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## THE 123'S OF THE OPPORTUNITY ZONES (PART THREE)

**I**n this article, we will provide several examples demonstrating the practical application of the terms and requirements we have been discussing in our first two parts.

We remind you that even though these rules and requirements are established at the federal level, the same were adopted in Puerto Rico for the purpose of incentives approved as part of Law 21-2019, Act for the Development of Opportunity Zones in Puerto Rico' 2019 and then Law 60-2019, The Puerto Rico Incentives Code.

**Example 1:** Gain to defer:

On May 1, 2019, Ricardo sold certain shares in the stock market for \$2,000,000. His original basis was \$1,000,000, generating an eligible capital gain of \$1,000,000. On May 15, 2019, Ricardo invested \$1,000,000 in a Qualified Opportunity Fund ("QOF"). When the time comes to file his income tax return for 2019, Ricardo will choose not to tax the gain in 2019.

**Analysis:**

The total amount of the capital gain is eligible for the incentive, since:

- it was generated in a sale with an unrelated person,
- an amount equal to the gain was invested on time (within 180 days since it was generated) in a QOF and
- at the time of filing the return for 2019, Ricardo will choose, in the corresponding way, not to tax the profit.

**Example 2:** Deferred gain to recognize when selling QOF interest:

Continuing with the example, if Ricardo sells his interest in the fund on May 17, 2024 for \$1,500,000, he will recognize the original gain of \$1,000,000 minus 10% plus \$500,000 for the increase in value on that year's return. In other words, Ricardo will pay tax only on \$900,000 of his original gain as he kept the investment in the Fund for at least 5 years. Instead, if Ricardo

sells his interest on the QOF after May 15, 2026 for the same amount, he will recognize a profit of \$850,000 plus the \$500,000 appreciation.

**Example 3:** If Ricardo sells his interest in the QOF for \$1,500,000 sometime after May 15, 2029, on December 31, 2026 (date set by law) he has to recognize the \$850,000 of his deferred gain and in 2029 the profit of \$500,000 from the increase in the value of the investment will be completely exempt from income tax for having kept the investment for at least 10 years.

We can summarize the three examples above in the following table:

The following example will discuss the application of the original use requirement in the zone. Specifically, purchased property that has been used in the area.

**Example 4:** During September 2019, a QOF buys a property for \$800,000. The property is located within the boundaries of a qualified opportunity zone. The property contains in addition to the land (valued at \$480,000), a building that had been used as a factory until 2010 (valued at \$320,000). QOF plans to turn the building into apartments for rent. Since the building has been vacant for at least 5 years, QOF does not have a minimum requirement for investment in improvements to meet the original use requirement in the area as long as it is put into service. If, on the contrary, the building had been abandoned in 2017, the fund would have 30 months to make an investment in improvements of at least \$320,000 so that the building qualifies as a qualified opportunity zone business property since it had already been used within the area.

In our next article, we will discuss the incentives that were introduced in Puerto Rico by Law 21-of May 14, 2019 and then included as part of Law 60-2019, better known as the Puerto Rico Incentives Code.