)

  ► The financial property does not include working capital held in cash, cash equivalents, or debt instruments with at term of 18 months or less or accounts receivable

► The property cannot be certain excluded property (golf courses, country clubs, massage parlors, hot tub facilities, tanning facilities, racetracks, gambling facilities or liquor stores)

► The phrase "substantially all" is not defined in the statute and is only defined for limited purposes in the Proposed Regulations
QUALIFIED OPPORTUNITY ZONE BUSINESS

- Proposed Regulations provide that working capital (defined as being held in cash, cash equivalents or debt instruments with a term of 18 months or less) can qualify as being used in a qualified opportunity zone business if it:
  - Has a written plan that identifies the working capital as property held for the acquisition, construction or substantial improvement of property in the opportunity zone;
  - There is a written schedule to deploy the working capital within 31 months; and
  - The business substantially complies with the schedule.

- Something to keep in mind - the test in the statute is that substantially all of the “tangible property” is QOZ business property. The Fund has a 90% test, but the QOZ business tests on the tangible property. The working capital rule above allows the QOZ business to keep funds on hand and still qualify as a QOZ business.
OPPORTUNITY ZONE INVESTMENTS

▸ Investors cannot create own gain by selling property to related party
  ▶ But investors can maintain up to a 20% interest

▸ Substantial improvement means doubling your investment
  ▶ 30 month measuring period does not commence on Day 1

▸ Ability to structure investments is fairly open ended
  ▶ GP and LP Opportunity Funds/ AIVs
  ▶ Proposed Regulations provide that LLCs also qualify - but you may not want to use that option

▸ One Fund/one property structure provides most flexibility and administrative ease
OPPORTUNITY ZONE INVESTMENTS

- Opportunity Fund deals and be used with tax credits such as LIHTC, energy, or historic

- There are open questions, and Proposed Regulations did not address all of them
DISPOSITION OF INVESTMENT

- The statute and the Proposed Regulations provide that an investor must sell the Fund interest and not the underlying property in order to get the tax benefits.

- May want to setup individual funds per investor to really provide for the flexibility of each individual investor, and have the QOZ business contain the restrictions of the different investors.

- There may be work arounds, but the Proposed Regulations do not allow the sale of the underlying assets to reflect reality of marketplace
PENALTIES
There is a penalty if the Fund fails to maintain the requirement that the Fund hold at least 90% of its assets in qualified opportunity zone property.

However, the reference in the statute of the 90% requirement is incorrect as it states, "the 90-percent requirement of subsection (c)(1)" when the 90% requirement appears in subsection (d)(1). Without a technical correction, it is unclear if the penalty can be imposed by the IRS.

The penalty is the excess of the amount equal to 90% of the Fund's assets over the aggregate amount of qualified opportunity zone property held by the Fund, multiplies by the federal underpayment rate for the month.

For Funds that are partnerships, the penalty is taken into account as part of the distributive share of each partner of the partnership.
FUND CERTIFICATION
FUND CERTIFICATION

- Proposed Regulations state that the Form 8996, Qualified Opportunity Fund, would be used for initial certification and annual reporting of compliance with the 90% test.

- Form 8996 would be attached to the taxpayer’s filed tax return for the given year.

- This Form 8996 essentially allows a taxpayer to "self-certify" and does not have to go through a prior certification process to qualify the Fund.

- Form 8996 is online and visible for viewing.
FUND CERTIFICATION

New Markets Tax Credit Procedures

The legislative history suggests that the Community Development Financial Institutions Fund ("CDFI Fund") will be responsible for the certification of qualified opportunity funds. However, guidance from the CDFI Fund indicates that it is supporting the IRS only with the opportunity zone nomination and designation process and not with the certification of qualified opportunity funds.

Based on the Legislative history, self-certification may not be permanent.
ADDITIONAL QUESTIONS/ANSWERS

▸ Can the fund use debt?
  ▶ Yes, the Proposed Regulations provide that a fund utilizing debt will not disqualify the fund

▸ What about as preferred equity?
  ▶ Proposed Regulations allowed preferred equity and preferred distributions

▸ Is there an argument that non-capital gain funds invested in a fund can be eligible for the deferral and/or exclusion?
  ▶ No, Proposed Regulations state that only capital gains are eligible for the deferral and/or exclusion

▸ Due to drafting errors in the statute, can the penalties be enforced?

▸ Is there a limitation or prohibition on related party transactions?
EXAMPLES AND APPLICATIONS
INVESTMENT IN FUND IS HELD FOR AT LEAST 10 YEARS

▸ Assume a taxpayer has $100 in gain from the sale of stock on June 1, 2018. Within 180 days from the date of the sale of the stock, the taxpayer invests the $100 gain in a Fund, and makes the appropriate election. The $100 gain is not subject to tax in 2018 (the year of the sale of stock) and is deferred until the investment in the Fund is sold, or December 31, 2026, whichever is earlier.

▸ Further, assume that the taxpayer holds the investment in the Fund for 10 years. The basis in the deferred $100 gain is increased by 15%, which reduces the taxable gain by $15, making only $85 for the gain subject to tax. Since the investment in the Fund was held for 10 years, (i.e. at least 7 years), the $85 gain is taxed in 2026.

▸ Additionally, assume that the taxpayer sells his investment in the Fund in 2029 (at least ten years after the original investment in the Fund), for $200, the fair market value of the investment, and makes the appropriate election. Since the basis of the investment in the fund equals the fair market value of the investment on the date of the sale, no tax is paid on the $100 of appreciation of the investment over the taxpayer's 11 year holding period.
The Tax effect of holding the investment in the fund for at least 10 years, compared to an ordinary investment, is as follows:

<table>
<thead>
<tr>
<th>At Least 10 Year Holding Period</th>
<th>Ordinary Investment</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred Gain (taxed in 2026)</td>
<td>$100.00</td>
<td></td>
</tr>
<tr>
<td>Basis Step-Up</td>
<td>$15.00</td>
<td>$0.00</td>
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<tr>
<td><strong>Taxable Gain</strong></td>
<td><strong>$85.00</strong></td>
<td><strong>$100.00</strong></td>
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<tr>
<td>Tax (at 23.8%)</td>
<td>$20.23</td>
<td>$23.80</td>
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<tr>
<td><strong>Tax (at 23.8%)</strong></td>
<td><strong>$20.23</strong></td>
<td><strong>$3.57</strong></td>
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<tr>
<td>Gain on Investment</td>
<td>$100.00</td>
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</tr>
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<td>Basis Step-Up</td>
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<tr>
<td><strong>Tax (at 23.8%)</strong></td>
<td><strong>$0.00</strong></td>
<td><strong>$23.80</strong></td>
</tr>
<tr>
<td><strong>Tax (at 23.8%)</strong></td>
<td><strong>$0.00</strong></td>
<td><strong>$23.80</strong></td>
</tr>
</tbody>
</table>

As a result of holding an investment in a Fund for 10 years, and making the proper elections, a taxpayer would save $27.37 in tax, and would get the benefit of the deferral of tax on the gain that is invested in the fund until 2026.
INVESTMENT IN FUND IS HELD FOR AT LEAST 7 YEARS

▶ Assume a taxpayer has $100 in gain from the sale of stock on June 1, 2018. Within 180 days from the date of the sale of the stock, the taxpayer invests the $100 gain in a fund, and makes the appropriate election. The $100 gain is not subject to tax in 2018 (the year if the sale of stock) and is deferred until the investment in the fund is sold, or December 31, 2026 whichever is earlier.

▶ Further, assume that the taxpayer holds the investment in the Fund for 7 years. The basis in the deferred $100 gain is increased by 15%, which reduces the taxable gain by $15, making only $85 of the gain subject to tax. Since the investment in the Fund is held for 7 years, the $85 gain is taxed in 2025.
INVESTMENT IN FUND IS HELD FOR AT LEAST 7 YEARS

The tax effect of holding the investment in the Fund for 7 years, compared to an ordinary investment, is as follows:

<table>
<thead>
<tr>
<th>At Least 7 Year Holding Period</th>
<th>Ordinary Investment</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred Gain (taxed in 2025)</td>
<td>$100.00</td>
<td></td>
</tr>
<tr>
<td>Basis Step-Up</td>
<td>$15.00</td>
<td></td>
</tr>
<tr>
<td>Taxable Gain</td>
<td>$85.00</td>
<td></td>
</tr>
<tr>
<td>Tx (at 23.8%)</td>
<td>$20.23</td>
<td></td>
</tr>
<tr>
<td>Gain (taxed in 2018)</td>
<td>$100.00</td>
<td></td>
</tr>
<tr>
<td>Basis Step-Up</td>
<td>$0.00</td>
<td></td>
</tr>
<tr>
<td>Taxable Gain</td>
<td>$100.00</td>
<td></td>
</tr>
<tr>
<td>Tax (at 23.8%)</td>
<td>$23.80</td>
<td>$3.57</td>
</tr>
</tbody>
</table>

As a result of holding an investment in a fund for 7 years, and making the proper election, a taxpayer would save $3.57 in tax, and would get the benefit of the deferral of tax on the gain that is invested in the Fund until 2025.
INVESTMENT IN FUND IS HELD FOR AT LEAST 5 YEARS

Assume a taxpayer has $100 in gain from the sale of stock on June 1, 2018. Within 180 days from the date of the sale of the stock, the taxpayer invests the $100 gain in a Fund, and makes the appropriate election. The $100 gain is not subject to tax in 2018 (the year of the sale of stock) and is deferred until the investment in the Fund is sold, or December 31, 2026, whichever is earlier.

Further, assume that the taxpayer holds the investment in the Fund for 5 years. The basis in the deferred $100 gain is increased by 10% which reduces the taxable gain by $10, making only $90 of the gain subject to tax. Since the investment in the Fund was held for 5 years, the $90 of gain is taxed in 2023.
INVESTMENT IN FUND IS HELD FOR AT LEAST 5 YEARS

The tax effect of holding the investment in the Fund for 5 years, compared to an ordinary investment, is as follows:

<table>
<thead>
<tr>
<th>At Least 5 Year Holding Period</th>
<th>Ordinary Investment</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred Gain (taxed in 2025)</td>
<td>$100.00</td>
<td>$100.00</td>
</tr>
<tr>
<td>Basis Step-Up</td>
<td>$15.00</td>
<td>$0.00</td>
</tr>
<tr>
<td>Taxable Gain</td>
<td>$90.00</td>
<td>$100.00</td>
</tr>
<tr>
<td>Tx (at 23.8%)</td>
<td>$21.42</td>
<td>$23.80</td>
</tr>
</tbody>
</table>

As a result of holding an investment in a Fund for 5 years, and making the proper election, a taxpayer would save $2.38 in tax, and would get the benefit of the deferral of tax on the gain that is invested in the Fund until 2023.
SELF-FUNDED FUND

- Entity owns low basis building with large potential capital gain on sale

<table>
<thead>
<tr>
<th>Sale of Building</th>
<th>Investment of Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building FMW</td>
<td>Building FMW</td>
</tr>
<tr>
<td>$500.00</td>
<td>$500.00</td>
</tr>
<tr>
<td>Basis</td>
<td>Basis</td>
</tr>
<tr>
<td>$10.00</td>
<td>$10.00</td>
</tr>
<tr>
<td>Capital Gain in 2018</td>
<td>Capital Gain Deferred in 2018</td>
</tr>
<tr>
<td>$490.00</td>
<td>$490.00</td>
</tr>
<tr>
<td>Tax (at 23.8) in 2018</td>
<td>Tax (at 23.8) in 2018</td>
</tr>
<tr>
<td>$116.62</td>
<td>$0.00</td>
</tr>
<tr>
<td>Remaining Funds</td>
<td>Remaining Funds</td>
</tr>
<tr>
<td>$383.38</td>
<td>$500.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>New Purchase</th>
<th>New Purchase through Fund Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Available Funds</td>
<td>Available Funds</td>
</tr>
<tr>
<td>$383.38</td>
<td>$500.00</td>
</tr>
<tr>
<td>FMW in 2029 (at 5%</td>
<td>FMW in 2029 (at 5%</td>
</tr>
<tr>
<td>Appreciation)</td>
<td>Appreciation)</td>
</tr>
<tr>
<td>$655.71</td>
<td>$855.17</td>
</tr>
<tr>
<td>Capital Gain</td>
<td>Capital Gain</td>
</tr>
<tr>
<td>$272.33</td>
<td>$355.17</td>
</tr>
<tr>
<td>Tax (at 23.8) in 2029</td>
<td>Tax (at 23.8) in 2029</td>
</tr>
<tr>
<td>$64.81</td>
<td>$0</td>
</tr>
<tr>
<td>Remaining Funds</td>
<td>Remaining Funds</td>
</tr>
<tr>
<td>$207.52</td>
<td>$855.17</td>
</tr>
<tr>
<td>Tax in 2026</td>
<td>$99.13</td>
</tr>
</tbody>
</table>

- Building is sold, entity establishes Fund and invests proceeds in new building

| Total Remaining Funds     | $756.04                             |
### MIXED FUND

- Both capital gains and other funds are invested in Fund
- Likely that Fund tax treatment is bifurcated and treated as investment in two separate funds

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Gains</td>
<td>$100.00</td>
</tr>
<tr>
<td>Other Investment</td>
<td>$100.00</td>
</tr>
<tr>
<td>Total Investment</td>
<td>$200.00</td>
</tr>
<tr>
<td>FMW in 2029</td>
<td>$500.00</td>
</tr>
<tr>
<td>Capital Gains</td>
<td>$300.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Tax on Disposition of Investment in 2029</strong></td>
<td></td>
</tr>
<tr>
<td>Capital Gain Investment (No Tax)</td>
<td>$0.00</td>
</tr>
<tr>
<td>Other Investment (150 at 23.8%)</td>
<td>$71.40</td>
</tr>
<tr>
<td>Total Tax</td>
<td>$71.40</td>
</tr>
</tbody>
</table>
"CHURNED" INVESTMENTS

- Fund initially invests in a Qualified Opportunity Zone Property in 2018
- Fund sells investment in 2020, uses proceeds to invest in other Qualified Opportunity Zone Property
- Investor sells interest in Fund in 2029
- Any gain in investment in Fund sold in 2029 is tax free
- Fund or its partners may elect to rollover any gain on sale of Qualified Opportunity Zone Property in 2020
- Funds should be able to "churn" property so long as it meets 90% test every 6 months
  - In other words, Fund must replace Qualified Opportunity Zone Property with Qualified Opportunity Zone Property
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