

NEWS ANALYSIS

What Will Qualified Opportunity Funds Have to Report?

by Marie Sapirie

Changes to the Opportunity Zone reporting requirements appear to be coming soon, but when Congress will act and what information it will require Treasury to collect is still uncertain. Congress seems to agree that some sort of reporting is desirable.

Immediately after passage of the Tax Cuts and Jobs Act, designing the framework for information collection and reporting was mostly Treasury's domain. Congress gave Treasury broad authority — but opaque directions — to write regulations to implement section 1400Z-2, including certification rules for qualified opportunity funds, and to prevent abuse. But Congress now seems to want to specify the types of information it would like the IRS to collect and report.

While lawmakers mulled over the options, the IRS revised Form 8996, "Qualified Opportunity Fund," which now requires funds to report the names of any investors who disposed of any part of their equity interest in the fund during the QOF's tax year. This will allow the IRS to match dispositions reported by individual investors with dispositions reported by QOFs.

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The revision added a new part for identifying qualified Opportunity Zone tract numbers and qualified Opportunity Zone business property values, as well as a place to list stock and partnership interests. QOFs will also report the investment value of stock or partnership interests in a qualified Opportunity Zone business. The form includes calculations of the six-month and year-end tests for qualified Opportunity Zone property, as well as a line for identifying the accounting method used to value the property. The instructions for the form haven't yet been released.

The form revision is reasonably designed to allow the IRS to trace claimed Opportunity Zone benefits, said Glenn Graff of Applegate & Thorne-Thomsen PC. "I think they asked for what they felt was reasonable to support the amount of the qualified opportunity fund investment and capital gains tax that is deferred, but didn't include things they felt weren't authorized by the statute and go beyond what is required to support the tax benefits," he said.

The revised form will allow the IRS and Treasury to determine how much money went into each census tract and possibly how much total investment or disinvestment occurred in Opportunity Zones over time, but additional reporting would be helpful in evaluating the community impact of the program, Graff said. The revised form doesn't address key metrics regarding community impact, such as details about job creation, changes in unemployment, changes in property values, and affordable housing availability.

Additional Information Reporting

Proposed legislation would give Treasury authority to collect information that would answer some questions about the effect of the Opportunity Zones on local residents. H.R. 2593, introduced in May by House Ways and Means Committee members Ron Kind, D-Wis., and Mike Kelly, R-Pa., would require Treasury to collect and report information on investments held by QOFs, including the number of QOFs; the amount of assets held in QOFs; the composition of QOF investments by asset class; the percentage of qualified Opportunity Zone census tracts that have received QOF investments; and the impacts and outcomes of zone designation in those areas on economic indicators, including job creation, poverty reduction, new business starts, and other metrics.

The bill adds information collection requirements for investments, including the total amount of the investment and its date; the type of investment and the location of the business or real property; the type of activity being supported by the investment; for businesses, the approximate number of full-time employees when the investment was made; and for real property, the approximate total square footage and the number

of residential units. The subsection on information collection about investments doesn't give Treasury carte blanche to include "other metrics" like the subsection on data collection at the national and state levels, but the list of "relevant information" to be collected on each investment appears nonexclusive. A companion bill, S. 1344, was also introduced in May by Senate Finance Committee member Tim Scott, R-S.C., and Sen. Cory A. Booker, D-N.J.

Additional reporting would be helpful in evaluating the community impact of the program, Graff said.

Graff said the bill asks Treasury to collect helpful information, and noted that the mandate to collect information on impacts and outcomes of Opportunity Zone designation allows Treasury to include metrics beyond job creation, poverty reduction, and new business starts. He suggested that it would be useful to distinguish between affordable housing and market-rate housing, such as by looking at net changes in the amount of affordable housing in a tract.

Graff said Congress might want to consider more ways to allow the assessment of the regime in greater detail. Job creation metrics may tell only part of the story when, for example, an existing automotive garage staffed mostly by zone residents is replaced by a law firm that employs primarily out-of-zone residents. It might also be beneficial to know the income levels of the newly created jobs, Graff said. Treasury could include information in its report to Congress about changes in local tax revenues or in property values in the area, which would help clarify the effect of the Opportunity Zone regime, he said.

If the House bill or an iteration of it passes, at least some of its data points will likely appear on a revised Form 8996. For example, there could be lines on the form asking about jobs created, types of investment, the locations of businesses and property, and the type of activity supported by the investment.

Scoping Questions

Congress is under pressure to do something about information collection and reporting. "We are amid a large-scale social experiment on

millions of low-income Americans by highly incentivizing unregulated investments into their communities and prioritizing the appreciation of capital over social impact," Aaron Seybert of the Kresge Foundation explained in his testimony on October 17 before the House Small Business Subcommittee on Economic Growth, Tax, and Capital Access. He said it's concerning that under the existing requirements, Americans will never know where Opportunity Zone capital comes from, where it's being invested, and who benefited from the investment. "Without a mandate to disclosure at both the fund and transaction level, it will be impossible to answer those questions," he said.

Also on October 17, Brett Theodos of the Urban Institute urged lawmakers to implement reforms to ensure that the forgone revenue doesn't subsidize deals that don't need support. "Reforms are needed to avoid providing the lion's share of incentives to the best-off Zones. . . . And reforms are needed if this incentive is to be tracked with proper accountability," he said.

John W. Lettieri of the Economic Innovation Group called the changes to Form 8996 "a really good first step" and a sign that Treasury is doing what it can within its current authority. He added that Congress can and should provide additional direction and authority to Treasury to expand the scope of what information is captured, but that what Congress should do regarding reporting requirements must be grounded in reality. Lettieri said he wanted to ensure that congressional leaders are closely consulting with the IRS so that the information collected and reported doesn't exceed the IRS's natural and appropriate role. "This should not be a contentious issue. Everybody generally agrees on what should happen," he added.

Lettieri said the priority should be to collect granular data without creating a disincentive to invest or compromising the proprietary information of businesses or investors, and that he would like to see a streamlined process for collecting, quantifying, and reporting data. "There are tensions that have to be addressed," he said, but added that they can be dealt with in an open and collaborative process between Treasury and the IRS and lawmakers.

“I think Opportunity Zones should be treated differently” from other community development programs regarding original data collection and reporting on community impacts, Theodos told Congress. “The program’s effects can be sufficiently well observed and understood as long as basic transaction inventory reporting is required — and this information is shared publicly.”

The public sharing is the potentially problematic piece. The information Treasury collects on Form 8996 is subject to the confidentiality requirements of section 6103. But under that provision, Treasury can still disclose data “in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer,” which means that aggregate data could be made available.

Certification?

Despite the occasional lament from lawmakers that a certification process would improve Opportunity Zone transparency, the prospects for one are increasingly dim. Ways and Means Committee member Lloyd Doggett, D-Texas, was the most recent lawmaker to publicly support a certification process as a safeguard to ensure that the local communities in Opportunity Zones benefit from the regime.

However, there’s no pending legislation to give greater direction to Treasury to create a certification process for QOFs than what’s in section 1400Z-2(e)(4)(A), which gives Treasury authority to write rules “as may be necessary or appropriate to carry out the purposes of this section” and “rules for the certification of qualified opportunity funds for the purposes of this section.” That’s probably by design. Although plenty of commentators would like to see a certification process like the one for community development entities in section 45D, and that’s what the TCJA conference report suggested the process should be modeled on, there’s so far merely self-certification by QOFs on Form 8996. Leaving the reference to the new markets tax credit as the model for the certification process in the conference report appears to be a telling oversight.

If Congress wanted Treasury to set up a certification process like the one in the new

markets tax credit, it should have been clear about that in the statutory text. A similar certification process might not be desirable or consistent with the Opportunity Zone regime, which was clearly designed to be different from the new markets regime. But that doesn’t mean Congress and possibly also Treasury shouldn’t include mechanisms to ensure that the Opportunity Zone benefits flow primarily to the existing residents in the neediest geographical areas, or to ensure some degree of community input into projects.

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Lettieri noted the tension between ensuring that broad participation in Opportunity Zones is possible and that bad actors are screened out. He pointed to the Economic Innovation Group’s recommendations that would provide some screening of QOF managers to enhance the program’s integrity and provide basic antiabuse safeguards, but distinguished the Opportunity Zone regime from the new markets tax credit. “The [new markets tax credit] is distributing something; OZ is not,” he said. Because the Opportunity Zone program was designed to be different and to require investors to put their own capital at risk, a different approach to preventing abuse is appropriate, he said.

Congress left Treasury and the IRS in an untenable position, caught between the statutory language and the ambiguous conference report. Lawmakers must act if they want more information collection than the IRS has proposed through Form 8996. Given the dual, and sometimes competing, purposes of encouraging investments in economically distressed areas and providing deferral for making those investments, Congress should spell out what it wants to know about the effects of the Opportunity Zone regime, while keeping in mind that overly onerous reporting requirements may discourage investments. ■