Tax Insights
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Tax Services

Enhanced and permanent Opportunity Zones as part of the One Big Beautiful Bill Act

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In brief

What happened?

On July 4, 2025, President Trump signed Public Law No: 119-21, the One Big Beautiful Bill Act (the Act) into law. Among other provisions, the Act permanently extends the opportunity zone (OZ) program with certain modifications and enhancements. Without these modifications, investments in OZs after December 31, 2026 would have no longer been eligible for OZ tax benefits.

Why is it important

The revisions to the OZ program aim to address some of the issues raised by policymakers by narrowing the scope of census tracts that are eligible to be nominated as OZs, as well as providing increased tax benefits for investment in rural areas. The Act also introduces new information reporting requirements for qualified opportunity funds (QOFs) and qualified opportunity zone businesses (QOZBs), along with penalties for failure to comply with these new requirements.

Actions to consider

Business leaders should evaluate the effect of the revisions to and expansion of the OZ program in the Act to determine how they affect current and future projects. Assessing the effects of the tax law changes will need to include not only the federal tax changes but should take into account any state tax, tax accounting and other related implications.

In detail

Overview

First enacted as part of the 2017 Tax Cuts & Jobs Act (TCJA), the OZ program was introduced with the intent to promote investments in certain economically distressed communities by allowing investors to defer taxes on capital gains (with the potential to fully exclude any future capital gains on exit). Through the program, investors can inject capital into low-income communities and promote long-term economic growth through a variety of investment vehicles known as QOFs. The OZ program has received broad bipartisan support while also drawing criticism around its implementation and effectiveness.

Investors also were eligible for significant tax benefits that included tax deferral for capital gains invested in a QOF; elimination of up to 15 percent of the tax on the capital gain that is invested in a QOF; and potential full elimination of tax when exiting a QOF investment after 10 years.

The revisions to the OZ program narrow the scope of census tracts that are eligible to be nominated as OZs, as well as providing increased tax benefits for investment in rural areas. The Act also introduces new information reporting requirements for QOFs and QOZBs, along with penalties for failure to comply with these new requirements.

The Act modifies the existing tax deferral benefits for potential investors in QOFs. For example, eligible capital gains invested into a QOF after December 31, 2026, will be subject to a rolling five-year deferral period, rather than a fixed date. The Act also removes the seven-year basis increase which was part of the original OZ program. The ten-year gain exclusion benefit and five-year basis increase remain largely unchanged (with an additional basis increase for investments in rural areas).

The designation period for the first set of new OZs will begin on July 1, 2026, with additional rounds of designations to follow every ten years thereafter. New designations will become effective as of January 1, 2027, and will remain in effect for a similar ten-year period.

Highlights of the changes to the OZ program

Permanent extension

As enacted under the TCJA, the original OZ program was effectively set to expire for new contributions on December 31, 2026, the date on which originally deferred capital gains would need to be included in taxable income. While OZ designations would have remained in effect until 2028, and investors who contributed eligible capital gains to QOFs prior to December 31, 2026 would still be eligible for the ten-year gain exclusion benefit on exit, investments after December 31, 2026 (potentially up to September 11, 2027 for certain eligible gains from pass-through investments) would no longer have been eligible for any of the OZ tax benefits.

The Act provides for new OZ designations every ten years. The determination of new designations will begin on July 1 (the "decennial determination date," the first of which is to occur on July 1, 2026) and become effective on the following January 1 (the "applicable start date," January 1, 2027 for the first set of new designations). Each state governor has 90 days from the decennial determination date to submit OZ nominations to the Treasury Secretary, consistent with the original program, and may request a 30-day extension.

Zone restrictions and changes

In addition to permanently extending the OZ program, the Act further restricts which census tracts may be eligible for designation.

In order for a census tract to be eligible for designation as an OZ under the TCJA OZ rules, a tract needed to meet the definition of a "low-income community" as defined under the new markets tax credit (NMTC) program, i.e., the tract needed to have a poverty rate of at least 20 percent or the median family income within the tract could not exceed 80 percent of statewide (or metropolitan area if located within such an area) median family income.

The Act separates the definition of low-income community from NMTC program by applying the following changes:

- The poverty rate within the tract is at least 20 percent *and* the median family income does not exceed 125 percent of median family income within the relevant area, or;
- The median family income within the tract does not exceed 70 percent of median family income within the relevant area.

Observation: The updated definition of low-income community is expected to decrease the number of census tracts available for OZ nomination. This will reduce the number of OZs as each state may designate no more than 25 percent of the number of low-income communities in that state. Note that if the number of low-income communities within a state is less than 100, a total of 25 tracts can be designated as OZs.

Observation: Investors and QOF sponsors should work with their local governments to nominate census tracts in areas they believe deserve consideration.

Observation: Certain census tracts designated as OZs under the TCJA OZ rules, by nature of the Act changes, may no longer qualify for designation under the new rules. QOFs formed prior to January 1, 2027 will need to ensure any post-2026 acquisitions fall within the new set of tracts. Treasury may need to issue transition rules for acquisitions in census tracts that may no longer qualify.

The previous rule designating all low-income communities of Puerto Rico as OZs has been repealed effective December 31, 2026. Puerto Rico and other US territories will continue to be eligible to nominate census tracts under the new rules.

The previous rule permitting certain census tracts contiguous to low-income communities to be nominated as OZs has been repealed.

Observation: One of the primary criticisms of the OZ program focused on the initial designation of tracts, especially those that were not themselves low-income communities. The removal of contiguous tracts as well as the tightening of the requirements may address some of these concerns.

Modification of tax benefits

Under the TCJA OZ rules, the tax benefits for investors in QOFs were threefold:

1. Deferral of tax on eligible capital gains until December 31, 2026;
2. Elimination of 15 percent of tax on eligible capital gains for investments held for at least seven years and 10 percent for investments held for at least five years;

3. Exclusion of tax on capital gains upon the sale or disposal of an interest in a QOF (or its underlying investments) when held for at least ten years.

The Act amends the OZ incentives, modifying each of these tax benefits for investments made after December 31, 2026 as follows:

1. The deferral period is modified from a fixed date to a rolling five years from the initial date of investment into a QOF.

2. The additional 5 percent basis increase for investments held for at least seven years is repealed; the 10 percent basis increase for investments held for at least five years remains unchanged (except for investments in qualified rural opportunity funds, discussed below).

3. For investments held longer than thirty years, the fair market value for purposes of an election made under Section 1400Z-2(c) is locked into the fair market value as of thirty years from the initial date of investment into a QOF.

Observation: Under the TCJA OZ rules, investments in QOFs made after December 31, 2021 did not qualify for any of the eliminations of tax on originally deferred capital gains. By changing the deferral period from a fixed date to a rolling period for investments made after December 31, 2026, investors in QOFs will ultimately be eligible for the full suite of tax benefits under the new rules so long as they hold their investments for the relevant period, without regard to when they make their investment.

Observation: Investors and QOF sponsors will need to pay close attention to states with specific-date conformity, states with rolling conformity and states that have decoupled from the OZ program. A number of states, including New York and California, do not conform in part or in whole with the OZ program.

Qualified rural opportunity funds

To further drive investment towards specific low-income communities, the Act introduces a new concept of “qualified rural opportunity funds” (QROFs). A QROF is a QOF of which at least 90 percent of its assets consist of qualified OZ property located within OZs composed entirely of a “rural area.” Rural areas are further defined to mean any area other than (a) a city or town with a population of greater than 50,000 inhabitants, or (b) any urbanized area contiguous to such a city or town.

Observation: Treasury will have to determine which census tracts qualify as a “rural area.” It is unclear what data Treasury will use to determine eligibility.

Investments in QROFs are eligible for additional tax benefits in order to make investment in rural areas more attractive. For investors in QROFs, the basis step-up for investments held for at least five years increases to 30 percent from 10 percent.

Additionally, qualified OZ business property that is not original use property must only be substantially improved by an amount equal to 50 percent of the adjusted basis (as opposed to 100 percent for property acquired in non-rural OZs).

Observation: The introduction of QROFs, along with the significant increase in tax benefits for investment in QROFs, indicates Congress’ intent to utilize the OZ program to drive economic growth in rural areas.

Observation: QOF sponsors may seek to adjust investment strategies and offer both QOF and QROF products to investors in order to meet market demands for QROFs due to their added tax benefits.

Observation: Reducing the substantial improvement threshold from 100 percent to 50 percent may help many rural based QOZBs receive capital.

Increased reporting requirements and penalties

Under the TCJA OZ rules, QOFs are required to file Form 8996 - Qualified Opportunity Fund with their federal income tax return in order to report their ability to maintain the 90 percent investment standard for QOFs. This reporting is fairly limited in scope, including only the value of the QOF's investment, the value of tangible property directly or indirectly owned or leased, the OZ tract in which such property is located, and the taxpayer identification number of any qualified opportunity zone stock or partnership interests held.

The Act significantly expands the required reporting for both new and existing QOFs, QROFs and QOZBs. In addition to the information QOFs are already required to report, QOF and QROF reporting will now include:

- The name, address, and NAICS code of any qualified opportunity zone stock or partnership interest held;
- The approximate number of residential units (if any) for any real property investments, and;
- The approximate average monthly number of full-time equivalent employees (within identified ranges) or such other indication of the employment impact of its OZ investments.

QOFs and QROFs are also required to furnish statements to investors that dispose of their QOF interests during the year.

To the extent a QOF or QROF does not comply with the new reporting requirements, it will be subject to penalties. QOFs and QROFs who fail to comply will incur penalties, subject to inflation adjustments, of $500 per day and capped at $10,000 ($50,000 for large QOFs or QROFs with gross assets in excess of $10,000,000). Penalties are further increased for instances of intentional disregard.

QOFs, QROFs, and QOZBs will also be subject to penalties for failing to provide the required statements to their respective investors.

Observation: The new OZ reporting requirements in the Act are similar to bills introduced in previous congressional sessions such as the "OZ Transparency Extension and Improvement Act."

Observation: The economic impact of the OZ program has been a key focus of attention from critics. The new reporting requirements seek to provide more detailed information around OZ investment and how it drives economic growth. The Secretary of the Treasury also will now be required to issue annual reports on QOFs and QROFs based on the information provided.

Observation: QOF, QROF, and QOZB sponsors will need to determine how best to collect the relevant information, which previously would not have been subject to reporting, as more details on the requirements are made available. While QOZBs would typically report certain information about tangible property value to their QOF owners, this was not previously a codified requirement subject to penalties for failure to provide.

Observation: As part of the Act, the IRS and Treasury were appropriated $15 million to administer the reporting requirements and also make publicly available a report with the information obtained from QOFs, QROFs and QOZBs.

What didn't make it into the Act

A number of proposed changes to the OZ program were offered in earlier House or Senate versions of the legislation. The following proposals were ultimately excluded from the final Act approved by Congress and signed by President Trump:

- The House bill provided for a single temporary extension of the OZ program through 2033.
- The House bill permitted investments of ordinary income up to $10,000 to qualify for OZ tax benefits.
- The House bill required a minimum number of rural areas to be designated as OZs.
- An earlier draft of the Senate version of the Act retained fixed gain recognition dates tied to the seventh year of the designation period.
- An earlier draft of the Senate version of the Act spread the 10 percent basis increase (30 percent for investments in QROFs) over a six-year period with annual increases.

Let's talk

For a deeper discussion on how OZs may affect your business, please contact:

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