

A WINNING COMBINATION: UNCLE SAM'S EXCESS PROPERTY INVENTORY AND THE OPPORTUNITY ZONE TAX INCENTIVE

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A new mandate requiring the federal government to sell property it no longer uses or needs creates significant "opportunities" for investors with capital gains to use the Opportunity Zone tax incentive to finance the acquisition and rehabilitation of the excess inventory. The General Services Administration (GSA) owns and leases over 370 million square feet of space in 9,600 buildings in more than 2,200 communities nationwide. Recent legislative reforms have ushered in a streamlined framework for the disposal of some of these undervalued and underutilized federal properties. These efforts have reduced regulatory burdens and created significant incentives for investment in the acquisition of federal properties. Coincidentally and serendipitously, several of these GSA properties fall within low-income census tracts designated as Opportunity Zones (OZs). An excess in underutilized properties combined with the abundance of incentives created by OZs is creating natural synergies for targeted investment strategies.

The GSA has a vast array of properties under its control, including many that no longer serve a necessary government function. While the federal government is required to sell these unused or underutilized properties, the process has historically been viewed as complicated and slow. Sponsored by former Congressman Jeff Denham, the Federal Asset Sale and Transfer Act of 2016 (FASTA) streamlined the process by creating the Public Buildings Reform Board (PBRB) to identify opportunities for the federal government to significantly reduce its inventory of civilian real property and thereby reduce costs. The GSA is currently seeking recommendations for up to \$750 million worth of underutilized and vacant federal properties to sell in the next six months — part of an eventual \$8 billion worth of opportunities the PBRB is mandated to consider.

The Tax Cuts and Jobs Act of 2017 introduced the OZ tax incentive that offers potentially significant tax benefits for investors to help to attract funding for projects and businesses in low-income census tracts, including the acquisition and rehabilitation of GSA buildings located within these tracts. Using the OZ incentive, individuals and other entities can delay paying federal income tax on capital gains until as late as December 31, 2026, if those gains are invested in OZ Funds that invest at least 90 percent of their assets in qualified businesses or tangible property located in designated OZs. Investments held at least five or seven years by that date are eligible for a total 10 percent or 15 percent step-up in basis, respectively. Further, the capital gains on investments in the OZ Funds can be free of federal income tax if the investment in the OZ Fund is held for at least 10 years. There are 8,766 designated OZs throughout the United States, the possessions, and the District of Columbia.

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Subject to meeting certain OZ rules and regulations, including that the properties are located in a designated OZ, the possibilities are almost limitless for utilizing the OZ incentive. These could include the acquisition and rehabilitation of GSA properties into affordable housing, commercial real estate, agricultural supply warehouses, manufacturing hubs, innovation centers, and renewable energy projects, to name just a few examples. Urban, suburban, and rural properties throughout the country can be rehabilitated and repurposed using the OZ incentive. The streamlined disposal of federal properties in tax incentivized OZs is a potential boon for well-placed investors and can reduce the cost of capital for developers and entrepreneurs.

K&L Gates has a wide array of partners and professionals to assist you in navigating the intricacies of OZ and GSA rules. We advise and provide guidance to clients about the FASTA process. Our multidisciplinary OZ team of tax and tax policy, investment management, real estate, corporate, and other professionals collaborate to provide a full spectrum of cross-practice services to help investors, developers, entrepreneurs, innovators, and fund sponsors understand and implement the OZ incentive in order to unlock its full investment potential, including in connection with the acquisition and rehabilitation of GSA property. For more information, please contact any of the authors listed on this alert or visit our OZ webpage at <http://www.klgates.com/opportunity-zones-ozs-practices/>.

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