

ASSET STRATEGY

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2026

INVESTING IN THE ZONE

INTRODUCTION TO QUALIFIED
OPPORTUNITY ZONES

What is the Qualified Opportunity Zone Program?

The **QOZ Program** was established in 2017 by the **Tax Cuts and Jobs Act ("TCJA")** as a place-based tax incentive to spur long-term investment in **designated low-income U.S. communities**. It was made permanent under the One Big Beautiful Bill Act (OBBBA) signed in 2025.

The core idea: **invest capital gains into specially designated areas (Qualified Opportunity Zones, or QOZs) via Qualified Opportunity Funds (QOFs) and receive favorable tax treatment in return.**



What are Qualified Opportunity Zones (QOZs)?

A **Qualified Opportunity Zone (QOZ)** is a U.S. census tract that has been formally nominated by the state's governor and certified by the U.S. Department of the Treasury for inclusion in the QOZ Program.

Under the initial legislation, each governor was permitted to select up to 25% of the state's eligible census tracts for nomination under the program.

To qualify for designation, a census tract must meet **one** of the following "low-income community" (*LIC*) tests (*using the most recently available census data at the time*):

- Have a poverty rate of at least **20%**.
- If it is located in a metropolitan area, the median household income of the tract must be **no greater than 80%** of the metropolitan median household income (or the statewide median household income, whichever is higher).
- If located outside a metropolitan area, the median household income must be **no greater than 80%** of the statewide median household income.

AS OF 2025, THERE ARE 8,764 QOZS ACROSS ALL 50 STATES, D.C., AND U.S. TERRITORIES; HOWEVER, THESE DESIGNATIONS WILL BE RE-EVALUATED AND PARTIALLY REPLACED BEGINNING JANUARY 1, 2027.

Source: <https://www.hud.gov/opportunity-zones> as of 10.9.25

Potential Tax Benefits of Qualified OZones (QOZ)?

Deferral	Basis Step-Up and Exclusion of Appreciation	Elimination of Gain on Sale for Long-Term Hold
Under the original program, if a taxpayer reinvested a capital gain into a QOF within 180 days of the gain event , the tax on that gain could be deferred until the earlier of the sale of the QOF interest or December 31, 2026. With OBBBA , for investments made January 1, 2027 or later, recognition of deferred gain occurs five years after investment (unless earlier disposition).	Under the TCJA rules: - A 10% basis step-up was available for five-year holds, and an additional 5% for seven-year holds. - If held for at least 10 years, the investor could elect to step up basis to fair market value and exclude appreciation from tax. Under OBBBA: - For investments made on or after Jan. 1, 2027, there is only a 10% basis step-up available if the investment is held for five years, with no additional step-up occurring at year seven. - For rural QROFs: a 30% step-up at five years if held that long. - For investments held 10 years or longer, the exclusion of appreciation remains, but for investments held beyond 30 years will have their basis locked in at the 30-year fair-market value; appreciation after that date is taxable.	If the investment is held at least 10 years (and meets QOF/QOZB requirements), the appreciation on sale may be tax-free at the federal level (subject to meeting all requirements). However, investors should always evaluate risk, asset performance, and structure.

Key Recent Changes to the QOZ Program (2026)

Thanks to the One Big Beautiful Bill Act (OBBBA), significant changes affect how the QOZ Program will work moving forward. These are critical for those who are planning now:

- The QOZ Program is now permanent.** The prior sunset date of December 31, 2026 for making new QOF investments has been eliminated.
- QOZ designations will be re-evaluated every 10 years.** Governors must nominate new zones starting July 1, 2026, with redesignations taking effect January 1, 2027.
- Tract-eligibility criteria have been tightened.** For example, low-income community thresholds are now reduced from 80% to 70% of the relevant median income, and contiguous tract designations have been eliminated.
- The law introduces enhanced benefits for rural investments.** A new category, **Qualified Rural Opportunity Funds (QROFs)**, offers **increased basis step-up (30%)** and relaxed "substantial improvement" requirements in rural QOZs.
- Qualified Rural Opportunity Funds (QROFs)** are a new sub-category of QOFs investing primarily in rural areas (defined as communities under 50,000 in population). QROFs offer enhanced incentives, including a **30%** basis step-up after five years and relaxed substantial-improvement rules (only a **50%** increase required).
- Robust new reporting and compliance requirements are in place for QOFs and QOZBs, including penalties for non-compliance.**

QOFs / QOBZ

What is a QOF?

A **Qualified Opportunity Fund (QOF)** is an entity organized as a partnership or corporation that generally must hold at least **90%** of its assets in Qualified Opportunity Zone (QOZ) property, subject to IRS rules and measurement methods (*see IRC Section 1400Z-2 and applicable IRS guidance*). QOFs invest in real estate and businesses (*existing or start-ups*) located within QOZs (*or in designated types of QOZB businesses*). The QOF must hold QOZ property (*such as an interest in a Qualified Opportunity Zone Business*) to satisfy the 90% asset test.

What is a QOBZ?

A **Qualified Opportunity Zone Business (QOZB)** is a business entity that meets specific eligibility requirements under § 1400Z-2 of the Internal Revenue Code: at least **70%** of its tangible assets must be Qualified Opportunity Zone Business Property (*used or located in a QOZ*); at least **50%** of its gross income must be derived from the active conduct of the business within a QOZ; no more than **5%** of its assets may be non-qualified financial property; and the business may not be a "sin business" (*such as a golf course, liquor store, country club, or racetrack*). The QOZB serves as the operating vehicle through which a Qualified Opportunity Fund (QOF) deploys capital.

Understanding Eligibility

What is an 'Eligible' Gain?

An eligible gain for the purposes of the Opportunity Zone Program is a gain from the sale or exchange of property with an unrelated party (*generally meaning no more than 20% common ownership*) that is treated as a capital gain for federal income tax purposes. Such gains may arise from:

- **Stocks, bonds, options, hedge fund interests.**
- **Primary or secondary residences.**
- **Bus. interests, machinery, comm. buildings.**
- **Land, livestock, artwork, wine collections, automobiles and other non-ordinary assets.**

Note that only gains recognized for federal income-tax purposes are eligible — ordinary income or Section 1231 losses do not qualify.

What is an 'Eligible' Taxpayer?

Taxpayers eligible to elect gain deferral under the Opportunity Zone rules include:

- **U.S. Individuals realizing eligible gains.**
- **C-corporations, including regulated investment companies (RICs) and real estate investment trusts (REITs).**
- **Partnerships or other pass-through entities where the partners or owners may elect deferral with respect to their distributive share of eligible gain.**

The first day of the 180-day reinvestment period generally begins on the date the gain would be recognized for federal income tax purposes (*absent the election*).

Important Deadlines

Legacy Opportunity Zone investments (those made before January 1 2027) must recognize deferred gain by December 31 2026.

Generally, to qualify for the tax benefits under the QOZ Program, eligible capital gains must be reinvested into a Qualified Opportunity Fund (QOF) within **180 days** of the sale or exchange of the asset. However, the rules governing gains reported on a Schedule K-1 from a partnership allow additional flexibility, creating more planning options for advisors.

For example, if a partnership operates on a calendar-year basis, K-1 partnership gains realized on or after January 1, 2025, must be invested in an eligible QOF by September 11, 2026, using one of the three permitted start dates for the 180-day window:

- **180 days starting on the date the partnership sold the asset.**
- **180 days beginning on the last day of the partnership's taxable year (December 31 for a calendar-year partnership).**
- **180 days starting on the date the partnership's tax return is due (*without extensions*)—March 15 in the case of a calendar-year partnership.**

Comparing QOFs & 1031 Exchanges

QOFs and 1031 exchanges both present the potential for meaningful tax incentives and may be used in tandem. However, the **two vehicles differ significantly** and therefore may suit different investor types.

Under the 2017 Tax Cuts and Jobs Act, only real property retains eligibility for 1031 exchanges. Capital gains from assets such as stocks, bonds, art, wine, livestock, classic automobiles, and other collectibles **no longer qualify**. Only real estate held for business or investment purposes may utilize a 1031 exchange, while capital gains from real estate or most other assets may instead be invested in a QOF.



Side-By-Side Comparison of 1031s & OZones

1031 Exchange	Category	Qualified Opportunity Zone
Real estate held for investment purposes.	← ELIGIBLE ASSETS* →	Capital gains from many types of capital assets may be eligible for deferral through investment in a Qualified Opportunity Fund (QOF). Eligibility depends on the nature of the gain and IRS rules and limitations; consult a tax advisor to confirm whether a particular gain qualifies.
Principal and gain from the real estate sale are eligible.	← ROLLOVER PARAMETERS →	Only the capital gain portion must be invested (<i>principal is not required</i>).
Real property without location restrictions.	← ELIGIBLE INVESTMENTS →	Investments in QOF property: commercial real estate, housing, infrastructure, businesses located in a QOZ (or in a QROF in rural zones for post-2026 investments).
Identify a replacement property within 45 days and close within 180 days.	← REPLACEMENT PROPERTY →	No specific property identification required; the gain must be invested in a QOF within 180 days of recognition (or other specified starting point for passthrough entities).
May be deferred indefinitely with a step-up in basis upon death.	← CAPITAL GAINS TAX →	For gains invested ≤ 12/31/26: defer until that date or sale. For gains ≥ 1/1/27 (OBBA): deferral lasts 5 yrs or until disposition; 10% basis step-up (30% for QROFs) after 5 yrs; appreciation excluded after 10 yrs; basis locks at FMV after 30.
Maximize after-tax return through income and appreciation.	← INVESTMENT GOALS →	Maximize after-tax return through income, appreciation, and deferred/eliminated gain, especially for investors with broader asset-class gains and longer hold horizons.

**Gains recognized from the disposition of the following assets are eligible to receive the respective tax benefits of the 1031 exchanges and investments in QOFs.*

When you sell investment real estate, you have options to reduce your tax bill. One option is a **1031 Exchange**: you sell a property and buy another similar property, and to avoid taxes, you must reinvest all the sale proceeds into the new property.

Another option is investing in a **Qualified Opportunity Fund (QOF)** through the Opportunity Zone program. In this case, you only need to invest the gain (the profit from your sale, including some depreciation recaptured as gain) — you can keep your original capital or “basis.”

- The QOF option also has fewer strict rules: you don’t face the 45-day property identification requirement, you don’t need a qualified intermediary, and you don’t have to trace every dollar the same way.

Deciding whether to use a 1031 exchange, a QOF, or both depends on your overall situation, including how much you originally paid (*basis*), how much depreciation you took, how much debt was on the property, your sale price, and what you want to happen in the long run. Because these rules are complex and carry big tax effects, you should work with a tax advisor, lawyer, and financial planner to make the best choice.

Taxable Investment vs. QOZ Return Comparison

Below is a chart that shows the difference in returns on two hypothetical investments with the same internal rate of return (IRR):

Potential Tax Advantages of Investing in a Qualified Opportunity Fund

SCENARIO:

HYPOTHETICAL AFTER-TAX VALUE ^{1,2,3,4,5}



INVESTMENT OVER 10-YEAR HOLD

(assuming hypothetical 10% compounded rate of return on both investments)



Investors may pay as little as **\$0** in capital gains on the next decade of investment returns ⁶

	Taxable Investment	Qualified OZone Fund
Original Capital Gain From Sale or Prior Investment	\$1,000,000	\$1,000,000
Tax Rate	20%	20%
Tax on Original Capital Gain	(\$200,000)	Deferred
Investable Amount	\$800,000	\$1,000,000
Compounded Hypothetical Annual Return	10%	10%
Appreciation Over 10 Years	\$2,074,994	\$2,593,742
Tax on Appreciation After 10 Years	(~\$254,999)	Eliminated
Long-Term Capital Gains Taxes Paid in 2027 on Original Capital Gain	\$0	(\$200,000) 20% of \$1,000,000
FINAL VALUE	\$1,819,995	\$2,393,742
DIFFERENCE (QOZ VS. NON-QOZ)	\$573,747 in favor of the QOZ Fund	

1. This illustration assumes the investor is subject to the top marginal U.S. federal long-term capital gains rate of 20%, with no additional net investment income tax or state tax, for a total assumed tax liability of 20%.

2. No brokerage, advisory, or additional transactional fees are included in the non-QOF example.

3. Assumes the QOF investor resides in a state that fully conforms to the federal QOZ provisions.

4. Assumes the investor has no capital losses available to offset the gain, and that the original invested capital gains are includible in the investor's taxable income by December 31, 2026.

5. This illustration assumes investment under the pre-2027 Opportunity Zone rules. Future investments under OBBBA (2027 +) may have different deferral and step-up timelines.

6. Depending on an investor's individual tax situation and the assumptions listed below, some investors could pay as little as \$0 in federal capital gains tax on a hypothetical next decade of investment returns. Assumptions (illustrative only): investments are held long-term (qualifying for long-term capital gains), no taxable events occur during the period, current federal tax law remains unchanged, and any gains are offset by allowable losses or exclusions. This is a hypothetical example, not a promise or projection of results; your tax liability will vary. Consult your tax advisor for advice specific to your circumstances.

Why NOW Is a Great Time to Invest in an OZone

OZone '1.0' (Current Version-TCJA 2017))

- **Permanent as of OBBBA**
- **Tax deferral:** If you invest eligible gains within 180 days, you may be eligible to defer recognition of tax on those gains until the earlier of a subsequent sale or December 31, 2026.
 - At recognition,
 - The "lesser-of" rule applies
 - Tax the lesser of deferred gain, or
 - FMV minus adjusted basis as of 12.31.2026.
- **Appreciation exclusion:** If you hold the investment for at least 10 years and satisfy applicable requirements, you may be eligible for a step-up in tax basis to fair market value on sale, which could reduce future taxable capital gains.



OZone '2.0' (Effective Jan. 1, 2027)

- Rather than a single deferral deadline, gains invested in QOF after January 1, 2027, are **deferred on a rolling basis and recognized either upon disposition or five years after the investment.**
- **Investors receive a 10% basis increase at the five-year mark.**
 - Investing through a Enhanced Rural Incentives via Qualified Rural Opportunity Funds (QROFs), which channels at least 90% of its assets into rural OZs, earns investors a 30% basis step-up at year five.
- In rural zones, the substantial-improvement threshold is reduced to 50% of basis rather than 100%
- Stricter Eligibility and Expanded Transparency - designation criteria are tightened

The Hidden Gem is Within The Tax Levers

Tax Lever 1)

The "Lesser Of" Rule: The J-Curve Advantage

Your deferred gain becomes taxable either when you sell your Qualified Opportunity Fund (QOF) investment or on December 31, 2026, whichever occurs first. The IRS requires you to recognize only the lesser of:

- **Your original deferred gain, or**
- **The QOF's fair market value at that time minus your basis.**
- **This "lesser of" rule acts as a tax safety net.** In a **J-curve scenario** (where early years show lower or negative returns), if your investment is still below its original deferred gain when values dip, you won't be taxed on more than it's worth. If it has grown above the deferred gain, your recognition is capped at the lower amount.

Tax Lever 2)

The Pass-Through Entity: Timeline Extension

If you realized eligible gain through a partnership or S-corporation and received a Schedule K-1 (*pass-through entity*), you may leverage timing flexibility for your 180-day reinvestment window. Rather than starting the 180-day clock from the date of the underlying asset's sale, you may choose:

- **180 days beginning on the last day of the pass-through's taxable year, or**
- **180 days beginning on the pass-through's tax-return due date (without extensions).**
- **This extended starting point gives investors using pass-through vehicles more runway for due diligence and investment planning before committing to a QOF.**

How the “J-Curve” Works in Opportunity Zone Investing

QOZ Can Give You Two Main Tax Benefits

1) Tax Deferral: If you invest eligible capital gains into a qualifying fund (a Qualified Opportunity Fund or QOF) in time, you can delay paying taxes on those gains. When you do pay, you'll pay tax on the **lesser of** (a) your original deferred gain or (b) the fund's fair market value minus your basis, which gives some protection against downside risk.

2) Basis Step-Up: If you hold the investment long enough and meet the rules, your basis can increase, which means less taxable gain when you sell. *(For example, under the original program, you could hold it for 10 years and reset your basis to a fair market value.)*

These two features work together: one helps protect you if things don't go well, and the other helps you capture upside if things go right. Being aware of both is key when planning a QOZ investment.

How The ‘J-Curve’ Fits Into All of This

The J-Curve describes how investments often dip early before rebounding over time, creating a “J” shaped return pattern. In Opportunity Zones, this downward trend in early years can work to investors' advantage, where a lower fair market value paired with a basis step-up shrinks your taxable exposure.

As the **asset recovers and gains value**, your **tax basis has already increased**, so the recovery phase delivers gains more efficiently. In certain circumstances, market underperformance may create tax-planning opportunities that can be considered alongside QOZ strategies; however, tax outcomes are not guaranteed and depend on each investor's facts, timing, and applicable law.

In short, the J-Curve isn't just about weathering early volatility; it's a built-in leverage mechanism for savvy OZ investors.





If you have any questions about Opportunity Zones, feel free to reach out to our team.

Set up a 15-Minute Discovery Call at:

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Institutional-grade properties generally refer to a property of sufficient size and stature to merit attention from large national or international investors, and typically have the characteristic of high-quality assets in major markets and at price points beyond the reach of individual investors and smaller partnerships.

The hypothetical examples are for illustration purposes only. Individual results may vary.

Certain Qualified Opportunity Zone (QOZ) areas may not be able to appreciate as predictably as more established areas. Some neighborhoods may be more accommodating to development than others, impacting the success of the investment. Development and redevelopment of real estate traditionally have more risk than other types of real estate strategies. The availability and cost of construction and development financing is uncertain and represents a risk inherent in the execution of a QOF strategy. The rules and regulations of the QOZ Program are complex, compliance with the QOZ Program comes with significant challenges. QOFs tend to be illiquid investments for ten or more years. Any discussion regarding "Qualified Opportunity Zones" — including the viability of recycling proceeds from a sale or buyout — is based on advice received regarding the interpretation of provisions of the Tax Cut and Jobs Act of 2017 (the "Jobs Act") and relevant guidance's, including, among other things, two sets of proposed regulations and the final regulations issued by the IRS and Treasury Department in December of 2019. A number of unanswered questions still exist, and various uncertainties remain as to the interpretation of the Jobs Act and the rules related to Opportunity Zones investments. We cannot predict what impact, if any.

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