LOCAL INITIATIVES SUPPORT CORPORATION

July 1, 2019

Internal Revenue Service
CC:PA:LPD:PR (REG-120186-18), Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

To Whom It May Concern:

The Local Initiatives Support Corporation (LISC) is pleased to offer comments in response to the Notice of Proposed Rulemaking, "Investing in Qualified Opportunity Funds", published on May 1, 2019.

LISC is a non-profit housing and community development organization and certified Community Development Financial Institution (CDFI) with offices in 35 cities throughout the country, and a rural network encompassing 89 partner organizations serving 44 different states. LISC's work supports a wide range of activities, including affordable housing, economic development, building family wealth and incomes, education, community safety, and community health. In 2018 alone, LISC raised and deployed approximately $1.5 billion of capital into low-income urban and rural communities – including over $1 billion in private equity capital through federal Low Income Housing Tax Credits and New Markets Tax Credits. We believe that the Opportunity Zones tax incentive has the potential to unleash tremendous amounts of patient, private capital into the underserved urban and rural communities that are the core of LISC's markets.

LISC is appreciative of the efforts undertaken by the IRS to promulgate rules that provide clarity to investors, fund managers and other community stakeholders with respect to Opportunity Zone investments. We are generally supportive of provisions contained in the two tranches of proposed regulations that remove some of the barriers to securing investments, including:

(i) Establishing a ramp up period for Qualified Opportunity Funds (QOFs) to deploy capital, as well as a one-year period to reinvest capital.

(ii) Allowing Qualified Opportunity Zone Businesses (QOZBs), including both operating businesses and real estate businesses, a period of up to 31 months to fully deploy Opportunity Fund proceeds.

(iii) Clarifying how QOZBs may reasonably demonstrate that revenues are generated in the Opportunity Zones; and

(iv) Clarifying that a business engaged in the leasing of real property may qualify as a QOZB.

But there are still several items that would benefit from clarification through future rulemaking or related guidance from the IRS. LISC is a member of, or his been partnering with, several different trade associations and industry affinity groups that will be submitting comments in response to this Notice, including: the Economic Innovation Group (EIG); the Novogradac and Associates Opportunity Zone Working Group; and the U.S. Impact Investing Alliance (USIIA). We are supportive of the comments that have been submitted by these groups, and in some cases below are reinforcing recommendations raised in these letters.

<u>Qualified Opportunity Funds:</u>

Certification Requirements. As noted in our comments submitted to Treasury in response to the May 1, 2019 Request for Information on Data Collection and Reporting, we believe that an Opportunity Fund should be required to identify, at the time of certification, its intended community development outcomes and objectives. Collecting this information at the time of an Opportunity Fund's certification is not at all burdensome (it can simply be a drop down menu on a form), so will not in any way slow down Fund formation or investment activity. We also believe that QOFs should be required to self-certify that its principals have not, within a three-year period preceding the formation of the Opportunity Fund, been indicted, charged with or convicted of, or had a civil judgment rendered against it for, commission of fraud or a criminal offense.

Investment Ramp Up Period. We appreciate that the IRS provided QOFs an initial period of six months to make investments without being subject to the 90% asset test. In addition to this six month safe harbor, we believe that the Opportunity Funds should be provided with a 31 month timeframe (to run concurrently with the timeframe offered to QOZBs) to deploy investment capital into Qualified Opportunity Zone Businesses and Properties. This will enable QOFs to better manage their capital among multiple investment projects (in the case of multi-investment funds), and to tailor their investment schedule to meet certain construction milestones in the case of single-asset real estate funds.

Investment Wind Down Period. Just as QOFs need time to place investment capital, they will also need time to wind down investments, as the Fund may seek to close down as it approaches the end of year 10. The IRS should similarly provide a "safe harbor" such that QOFs may have at least two years to unwind transactions whereby the proceeds will not count against the 90 percent asset test.

Treatment of idle capital. As noted in previous comments submitted by LISC, to the extent the IRS is offering significant periods for which QOF capital will not be tested against the 90% asset test (i.e., during an initial ramp up period, a reinvestment period, or a wind-down period), then consistent with the intent of the Opportunity Zone program, the IRS should consider requiring that such funds must be held in a mission driven financial institution (e.g., a certified CDFI, a low-income credit union) or a minority depository institution.

Qualified Opportunity Zone Businesses:

QOZBs operating in multiple Opportunity Zone census tracts. The regulations frequently site that a QOZB must meet certain threshold level requirements with respect activities undertaken in the Opportunity Zone. However, it is anticipated that many QOZBs will be serving multiple Opportunity Zone census tracts. The regulations should clarify that that various references to "the" opportunity zone is to be read as one or more opportunity zones

Treatment of unimproved land. Provide that unimproved land acquired by a QOF or QOZB does not need to be improved by more than an insubstantial amount only in instances where: (i) the use of the land by the QOF or QOZB is an integral part of the trade or business of the QOF or QOZB; and (2) the QOF or QOZB reasonably expects its use of the land to generate economic activity which was not reasonably expected to occur by the owner of the land prior to its purchase and use by the QOF or QOZB.

Treatment of vacant property. The current requirement that a property must be vacant for at least five years in order to automatically be deemed to have met the "original use" test is unnecessarily long. This should be reduced to two years, and one year if the property is part of a community revitalization plan. Alternatively, the IRS could deem that one year is sufficient in instances where the property had been vacant prior to the Opportunity Zone receiving its designation by the Treasury Department.

Working capital safe harbor. QOZBs are permitted in certain circumstances to deploy Opportunity Zone investment capital over a 31 month period. The IRS should provide that certain disruptions that are beyond a business's control will not cause the business to lose the benefits of the working capital safe harbor.

Leasing of real property. The regulations required that in order to be deemed Qualified Opportunity Zone Business Property, the lease must be provided to the QOZB at a market rate. However, many tenants – particularly non-profit tenants – are often offered below market lease rates. The final regulations should limit the requirement for leases to be arm's length to leasing arrangements between related parties.

Treatment of Investments

Special Amount includible rule for partnerships and S corporations. The special inclusion rule in the proposed regulations may inadvertently hinder the use of the opportunity zone program for low income housing tax credit (LIHTC) investors. LIHTC properties have long term affordability requirements and lower cashflows, and therefore have limited appreciation at the end of the LIHTC Compliance period. Therefore, the main Opportunity Zone tax benefit for a LIHTC investor is the deferral and reduction of the initial capital gains tax. We ask the IRS reexamine this provision, and to adopt the technical amendments to this section of the proposed regulations as proposed by the Novogradac Opportunity zone working Group and also supported by the National Council of State Housing Agencies (NCSHA). This would allow additional capital gains dollars to be used to finance LIHTC properties in Opportunity Zones.

Investments made through a subsidiary. The proposed regulations state that the actual corporate subsidiary with the gain has to be the entity investing in the QOF. Many institutional banks, in accordance with regulatory requirements, invest in community development properties through a subsidiary community development corporation (CDC). These CDCs may not be the entity with the capital gains. Allowing for bank CDCs to invest the capital gains realized from consolidated affiliates would allow banks CDCs to access this additional capital source. We therefore support an expansion of the definition of the entity that has the capital gain to allow institutional investors to be able to claim bank affiliate capital gains through their CDC and use these funds for investments in QOFs.

Anti-Abuse Rules

LISC appreciates that the IRS is seeking additional comments with respect to what constitutes abuse under the Opportunity Zone incentive. While Opportunity Funds should generally be given a great deal of latitude to pursue investment strategies, LISC believes that the activities should at a bare minimum result in beneficial outcomes to the residents of those communities. To this end, to the extent the IRS intends to identify a specific listing of abusive activities, LISC believes that activities that have not gone through any community vetting/approvals OR vetting/approvals from the local governmental jurisdiction AND for which the end result is the dislocation of community residents should be identified as an abusive activity. To the extent the IRS receives recommendations from other commentators as to what activities would constitute abuse, we would recommend that such a list be posted for further public comment and reaction prior to appearing in regulations or in other formal guidance documents.

In addition, the IRS should consider offering a safe-harbor that will protect from the anti-abuse provisions any QOFs that obtain independent certification similar to the third-party standard adopted under benefit corporation legislation demonstrating that the QOF's activities further specified, measurable public benefits in a QOZ.

We thank you for considering these comments.

Sincerely,

Matt Josephs
Senior Vice President for Policy