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# The Wizard of OZ (that's "Opportunity Zones"): Kowalski on What's Next From Treasury, Part 1 of 2 by Flanigan

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Daniel Kowalski on What's Next From Treasury, Part 1 of 2

New York City, Connect Opportunity Zone Conference, Harvard Club, October 22nd: As December 31st (a mini-"D-Day") approaches for the OZ program, (very "mini" in the opinion of many) and the U.S. Treasury Department works on the final OZ regulations, I had the opportunity to interview–and the audience at the Connect Opportunity Zones Conference had the opportunity to hear–Daniel Kowalski address some important questions still unresolved about the OZ program.

Kowalski has given himself to public service for 30 years, mostly around tax policy in some form, serving at every governmental level, starting many years ago in the NYC Audit Dept., with later stints in the New York Assembly and even in that remote secondary (tertiary?) market known as the State of Missouri (test: what's the capital city?—answer is at the end of this article). He has risen to the national level now as counselor to the U.S. secretary of the Treasury. In that role he is specifically designated as the connector between the White House and the Treasury on OZ issues. And in that role he has served as the Administration's delegate to the benighted masses craving all the OZ insight and wisdom we can get.

Of course he was circumspect, taking care not to jump the gun on the ongoing Treasury process of drafting the final OZ program regulations, but he did provide some hints and insights, and a fairly definite answer to a couple of questions, including my opening one: When will the final regulations be issued? Answer: This listener thinks he heard a definite "before December 31st" and maybe as early as shortly after Thanksgiving, Kowalski specifically acknowledging that investors and their advisors deserved whatever enlightenment the Treasury is able to give before some important and irrevocable decisions have to be made by year-end. (Note that he mentioned in passing that the final regulations, which will likely include the two interim installments already delivered, may exceed 500 pages!)

My next question addressed one of the most important remaining troublesome issues identified by many commentators. As we know, the most common way to sell a business is to sell assets rather than equity interests. However, under the existing proposed regulations, in order for the investor to obtain that all-important tax-exclusion benefit at the end of 10 years, there must be a sale of the equity interest in the OZ business by the OZ fund or a sale of the equity interest in the OZ fund by the OZ investor. I interpreted Kowalski's careful and nuanced answer to indicate that Treasury is friendly to inclusion of an asset-sale alternative.

Another problem is the language of the interim regulations that requires any IRC Section 1231 gain1 qualifying for investment in an OZ fund to be invested by June 27th of each year, causing an investment "blackout" for the last six months of every year. Again, Kowalski's statement indicated to me that relief almost certainly seems to be coming on this issue.

Another lament has been the impending December 31st, 2019 deadline to make an investment in order to obtain the 5% reduction in taxable gain granted by the OZ statute. This is the "mini-D-Day" referred to above. The lament is that this is just too soon for investors to get ready, and for sponsors to have projects ready, for investment, especially since it allegedly took so long for Treasury to issue clarifying regulations in October 2018 and April 2019. The "ask" is for an extension of that deadline to December 31st, 2020. But Kowalski was emphatic that Treasury could not help on that one. Paraphrasing him, that requirement is in the statute, and Treasury has no authority to contradict the specific Congressional language. He did note that there was a move afoot in Congress to legislate that extension, but we can all be permitted to doubt that such a tiny boat could be successfully floated in the maelstrom of the current political typhoon.

There will be more on the Kowalski interview in Part 2, my next article, covering subjects important not just to real estate players but even more to startups and other operating businesses, including:

1) Problems with the required asset-by-asset method of complying with the substantial improvement test;

2) The requirement that 70% of the tangible property of the OZ business must be, “used in the zone 90% of the time;” and

3) Difficulties caused by “interim gains” (see my article of July 2nd, 2019, “Interim Gains & Reinvestment”).

Oh—and the test answer is Jefferson City. Congratulations to those (and their grade school geography teachers) who answered it without cheating.

1 This is gain from the sale of “Section 1231 property,” which is “property used in a trade or business” that is depreciable under IRC Section 167. So, for example, a sale of real estate is Section 1231 property. On the other hand, a sale of stock or other equity interests is not Section 1231 property.

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