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Room 5203
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

To Whom It May Concern:

We are writing regarding the second round of proposed regulations implementing the new Opportunity Zone tax incentive on behalf of the members of the National Multifamily Housing Council (NMHC) and the National Apartment Association (NAA) who represent the $1.3 trillion apartment industry and its nearly 39 million residents. For more than 20 years, NMHC and NAA have partnered to provide a single voice for America's apartment industry. Our combined memberships are engaged in all aspects of the apartment industry, including ownership, development, management and finance. NMHC represents the principal officers of the apartment industry's largest and most prominent firms. As a federation of 160 state and local affiliates, NAA encompasses over 75,000 members representing 9.25 million rental housing units globally.

At the outset, we would like to congratulate the Treasury Department and Internal Revenue Service for proposing extraordinarily thoughtful guidance to effectuate the Opportunity Zones program and, in particular, thank you for responding to many of the issues we raised in our June 8, 2018, and December 7, 2018, letters.

While we believe the first and second round of proposed Opportunity Zone regulations will help drive considerable investment in Opportunity Zones, we wanted to take this opportunity to recommend that several additional issues be clarified or reconsidered as part of final regulations. To make the Opportunity Zones program as effective as possible, the multifamily industry recommends that final regulations clarify or address the following issues:

**Modify Proposed Rules that Inhibit Rehabilitation of Property**

NMHC and NAA have long taken the view that it could be difficult to realize Opportunity Zone tax benefits in the context of rehabilitating multifamily property. This is a result of the statutory requirement to double the basis of an acquired property within 30 months.

We are extremely pleased that the first round of proposed regulations issued in October 2018 attempted to address this issue by excluding the basis of land from the required improvement threshold. While NMHC and NAA asked in our June and December 2018 letters that the Treasury Department and Internal Revenue Service waive the "double the basis" rule if a property has been vacant for a period exceeding one year, the Treasury Department and Internal Revenue Service have proposed a five-year vacancy period.

In the preamble to the proposed regulations, the Treasury Department and Internal Revenue Service solicited comments regarding the aggregation of different units of property for purposes of applying the "double-the-basis" rule. This is an issue worth exploring.

**Recommendations:**

*Five-Year Vacancy Period*

NMHC and NAA believe a five-year period vacancy period is far too lengthy and strongly encourage the Treasury Department and Internal Revenue Service to impose a one-year vacancy requirement in final regulations. Notably, the Treasury Department and Internal Revenue Service took exactly this approach in T.D. 8673, final regulations pertaining to Enterprise Zone Facility Bonds issued by state and local governments: "The final regulations provide that if real property is vacant for at least a one-year period including the date of zone designation, use prior to that period is disregarded for purposes of determining original use."

While the multifamily industry understands the concern that a building owner could leave an asset vacant simply in an effort to increase its attractiveness to potential Opportunity Funds, there could be a considerable cost to doing so in the form of foregone rental receipts. Owners of performing multifamily assets that are generating rental income are unlikely to allow a building to remain vacant for the potential sale to an Opportunity Fund. It is only buildings that are not in position to generate significant revenue that are likely to be left vacant. However, it could still be difficult to double the basis of such vacant structures in a manner that is economically viable for Opportunity Zone purposes. If the Treasury Department and Internal Revenue Service allowed acquired buildings left vacant for at least one year to meet the original use test, such structures could prove to be viable Opportunity Fund investments.

In addition, a five-year vacancy requirement may present administrative difficulties, as owners will be required to track when a building became and remained vacant. This may be particularly challenging with respect to buildings that first became vacant before the promulgation of the regulations (i.e., when taxpayers first became aware of the need to track vacancy).

If the Treasury Department and Internal Revenue Service are concerned about abuse but are comfortable with a five-year vacancy period (or upon re-consideration, some shorter period), perhaps the rule in the final regulations could be modified such that the five-year (or shorter) period becomes a safe harbor. If the building were vacant less than the safe harbor period, but at least one year, the taxpayer would be allowed to demonstrate that the vacancy resulted for a reason other than to qualify the building for favorable Opportunity Zone treatment. The demonstration would be based on the relevant facts and circumstances, which could include changes in zoning laws, the loss of relevant safety or health permits, changes in market conditions, or circumstances that made the building uninhabitable or inaccessible (e.g., latent structural defects, floods, natural disaster, etc.).

*Aggregation Rule*

NMHC and NAA believe that the Treasury Department and Internal Revenue Service should allow taxpayers to elect to aggregate all related costs for purposes of determining whether the "double-the-basis" rule is met. Multifamily improvement projects entail many capital costs related to different pieces of property. Although the bulk of the property likely will be classified as residential rental property, the improvement of a multifamily project may include property included in other classes, such as land improvements (e.g., parking facilities, landscaping, etc.) and tangible personal property (office equipment; furniture and fixtures; appliances; carpeting; electricity; heating and cooling systems; communications equipment, etc.). For tax purposes, these additional types of property are treated as units of property separate from the residential rental building in the hands of the taxpayer.

As suggested in the preamble to the proposed regulations, the Treasury Department and Internal Revenue Service should provide in forthcoming guidance that a taxpayer may elect to apply the "double-the-basis" rule by taking into account all capitalized costs associated with improving a residential rental project, whether or not such costs are capitalized into the cost of the residential rental property. Whether such costs are appropriately associated with the improvement of a multifamily housing project will depend on the relevant facts and circumstances. To address any potential uncertainty of a facts-and-circumstances test, guidance could provide a nonexclusive list of factors that would indicate that capitalized costs are associated with a multifamily project, including whether the costs (1) are incurred by the same or related legal entity that owns the residential rental property; (2) give rise to property that normally is associated with residential rental property; (3) give rise to property on contiguous pieces of land; (4) are described in regulatory permits; or (5) are described in any financing document, prospectus, offering material, or similar document.[1]

Allowing this election will provide needed flexibility to the "double-the-basis" rule and will correspond to business realities. As discussed above, real estate developers consider the costs associated with an overall multifamily "project" rather than as associated with individual units of property as defined by the tax law. The improvement of a particular building may not relate to the structure itself; it may relate to tangible personal property that is part of the building's interior and tends to wear out sooner than the exterior, the need for updated communication or utility systems, or other related infrastructure needs such as parking lots, roads, etc. To help realize the full potential from improving a structure, guidance should provide developers with the flexibility to choose and incur the most appropriate expenditures.

*Legislative Modifications*

While beyond the scope of final regulations, the multifamily industry also once again urges the Trump Administration to support statutory modifications to reduce the basis increase necessary to qualify a multifamily rehabilitation project for Opportunity Zone purposes. It is noteworthy that to qualify for an allocation of Low-Income Housing Tax Credits, owners must commit to rehabilitations valued at the greater of: (1) 20 percent of adjusted basis of a building; or (2) $6,000 ($7,000 in 2019 as adjusted for inflation) per low-income unit (Internal Revenue Code Section 42(e)(3)(A)(ii)(II)).

Given the nation's housing affordability challenge, we believe that the Treasury Department, Internal Revenue Service, and Congress should utilize every available tool to help expand the supply of housing. We further note that it is likely to be considerably more efficient to utilize existing structures to expand supply than to build new.

## Flexible Opportunity Fund Reinvestment Rules

In our December 2018 letter, we noted that individuals may wish to exit one Opportunity Fund to invest in another. Enabling taxpayers to exit funds and invest in competing funds without penalty serves two essential purposes. First, it keeps taxpayers invested in Opportunity Funds and capital flowing to economically distressed areas. Second, it ensures capital is put to its most productive use. Allowing taxpayers to rebalance their Opportunity Fund investments to seek higher rates of return will ensure capital is efficiently invested.

**Recommendation:** We recommend that the Treasury Department and Internal Revenue Service allow investors to exit one Opportunity Fund and reinvest the proceeds in another Opportunity Fund without negative consequence to the five-, seven-, and 10-year basis adjustment thresholds so long as

[1] See, for example, section 7.01(2) of Notice 2018-59 that allows taxpayers to aggregate multiple units of separate pieces of property into a single project.

proceeds from exiting a Qualified Opportunity Fund are reinvested in another Qualifying Opportunity Fund within 180 days.

**Extend Penalty Relief to Taxpayers Affected by Events Beyond the Taxpayer's Control**

In our June 2018 letter, we requested that the Treasury Department and Internal Revenue Service provide sufficient time for Opportunity Funds to invest capital in Opportunity Zone property before a penalty is triggered pursuant to the 90 percent asset test. We were extremely pleased that the first round of proposed regulations permits Opportunity Funds to take up to 31 months to deploy capital so long as the taxpayer has a comprehensive plan for the funds. In our December 2018 letter, we recommended that Opportunity Funds be granted up to one additional year to deploy capital for either new construction or rehabilitation purposes upon demonstrating to the Internal Revenue Service that a state or local government or authority delayed development. We are grateful that the Treasury Department and Internal Revenue Service are proposing to extend the period to deploy capital for delays attributable to the government in cases in which applications were completed prior to the relevant deadline.

While the Treasury Department and Internal Revenue Service have proposed beneficial rules for delays attributable to the government, multifamily development may also be affected by other events beyond the taxpayer's control, such as acts of God, natural disasters, financing delays, labor disruptions, etc. Treasury and the IRS have allowed excusable delays for purposes of other time-sensitive deadlines.[2]

**Recommendation:** NMHC and NAA request that the Treasury Department and Internal Revenue use the reasonable cause exception under Internal Revenue Code Section 1400Z-2(f)(3) to extend penalty relief in cases a taxpayer may be unable to deploy capital due to events beyond the taxpayer's control, and provide a nonexclusive list of acceptable delays.

**Sales of Assets Held by Lower-Tier Partnerships**

The second round of proposed Opportunity Zones guidance enables investors in Opportunity Funds that sell assets to exclude capital gains so long as they have held their investment interest for at least 10 years. Such investors need not sell their interest in the Opportunity Fund. There may be cases, however, in which an Opportunity Fund itself will not own the underlying assets. Instead, the assets could be owned by lower-tier partnerships. It is unclear if the capital gains exclusion applies to assets held in lower-tier partnerships in cases in which an investor has held an Opportunity Fund investment interest for at least 10 years.

**Recommendation:** NMHC and NAA request that final regulations clarify that investors may exclude capital gains from asset sales by lower-tiered partnerships so long as an investment interest has been held for at least 10 years.

**Investment of REIT Capital Gain Dividends**

In our December 2018 letter, we noted that under the first round of proposed Opportunity Zone regulations, taxpayers may have insufficient time to invest capital gains into Opportunity Funds because they might not be able to ascertain the character of the income they wish to invest.

[2] See, for example, section 6.03 of Notice 2018-59 that provides an exception for, and a nonexclusive list of, exclusive delays relating to the construction of qualified energy property.

The first round of Opportunity Zone regulations provided that taxpayers have 180 days to invest capital gains into an Opportunity Fund. However, the multifamily industry noted that the character of Internal Revenue Code Section 1231 income might be unknown until the end of a taxable year when gains and losses can be netted. Similarly, the character of a REIT dividend might not be known when the dividend is paid and instead only becomes clear when a Form 1099-DIV is issued after a taxable year concludes.

We are extremely pleased that the Treasury Department and Internal Revenue Service have proposed to address this issue with respect to Section 1231 income and will allow taxpayers 180 days from the end of a taxpayer's taxable year to invest Internal Revenue Code Section 1231 gains into Opportunity Funds. We believe that the Treasury Department and Internal Revenue Service should extend similar treatment to REIT capital gain distributions. We can think of no legal or policy rationales that could justify precluding similar tax treatment.

**Recommendation:** NMHC and NAA request that the Treasury Department and Internal Revenue Service provide taxpayers with 180 days following the end of a REIT's taxable year to invest capital gain dividends into Opportunity Funds.

**Opportunity Fund Data Reporting**

There has been widespread discussion regarding how to measure the effectiveness of Opportunity Zone investments and the extent to which the program will be successful in driving investment capital into economically distressed areas. In April 2019, the Treasury Department issued a *Request for Information on Data Collection and Tracking for Qualified Opportunity Zones*. The Department of Housing and Urban Development (HUD) has also issued a Request for Information, *Review of HUD Policy in Opportunity Zones*. The Treasury Department's Request for Information asks a series of questions regarding data that could be collected to analyze the effectiveness of Opportunity Zones. HUD's Request for Information specifically asks: How can HUD properly evaluate the impact of Opportunity Zones on communities?

NMHC and NAA would offer the following comments with regard to these requests for information. First and foremost, with taxpayer dollars being utilized, the multifamily industry strongly supports evaluating the efficacy of Opportunity Zone investment incentives. We believe legislation (H.R. 2593 and S. 1344) introduced in May 2019 by Representatives Ron Kind and Mike Kelly and Senators Cory Booker, Tim Scott, Maggie Hassan, and Todd Young would establish an appropriate framework for collecting relevant information. We support the passage of H.R. 2593 and S. 1344 or the issuance of regulations based on its provisions.

Second, we note that while the multifamily industry may utilize Opportunity Zone tax incentives, the program is contained within the Internal Revenue Code and is, therefore, subject to oversight by the Treasury Department and Internal Revenue Service. We would be concerned by any separate reporting requirements that HUD might seek to impose. We note that the Treasury Department is well equipped in safeguarding confidential taxpayer information, and we would be concerned with any proposal that would allow other agencies to access such information without proper safeguards. Furthermore, as the Opportunity Zone program is not limited to housing, the multifamily industry believes that multifamily firms should have no additional reporting requirements to HUD that non-real estate companies would not be subjected to by virtue of not being involved in real estate. All that said, we would encourage HUD and the Treasury Department to work together to analyze the effectiveness of the Opportunity Zone program in such a manner that maintains ultimate oversight within the purview of the Treasury Department and does not add reporting requirements to opportunity funds invested in multifamily housing that are not imposed on all other opportunity funds.

NMHC and NAA thank you for considering our views. We hope to work with you to make Opportunity Zones as successful as possible. Please feel free to contact Cindy Chetti, NMHC's Senior Vice President of Government Affairs, at 202-974-2300, or Greg Brown, NAA's Senior Vice President of Government Affairs, at 703-518-6141, should you have any questions.

Sincerely,

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