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## OZ: NY Moves to Reduce Certain State Opportunity Zone Benefits for NY deals - Smart, Necessary or Something Else?

New York legislators have moved forward in their 2021 budget process to **limit some of the state Opportunity Zone benefits** that had previously applied in New York. Some commentators have pointed to the budget process reduction of benefits as a "left wing" reaction to former President Trump's support of the federal OZ program (which applies in all 50 states and the US Virgin Islands and Puerto Rico). Others have stated that it is a necessary move to reduce benefits for deals that should not be receiving federal and state benefits.

If the budget is approved, and the provisions become operative, New York will no longer offer some of the state tax benefits to real estate investors funding Opportunity Zone projects in New York, placing New York deals at a disadvantage to New Jersey, Connecticut, Ohio and other adjacent states that have approved and will retain their state benefits.

The OZ program is a Federal program that was enacted in 2017 and which became operative in 2018. Governors of all 50 states, including New York, were asked to review census data provided by the federal government which focused the Opportunity Zone program on low income areas throughout the US as identified in HUD census data from 2010. The Governors of all 50 states were then given 3 months to choose from within the potential applicable opportunity zones in their state which zones should become Opportunity Zones. Thereafter, once these zones were selected by the various governors, they were sent to Treasury for final approval, all of which selected zones were ultimately approved.

This process occurred during early 2018. Thereafter, the majority of states also "followed form" and permitted zones that the states had previously selected to be OZs to also be eligible for state benefits which would be the same as the federal benefits that existed under the program (i.e., (1) **deferral** of capital gains until 12-31-2026 (the "**Deferral Benefit**"); (2) potential **reduction of the amount that is subject to tax** by 15% if gain eligible dollars were invested into a qualified opportunity zone fund in 2018 or 2019, or 10% if gain eligible dollars were invested into a qualified opportunity zone fund in 2020 or 2021 (the "**Reduction Benefit**"); and, (3) if the investor followed the rules of the OZ Program and invested an amount of gain eligible dollars into a QOF (the "fund") and left its investment in the QOF for 10 years or more, and, thereafter the QOF sold the property or the business it owned after the 10 year period but before 12-31-2047, then all gain on the sale of the business or real estate would NOT be subject to federal capital gains tax (the "**Exclusion Benefit**"). By electing to follow form, the states that did so, elected to have the Deferral Benefit, the Reduction Benefit and the Exclusion Benefit also apply at the state level on gains that would have otherwise been payable to the state; meaning the applicable states would also permit investments in their applicable OZ areas to obtain a state level Deferral Benefit, Reduction Benefit and the Exclusion Benefit.

New York, like all of its adjacent neighboring states, was one of the states that enacted legislation to incent Opportunity Zone investments by permitted such OZ benefits at the state level (i.e., the Deferral Benefit, the Reduction Benefit and the Exclusion Benefit at the New York level).

Under the 2021 New York budget proposal, the **New York Deferral Benefit and the New York Reduction Benefits** at the New York level would **NO LONGER** be applicable. The result of this change is that investors in New York businesses in the New York OZs and in real estate in the New York OZ, will no longer receive the same benefits as neighboring states, which could result in investors looking at these other adjacent states first or in a more meaningful way, given that the state level OZ incentives exist there rather than in New York.

While some commentators have stated this will "deal[] another blow to the program and developers taking advantage of it", my personal view is that the benefits being eliminated in the budget process (i.e., deferral of capital gains payments until 12-31-2026 and reduction of the amount subject to tax by 10% if investment was made in 2020 or 2021), are not the real driver of the OZ program and the massive amount of investment that has occurred in the low and moderate income opportunity zones nationally since the enactment of the OZ program – rather, it is the **Exclusion Benefit, which is NOT being eliminated in New York**, that is the main driver of behavior in the OZs.

Even with the New York budget modifications, New York's 514 census tracts included in the program will still qualify for federal tax incentives for investing in these distressed areas and the **New York Exclusion Benefit will still apply**.

**Follow The Yellow Brick Road**: So, has New York cut off its nose to spite its face? Slightly, as some investors who are seeking both federal and state benefits to justify a more difficult project will likely look elsewhere. That said, the real driver of transactions in the OZ space as noted above is the Exclusion Benefit which applies once one has been invested in the applicable opportunity zone for 10 years or more, and this benefit, notwithstanding the New York change, will still exist at BOTH the federal and New York state level. On balance, while the budget change sounds like a big move and strikes a blow for anti-Trump sentiment, in reality, the real opportunity of the OZ program in hopefully creating jobs for local residents will remain and the Exclusion Benefit driver will remain in tact and continue to provide a reinforcer for this type of behavior.

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