

OPPORTUNITY ZONE OPPORTUNITIES ABOUND IN NEW JERSEY

By: Matthew J. Schiller and Steven G. Mlenak

The IRS recently released proposed regulations concerning the Opportunity Zone program (OZ Program) created under the Tax Cuts and Jobs Act. The OZ Program encourages development within designated "Opportunity Zones" (OZs) through its various tax incentives. Although numerous outstanding issues remain, it is clear that the OZ Program can benefit developers via direct tax benefits and by creating a new means to raise capital for qualified projects. Accordingly, it is critical for developers to understand the OZ Program and its potential interplay with New Jersey's other incentive programs and laws, including the Local Redevelopment and Housing Law (LHRL) and the Long Term Tax Exemption Law (LTTEL).

Qualified Opportunity Zones in New Jersey

OZs are qualified census tracts with a poverty rate of 20% or a median family income of up to 80% of the median income of the metropolitan area or of the statewide median income. There are 169 census tracts (in 75 municipalities) in New Jersey that have been approved as OZs (the maximum number allowed under the Tax Cuts and Jobs Act). Accordingly, no additional OZs will be created or designated in New Jersey without further action by Congress.

What Are the OZ Program's Tax Benefits?

Investing capital gains in Qualified Opportunity Funds (QOFs) as explained below can result in 3 primary tax benefits:

- An appreciated asset is sold after December 31, 2017.
- The capital gain amount is invested

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into a QOF within 180 days from the date the gain would be recognized.

Tax Benefit: The investor defers payment of taxes due for the capital gain amount invested into a QOF.

- Upon the earlier of either the sale of its QOF interest, or December 31, 2026, taxes will be due for the deferred capital gain.
Tax Benefit: 10% of the deferred capital gain will be forgiven if the QOF interest is held for 5 years or more (the capital gain was invested into a QOF prior to December 31, 2021). If the QOF interest is held for 7 years or more (the capital gain is invested in a QOF before December 31, 2019), an additional 5% (15% total) of the deferred capital gain will be forgiven.

- The QOF interest is held for at least 10 years after investment.
Tax Benefit: There will be no tax on the gain realized from its initial QOF investment (i.e., the initial capital gain investment) upon sale.

What Are QOFs?

QOFs are investment vehicles organized as a corporation or partnership (which may be an LLC taxed as a corporation or partnership) for the purpose of investing in qualified opportunity zone property (QOZ Property). At least 90% of a QOF's assets must be invested in QOZ Property or as an equity interest in a qualified opportunity zone business (QOZ Business). Investors may invest in an existing QOF or create a new QOF for its own purposes. QOFs will be self-certified to the IRS and must demonstrate satisfaction of the 90% asset test twice per year.

QOFs can either directly acquire, own and develop/substantially improve property located in an OZ or hold an interest in a QOZ Business. To qualify as a QOZ Business, 70% of the tangible property owned or leased by the business entity must constitute QOZ Property both at the time the QOF acquires its equity interest in the QOZ Business and during substantially all of the period that the QOF holds its QOZ Business interest.

QOZ Property is property: (1) purchased after December 31, 2017; (2) whose "original use" commences upon acquisition or is substantially improved upon acquisition; and (3) that is used/located in an OZ. Notably, if acquiring

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an existing building, the building must be “substantially improved” within 30 months after acquisition (i.e., double the basis of the building), as measured by the additions/improvements made thereto (note: the land need not be “substantially improved”).

Notably, the proposed regulations also provide a “Working Capital Safe Harbor” qualifying cash/financial property as QOZ Property so long as (1) there is a written plan designating the funds for the acquisition, construction or substantial improvement of QOZ Property; (2) there is a written schedule for the planned use of the funds within 31 months; and (3) the funds are actually used in accordance with the schedule.

New Jersey Laws Can Further Assist OZ Developments

As much of New Jersey is already developed, many developers are now focusing on redevelopment opportunities. To help offset costs and risks associated with such redevelopment efforts, New Jersey affords developers with a variety of tools to encourage redevelopment efforts, such as the LHRL and LTTEL.

The LHRL provides protocols and statutory criteria for a property to be designated as an “area in need of redevelopment,” thus permitting the municipality to amend its ordinance and make the proposed use “as of right” onsite. Under the LHRL, a property may qualify as an “area in need of redevelopment” if it is, among other things, “substandard, unsafe, unsanitary, dilapidated, or obsolescent, or possess any of such characteristics, or are so lacking in light, air, or space, as to be conducive to unwholesome living or working conditions” or upon “the discontinuance of the use of buildings previously used for commercial, manufacturing, or industrial purposes.”

Although OZ designations are based

upon income metrics, there will likely be a nexus between an area’s income and the condition and usefulness of many of the properties located therein. Accordingly, developers may seek to utilize the LHRL’s redevelopment designation process to permit the proposed use “as of right”, circumventing the need for use variance relief, and qualify the development for certain economic incentives, such as a payment in lieu of taxes (PILOT) program under the LTTEL, which could substantially reduce the development’s property tax obligations upon completion.

What’s Next?

The IRS is currently receiving public comments on its proposed OZ Program regulations. Moreover, additional regulations are scheduled to be released in early 2019. Notwithstanding that the OZ Program is a “work in progress,” developers should be conscious of the limited number of OZ Properties available for development in New Jersey, as well as the December 31, 2019 deadline to take full advantage of the OZ Program’s tax benefits. Given such, there will likely be significant participation in the OZ Program throughout 2019 and beyond.

Accordingly, developers seeking to participate under the OZ Program should consult with their attorneys and accountants to discuss how they can best take advantage of the OZ Program and other New Jersey laws such as the LHRL and LTTEL, to maximize their development opportunities.

BID PROTESTS ON PUBLIC PROJECTS

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difficult for a disappointed bidder on these projects to protest the award. Generally, the only argument disappointed bidders will have is that the public entity made a mistake in its technical review. But the courts will generally not engage in the type of detailed technical analysis necessary for those arguments, under the theory that to do so would be to second-guess the determination of procurement officials.

Besides making it difficult for disappointed bidders, it is easy for public officials to make subjective determinations in these cases that can result in conscious or unconscious favoritism—something our bidding laws are designed to prevent.

None of this means that contractors should avoid these types of projects. It simply means that when bidding on a project like this, a bidder should fully explain what it is proposing and what it intends to do, and realize that if it is not awarded the project, any attempt to protest the bid will be an uphill battle.

SUPREME COURT DECLINES TO HEAR UNDESIGNATED REDEVELOPER’S APPEAL

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redevelopment costs to developers, control the project timeline, and impose accountability and timelines upon owners and developers in the form of contractual obligations, enforcement and remedies.

Accordingly, in future cases an important distinction that may impact the Court’s analysis is whether a subject property has been designated as a condemnation or non-condemnation redevelopment area under the LRHL. As of now, whether that distinction is enough to sway the Court’s view of redevelopment by a property owner without an official redevelopment designation remains unclear.