

November 30, 2018

Mr. Scott Dinwiddie
Associate Chief Counsel
Income Tax & Accounting
CC:PA:LPD:PR (REG-115420-18), Room 5203
Internal Revenue Service
P.O. Box 7604 Ben Franklin Station
Washington, D.C. 20044

Re: Ovation Partners, L.P. – Opportunity Zone Fund

Dear Mr. Dinwiddie:

Ovation Partners is an investment adviser with more than \$500 million of assets under management across a variety of private credit and specialty finance asset categories.

We are excited about the potential for investment in opportunity zones created by Internal Revenue Code (“**IRC**”) Sections 1400Z-1 and 1400Z-2. The Proposed Regulations under Section §1400Z-2 of the IRC (the “Proposed Regulations”) recently issued by the Department of Treasury (“**Treasury**”) were an important step towards resolving some of the uncertainty in the law itself that has been an impediment to jumpstarting investment in opportunity zones.

We appreciate the fact that the Proposed Regulations took into account many of the comments provided by taxpayers, and that in the Preamble to the Proposal Regulations, Treasury requested further comments on specific aspects of the Proposed Regulations, as well as on general matters that are necessary for full implementation of this investment incentive.

As a private investment vehicle, our focus is on meeting the needs of potential investors in qualified opportunity funds (“QOF”). We would like to bring to your attention an issue we have encountered regarding the timing requirements for investing in QOF’s after a taxpayer realizes gain from the sale or exchange of property. We believe that providing clarity on this issue will assist taxpayers in maximizing their ability to invest in opportunity funds as soon as possible, thus maximizing the early flow of capital into opportunity zones.

Overview

Under Section 1400Z-2 (a)(1), a taxpayer who realizes a gain from a sale or exchange may elect to defer recognition on that gain if he or she invests up to the amount of the gain in a QOF within 180 days of the gain realization event. The proposed Regulations clarify that, if the taxpayer is a partnership (or other pass through-entity) the partnership may elect to defer the gain by investing in a QOF. If it does, then no part of the deferred gain is required to be included in the distributive shares of the partners under IRC Section 702, and the gain is not subject to IRC Section 7.05(a)(i). If, however, the partnership does not elect to defer the gain, the gain is includible in the distributive shares of the partners under IRC Section 702 and is subject to IRC Section 705(a)(i). In this case, if a partner's distributive share complies with the eligibility rules of Section 1400Z-2(a)(1), the partner may elect its own deferral with respect to its distributive share if the partner invests in a QOF.

If the partner elects to defer gain instead of the partnership, the default rule is that the partner's 180-day period begins on the last day of the partnership's tax year, because that is the day the partner would recognize the gain if it had not been deferred. The Proposed Regulations also provide an alternative rule if the partner knows (i) the date of the partnership's gain and (ii) that the partnership has decided not to elect deferral under Section 1400Z-2. In that case, the partner may choose to begin its own 180-day period on the same date as the gain actually occurred, which in all cases is the earlier of the two dates allowed.

Analysis

The alternate (earlier) deferral period made available to a partner when the partnership does not choose to defer realized gain provides helpful flexibility to the partner, but fails to address the following question:

Where a partnership has elected not to defer gain, can an individual partner defer its allocable share of the gain and use the date of the sale or exchange that triggered the gain as the beginning of the 180-day investment period for a portion of the gain, but use the end of the partnership's tax year as the beginning of the 180-day period for the remaining portion of the gain? This would result in two different 180-day periods for the partner's share of the gain from a single sale or exchange and would give the partner the ability to make an early investment for a portion of the gain but additional time to invest the remaining gain. This serves the purpose of the law, which is to get qualified deferral gains invested as early as possible in projects that meet the criteria of the law.

For example, assume a \$10 million partnership gain from a sale or exchange on March 1, 2018. Assume that the partnership decides not to elect to defer the gain and communicates that to its partners. Any partner can then elect to defer the gain. The default rule is that each partner's 180-day period commences on the last day of the partnership's tax year, or December 31, 2018. However, the partners may elect instead to use the first day of the partnership's 180-day period, or March 1, 2018. Assume that Partner A's allocable share of the partnership gain is \$5 million and that Partner A finds an opportunity to invest \$1 million in a qualified opportunity fund in July of

2018. Assume that the target can absorb an investment of no more than \$1 million. Can Partner A elect to use the partnership's 180-day period for the \$1 million of gain but use Partner A's 180-day period (commencing on December 1, 2018) for the remaining \$4 million of gain, giving Partner A until June of 2019 to invest the second \$4 million?

The Proposed Regulations do not address the above scenario. The Proposed Regulations acknowledge in several places that a partnership may elect to defer all or less than all of the gain arising from a sale or exchange, and if the partnership decides not to defer all or less than all of the gain, a partner may elect to defer some or all of its allocable share of the gain. This rule appears to be intended to provide flexibility so that the partners and the partnership can determine the best way to handle the gain deferral amongst themselves. But the Proposed Regulations do not specifically address whether a partner may split its allocable share of gain between two different 180-day periods.

The Proposed Regulations do provide that a taxpayer can split its deferred gain into investments in one or more QOF's. There seems to be no reason that a partner making investments in two different QOF's could time each investment differently and make one investment in a QOF based on the partnership's 180-day period and a later investment in a different QOF using the partner's 180-day period. Indeed, it may facilitate the prompt investment of funds in opportunity zones if the taxpayer can take advantage of the early investment opportunity even if less than the total gain deferral is available with that investment.

It should be noted that splitting the 180-day periods is merely a timing issue, and should not be considered to violate the rule that only one deferral election can be made with respect to a particular gain realization event. The limitation on making more than one deferral election relates to the election to defer or not, not the applicable deadline for making the deferred gain investment.

Recommendation

There does not seem to be a policy reason to prevent a partner from having the flexibility to choose the timing of its deferred gain investment and, if more than one investment opportunity arises, to split the gain deferral between the two on a timeline that makes sense. Since the partner has the flexibility to choose either the partnership's 180-day period or that of the partnership under the Proposed Regulations, permitting the partner to use one 180-day period for an early investment and the later 180-day period for a later investment seems like a logical extension of the existing regulatory framework. We do not believe that this change creates the possibility of abuse. Because the proposed change would simply be a clarification of a concept introduced in the existing Proposed Regulations, we believe that Treasury has the authority to include this clarification in the final Regulations.

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Page 4

We appreciate your consideration of these comments and look forward to the opportunity to discuss them with you if you would find that helpful. I can be reached at your convenience at (303) - (726) - (7633) or by email at John@ovationpartners.com.

Very truly yours,

By:

A handwritten signature in black ink, appearing to read "John W Simmons", written over a horizontal line.

John W Simmons

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