Reg. Section 1.1400Z2(a)-1(c)(9)

Deferring tax on capital gains by investing in opportunity zones

. . .

(c) Operational and special rules.

(1)Attributes of gains included in income under section 1400Z-2(a)(1)(B). If section 1400Z-2(a)(1)(B), section 1400Z-2(b), and the section 1400Z-2 regulations require a taxpayer to include in income some or all of a previously deferred gain, the rules of paragraphs (c)(1)(i) and (ii) of this section apply with respect to such gain.

(i) Deferral year attributes. The gain so included per paragraph (c)(1) of this section has the same attributes in the taxable year of inclusion that the gain would have had if recognition of the gain had not been deferred under section 1400Z-2(a)(1)(A). These attributes include those taken into account by sections 1(h), 1222, 1231(b), 1256, and any other applicable provisions of the Code.

(ii) Inclusion year treatment. The gain so included per paragraph (c)(1) of this section is subject to the same Federal income tax provisions and rates that would apply to any other gains that are realized and recognized at the same time as the included gain and that have the same attributes as the deferred gain. For example, when a deferred qualified 1231 gain, as defined in paragraph (b)(11)(iii) of this section, is required to be included in income, the included section 1231 gain is treated as if it were a section 1231 gain (within the meaning of section 1231(a)(3)(A)) that was recognized on the date of inclusion.

(iii) Rules for associating included gain with deferred gains.

(A) In general. For purposes of paragraphs (c)(1)(i) and (ii) of this section, a taxpayer determines which previously deferred gain is associated with a qualifying investment in accordance with guidance published in the Internal Revenue Bulletin or in forms and instructions (see §§601.601(d)(2) and 601.602 of this chapter). The rules of paragraphs (c)(1)(iii)(B) and (C) of this section apply only to the extent a deferred gain is not clearly associated with a particular qualifying investment under this paragraph (c)(1)(iii)(A).

(B) Only one eligible gain associated with a deferral election. If only one eligible gain could have been deferred with respect to a qualifying investment, that deferred gain is associated with that qualifying investment. For example, if an eligible taxpayer makes a deferral election with respect to an investment in a QOF and only one eligible gain of the taxpayer satisfies the 180-day period with respect to the investment in the

QOF, that eligible gain is the gain deferred with respect to the qualifying investment for purposes of paragraphs (c)(1)(i) and (ii) of this section.

(C) Multiple eligible gains associated with a deferral election.

(1) In general. If more than one eligible gain may have been deferred with respect to an investment in a QOF for which a deferral election has been made, then for purposes of paragraphs (c)(1)(i) and (ii) of this section, the eligible taxpayer is treated as making the investment in the QOF first with respect to the earliest realized eligible gain, followed by the next earliest eligible gain and any other eligible gains in order of the date of their realization.

(2) Rule for gains realized on the same day. If in the application of paragraph (c)(1)(iii)(C)(1) of this section, two eligible gains are realized on the same day, such gains are allocated to the investment in the QOF proportionately.

(2)Identification of which interest in a QOF corporation has been disposed of.

(i) Need for identification. If a taxpayer holds shares of QOF stock with identical rights (fungible interests), and if the taxpayer disposes of less than all of the fungible interests, it is necessary to identify which interest or interests were disposed of. A taxpayer may effect this identification in accordance with the rules and principles of §1.1012-1(c). Consistent with §1.1012-1(c), if a taxpayer does not adequately identify which of the fungible interests are disposed of, the first-in, first-out identification method (FIFO method) applies.

(ii) Consequences of identification. The identification determines-

(A) Whether an investment disposed of is a qualifying investment or a non-qualifying investment; and

(B) In the case of qualifying investments-

(1) The attributes of the gain addressed in paragraph (c)(1) of this section; and

(2) The extent, if any, of an increase under section 1400Z-2(b)(2)(B) in the basis of an investment interest that is disposed of.

(3)Pro-rata method. If, after application of the FIFO method, a taxpayer is treated as having disposed of less than all of the investment interests that the taxpayer acquired on one day, and if the interests acquired on that day vary with respect to the characteristics described in paragraph (c)(2)(ii) of this section, then a proportionate allocation must be made to determine which interests were disposed of (pro-rata method).

(4)Examples. The following examples illustrate the rules of paragraph (c)(1) through (3) of this section.

(i)

Example (1). Short-term gain. For 2018, taxpayer B properly made an election under section 1400Z-2 to defer $100 of eligible gain that, if not deferred, would have been recognized as short-term capital gain, as defined in section 1222(1). In 2022, sections 1400Z-2(a)(1)(B) and (b) require taxpayer B to include the gain in gross income. Under paragraph (c)(1) of this section, the gain included in 2022 is short-term capital gain.

(ii)
Example (2). Collectibles gain. For 2018, taxpayer C properly made an election under section 1400Z-2 to defer a gain that, if not deferred, would have been collectibles gain as defined in section 1(h)(5). In a later taxable year, section 1400Z-2(a)(1)(B) and (b) requires some or all of that deferred gain to be included in gross income. The gain included is collectibles gain.

(iii)
Example (3). Net capital gain from section 1256 contracts. For 2019, taxpayer D had $100 of net capital gain realized from section 1256 contracts that is eligible gain under paragraph (b)(11)(vi)(B) of this section. D timely invested $100 in a QOF and properly made an election under section 1400Z-2 to defer that $100 of gain. In 2023, section 1400Z-2(a)(1)(B) and (b) requires D to include that deferred gain in gross income. Under paragraph (c)(1) of this section, the character of the inclusion is governed by section 1256(a)(3), which requires a 40:60 split between short-term and long-term capital gain. Accordingly, $40 of the inclusion is short-term capital gain and $60 of the inclusion is long-term capital gain.

(iv)
Example (4). FIFO method. For 2018, taxpayer E properly made an election under section 1400Z-2 to defer $300 of short-term capital gain. For 2020, E properly made a second election under section 1400Z-2 to defer $200 of long-term capital gain. In both cases, E properly invested in QOF corporation Q the amount of the gain to be deferred, resulting in a total investment in Q of $500. The two investments are fungible interests and the price of the interests was the same at the time of the two investments. E did not purchase any additional interest in Q or sell any of its interest in Q until 2024, when E sold for a gain 60 percent of its interest in Q. E did not adequately identify which investment in QOF Q E sold. Under paragraph (c)(2)(i) of this section, E must apply the FIFO method to identify which investments in Q that E disposed of. 60

percent of E's total investment in Q is $300 (60% x $500), thus under the FIFO method, E sold its entire 2018 initial investment of $300 in Q. Under section 1400Z-2(a)(1)(B) and (b), the sale triggered an inclusion of deferred gain. Because the inclusion has the same character as the gain that had been deferred, the inclusion is short-term capital gain.

(v)
Example (5). FIFO method. In 2018, before Corporation R became a QOF, Taxpayer F invested $100 to R in exchange for 100 R common shares. Later in 2018, after R was a QOF, F invested $500 to R in exchange for 400 R common shares and properly elected under section 1400Z-2 to defer $500 of realized short-term capital gain from a separate investment. Even later in 2018, on different days, F realized $300 of short-term capital gain and $700 of long-term capital gain. On a single day that fell during the 180-day period for both of those gains, F invested $1,000 in R in exchange for 800 R common shares and properly elected under section 1400Z-2 to defer the two gains. In 2020, F sold 100 R common shares. F did not adequately identify which investment in R F sold. Under paragraph (c)(2)(i) of this section, F must apply the FIFO method to identify which investments in R F disposed of. As determined by that identification, F sold the initially acquired 100 R common shares, which were not part of a deferral election under section 1400Z-2. R must recognize gain or loss on the sale of its R shares under the generally applicable Federal income tax rules, but the sale does not trigger an inclusion of any deferred gain.

(vi)
Example (6). FIFO method. The facts are the same as in paragraph (c)(4)(v) of this section (Example 5), except that, in addition, during 2021 F sold an additional 400 R common shares, and, as with the other sale, F did not adequately identify which investment in QOF R F sold. Under paragraph (c)(2)(i) of this section, F must apply the FIFO method to identify which investments in R were disposed of. As determined by this identification, F sold the 400 common shares which were associated with the deferral of $500 of short-term capital gain. Thus, the deferred gain that must be included upon sale of the 400 R common shares is short-term capital gain.

(vii)
Example (7). Pro-rata method. The facts are the same as in examples 5 and 6, except that, in addition, during 2022 F

sold an additional 400 R common shares. Under paragraph (c)(2)(i) of this section, F must apply the FIFO method to identify which investments in R were disposed of. In 2022, F is treated as holding only the 800 R common shares purchased on a single day, and the section 1400Z-2 deferral election associated with these shares applies to gain with different characteristics (described in paragraph (c)(2)(ii) of this section). Under paragraph (c)(3) of this section, therefore, R must use the pro-rata method to determine which of the characteristics pertain to the deferred gain required to be included as a result of the sale of the 400 R common shares. Under the pro-rata method, $150 of the inclusion is short-term capital gain ($300 x 400/800) and $350 is long-term capital gain ($700 x 400/800).

(5)Making an investment for purposes of an election under section 1400Z-2(a).

(i) Transfer of cash or other property to a QOF. A taxpayer makes an investment in a QOF by transferring cash or other property to a QOF in exchange for eligible interests in the QOF, regardless of whether the transfer is one in which the transferor would recognize gain or loss on the property transferred.

(ii) Furnishing services. Rendering services to a QOF is not a transfer of cash or other property to a QOF. Thus, if a taxpayer receives an eligible interest in a QOF for services rendered to the QOF or to a person in which the QOF holds any direct or indirect equity interest, then the interest in the QOF that the taxpayer receives is a non-qualifying investment.

(iii) Acquisition of eligible interest from person other than QOF. An eligible taxpayer may make an investment in a QOF by acquiring an eligible interest in a QOF from a person other than the QOF, provided that all of the requirements of section 1400Z-2(a)(1) and the section 1400Z-2 regulations for making a valid deferral election with respect to that investment are otherwise satisfied with respect to such acquisition. For example, an eligible taxpayer who acquires an eligible interest in a QOF other than from the QOF also must have an eligible gain within the 180-day period prior to the eligible taxpayer's acquisition of the eligible interest in the QOF.

(6)Amount invested for purposes of section 1400Z-2(a)(1)(A).

(i) In general. In the case of any investments described in this paragraph (c)(6), the amount of a taxpayer's qualifying investment cannot exceed the amount of eligible gain to be deferred under the deferral election. If the amount of an otherwise qualifying investment exceeds the amount of eligible gain to be deferred under the deferral election, the amount of the excess is treated as a non-qualifying investment. See paragraph (c)(6)(iii) of this section for special rules applicable to transfers to QOF partnerships.

(ii) Transfers to a QOF.

(A) Cash. If a taxpayer makes an investment in a QOF by transferring cash to a QOF, the amount of the taxpayer's investment is that amount of cash.

(B) Property other than cash-Nonrecognition transactions. This paragraph (c)(6)(ii)(B) applies if a taxpayer makes an investment in a QOF by transferring property other than cash to a QOF and if, but for the application of section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations, the taxpayer's basis in the resulting investment in the QOF would be determined, in whole or in part, by reference to the taxpayer's basis in the transferred property. This paragraph (c)(6)(ii)(B) applies separately to each item of property transferred to a QOF.

(1) Amount of qualifying investment. If paragraph (c)(6)(ii)(B) of this section applies, the amount of the taxpayer's qualifying investment is the lesser of the taxpayer's adjusted basis in the eligible interest received in the transaction, without regard to section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations, or the fair market value of the eligible interest received in the transaction, both determined immediately after the transfer.

(2) Fair market value of the eligible interest received exceeds its adjusted basis. If paragraph (c)(6)(ii)(B) of this section applies, and if the fair market value of the eligible interest received is in excess of the eligible taxpayer's adjusted basis in the eligible interest received, without regard to section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations, then the eligible taxpayer's investment in a QOF is a mixed-funds investment to which section 1400Z-2(e)(1) applies. In such a case, an amount equal to the adjusted basis of the eligible interest in the hands of the eligible taxpayer is the eligible taxpayer's qualifying investment, and the excess is the eligible taxpayer's non-qualifying investment.

(3) Transfer of built-in loss property and section 362(e)(2). If paragraph (c)(6)(ii)(B) of this section and section 362(e)(2) both apply to a transaction, the eligible taxpayer and the QOF are deemed to have made an election under section 362(e)(2)(C).

(C) Property other than cash-Taxable transactions. This paragraph (c)(6)(ii)(C) applies if an eligible taxpayer makes an investment in a QOF by transferring property other than cash to a QOF and if, without regard to section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations, the eligible taxpayer's basis in the eligible interest received would not be determined, in whole or in part, by reference to the eligible taxpayer's basis in the transferred property. If this paragraph (c)(6)(ii)(C) applies, the amount of the eligible taxpayer's investment in a QOF is the fair market value of the transferred property, as determined immediately before the transfer. This paragraph (c)(6)(ii)(C) applies separately to each item of property transferred to a QOF.

(D) Basis in a mixed-funds investment. If a taxpayer's investment in a QOF is a mixed-funds investment to which section 1400Z-2(e)(1) applies, the taxpayer's basis in the non-qualifying investment is equal to the

taxpayer's basis in all of the eligible interests received, determined without regard to section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations, and reduced by the basis of the taxpayer's qualifying investment, determined without regard to section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations.

(iii) Special rules for transfers to QOF partnerships. In the case of an investment in a QOF partnership, the following rules apply:

(A) Amounts not treated as a qualifying investment.

(1) Non-contributions in general. To the extent the transfer of property to a QOF partnership is characterized other than as a contribution, such as characterization as a sale under section 707 and the regulations in this part under section 707 of the Code, the transfer is not treated as being made in exchange for a qualifying investment.

(2) Reductions in investments otherwise treated as contributions. If any transfer of cash or other property to a partnership is not treated as a contribution, in whole or in part, under paragraph (c)(6)(iii)(A)(1) of this section, the part of the transfer to the partnership that is not disregarded is not a qualifying investment to the extent the partnership makes a distribution to the partner and the transfer to the partnership and the distribution would be recharacterized as a disguised sale under section 707 and the regulations in this part under section 707 of the Code if:

(i) Any cash contributed were non-cash property; and

(ii) In the case of a distribution by the partnership to which §1.707-5(b) (relating to debt-financed distributions) applies, the partner's share of liabilities is zero.

(B) Amount invested in a QOF partnership.

(1) Calculation of amount of qualifying and non-qualifying investments. To the extent paragraph (c)(6)(iii)(A) of this section does not apply, the amount of equity received by an eligible taxpayer in a QOF partnership in exchange for the lesser of the net basis or net value of the property contributed to the QOF partnership by the eligible taxpayer is a qualifying investment. The amount of equity received by an eligible taxpayer in a QOF partnership that is a non-qualifying investment is the excess, if any, of the total equity received by the eligible taxpayer over the amount treated as a qualifying investment.

(2) Net basis. For purposes of paragraph (c)(6)(iii)(B) of this section, net basis is the excess, if any, of-

(i) The adjusted basis of the property contributed to the partnership; over

(ii) The amount of any debt to which the property is subject or that is assumed by the partnership in the transaction.

(3) Net value. For purposes of paragraph (c)(6)(iii)(B) of this section, net value is the excess of-

(i) The gross fair market value of the property contributed to the partnership; over

(ii) The amount of the debt described in paragraph (c)(6)(iii)(B)(2)(ii) of this section.

(4) Basis of qualifying and non-qualifying investments. The initial basis of a qualifying investment, before application of section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations or any section 752 debt allocation, is the net basis of the property contributed. The basis of a non-qualifying investment, before any section 752 debt allocation, is the remaining net basis. The basis of the qualifying investment is adjusted as provided in section 1400Z-2(b)(2)(B) and the section 1400Z-2 regulations. The bases of qualifying and non-qualifying investments are increased by any debt allocated to those investments under the rules of §1.1400Z2(b)-1(c)(6)(iv)(B).

(5) Rules applicable to mixed-funds investments. If one portion of an investment in a QOF partnership is a qualifying investment and another portion is a non-qualifying investment, see §1.1400Z2(b)-1(c)(6)(iv) for the rules that apply.

(iv) Acquisitions from another person. An eligible taxpayer may make an investment in a QOF by acquiring in a sale or exchange to which §1.1001-1(a) applies an eligible interest in a QOF from a person other than the QOF. The amount of the eligible taxpayer's investment in the QOF with respect to which the eligible taxpayer may make a deferral election is the amount of the cash, or the net fair market value of the other property, as determined immediately before the exchange, that the eligible taxpayer exchanged for the eligible interest in the QOF.

(v) Examples. The following examples illustrate the rules of this paragraph (c)(6).
(A)
Example (1). Transfer of built-in gain property with basis less than gain to be deferred.
(1) Facts. Individual B realizes $100 of eligible gain within the meaning of paragraph (b)(11) of this section. B transfers unencumbered property with a fair market value of $100 and an adjusted basis of $60 to QOF Q, a C corporation, in a transaction that is described in section 351(a).
(2) Analysis. Paragraph (c)(6)(ii)(B) of this section applies because B transferred property other than cash to Q and, but for the application of section 1400Z-2(b)(2)(B), B's basis in the eligible interests in Q would be determined, in whole or in part, by reference to B's basis in the transferred property. The fair market

value of the eligible interest B received is $100, and, without regard to section 1400Z-2(b)(2)(B), B's basis in the eligible interest received would be $60. Thus, pursuant to paragraph (c)(6)(ii)(B)(2) of this section, B's investment is a mixed-funds investment to which section 1400Z-2(e)(1) applies. Pursuant to paragraphs (c)(6)(ii)(B)(1) and (2) of this section, B's qualifying investment is $60 (the lesser of the taxpayer's adjusted basis in the eligible interest, without regard to section 1400Z-2(b)(2)(B), of $60 and the $100 fair market value of the eligible interest received). Pursuant to section 1400Z-2(b)(2)(B)(i), B's basis in the qualifying investment is $0. Additionally, B's non-qualifying investment is $40 (the excess of the fair market value of the eligible interest received ($100) over the taxpayer's adjusted basis in the eligible interest, without regard to section 1400Z-2(b)(2)(B) ($60)). B's basis in the non-qualifying investment is $0 (B's $60 basis in its investment determined without regard to section 1400Z-2(b)(2)(B), reduced by the $60 of adjusted basis allocated to the investment to which section 1400Z-2(e)(1)(A)(i) applies, determined without regard to section 1400Z-2(b)(2)(B)). See paragraph (c)(6)(ii)(D) of this section. Pursuant to section 362, Q's basis in the transferred property is $60.

(B)
Example (2). Transfer of built-in gain property with basis in excess of eligible gain to be deferred. The facts are the same as in paragraph (c)(6)(v)(A)(1) of this section (Example 1), except that B realizes $50 of eligible gain within the meaning of paragraph (b)(11) of this section. Pursuant to paragraph (c)(6)(i) of this section, B's qualifying investment cannot exceed the amount of eligible gain to be deferred (that is, the $50 of eligible gain) under the section 1400Z-2(a) election. Therefore, pursuant to paragraph (c)(6)(ii)(B)(1) of this section, B's qualifying investment is $50 (the lesser of the taxpayer's adjusted basis in the eligible interest received, without regard to section 1400Z-2(b)(2)(B), of $60 and the $100 fair market value of the eligible interest, limited by the amount of eligible gain to be deferred under the section 1400Z-2(a) election). B's qualifying investment has an adjusted basis of $0, as provided in section 1400Z-2(b)(2)(B)(i). Additionally, B's non-qualifying investment is $50 (the excess of the fair market value of the eligible interest received ($100) over the amount ($50) of B's section 1400Z-2(a)(1)(A) investment). B's basis in the non-qualifying investment is $10 (B's $60 basis in its investment determined without regard to section 1400Z-2(b)(2)(B)), reduced by the $50 of adjusted basis allocated to B's qualifying investment, determined without regard to section 1400Z-2(b)(2)(B).

(C)
Example (3). Transfers to QOF partnerships.
(1) Facts. A and B each realized $100 of eligible gain and each transfers $100 to a QOF partnership. In a subsequent year, the partnership borrows $120 from an unrelated lender and distributes $120 equally to A and B.
(2) Analysis. If the contributions had been of property other than cash, the contributions and distributions would have been tested under the disguised sale rules of section 707 and the regulations in this part under section 707 of the Code, determining the timing of the distribution and amount of the debt allocated to each partner. Under paragraph (c)(6)(iii)(A)(2) of this section, the cash of $200 ($100 from A and $100 from B) is treated as property that could be sold in a

disguised sale transaction and each partner's share of the debt is zero for purposes of determining the amount of the qualifying investment. To the extent there would have been a disguised sale applying the rule of paragraph (c)(6)(iii)(A)(2) of this section, the amount of the qualifying investment would be reduced by the amount of the contribution so recharacterized.

(D)
Example (4). Return of capital by QOF partnership.
(1) Facts. A realized $100 of eligible gain and transfers $100 of cash to a QOF partnership. Later in the partner's tax year, the partnership distributes $20 to A in a distribution that is not recharacterized under paragraph (c)(6)(iii)(A)(2) of this section. At the time of the distribution, no allocations of income, gain, loss, or deduction had been made to A, and A's share of the partnership's debt was zero under section 752.
(2) Analysis. Because the contribution and distribution are not recharacterized under paragraph (c)(6)(iii)(A)(2) of this section, the amount of A's qualifying investment is $100 despite the $20 distribution. At the time the $20 distribution is made to A, A's basis in its qualifying investment is zero, and thus the distribution is an inclusion event under §1.1400Z2(b)-1(c)(6)(iii).

(E)
Example (5). Property contributed has built-in gain. The facts are the same as in paragraph (c)(6)(v)(C)(1) of this section (Example 3), except that the property contributed by A had a value of $100 and basis of $20 and the partnership did not borrow money or make a distribution. Under paragraph (c)(6)(iii)(B)(1) of this section, the amount of A's qualifying investment is $20 (the lesser of the net value or the net basis of the property that A contributed), and the excess of the $100 contribution over the $20 qualifying investment is a non-qualifying investment. Under paragraph (c)(6)(iii)(B)(4) of this section, A's basis in the qualifying investment (determined without regard to section 1400Z-2(b)(2)(B) or section 752(a)) is $20. After the application of section 1400Z-2(b)(2)(B) but before the application of section 752(a), A's basis in the qualifying investment is zero. A's basis in the non-qualifying investment is zero without regard to the application of section 752(a).

(F)
Example (6). Property contributed has built-in gain and is subject to debt. The facts are the same as in paragraph (c)(6)(v)(E) of this section (Example 5), except that the property contributed by A has a gross value of $130 and is subject to debt of $30. Under paragraph (c)(6)(iii)(B)(1) of this section, the amount of A's qualifying investment is zero, the lesser of the property's $100 net value ($130 minus $30) or $0 net basis ($20 minus $30, but limited to zero). The entire contribution constitutes a non-qualifying investment.

(G)
Example (7). Property contributed has built-in loss and is subject to debt. The facts are the same as in paragraph (c)(6)(v)(F) of this section (Example 6), except that the property contributed by A has a basis of $150. Under paragraph (c)(6)(iii)(B)(1) of this section, the amount of A's qualifying investment is $100,

the lesser of the property's $100 net value ($130 minus $30) or $120 net basis ($150 minus $30). The non-qualifying investment is $0, the excess of the net value ($100) over the qualifying investment ($100). A's basis in the qualifying investment (determined without regard to section 1400Z-2(b)(2)(B) and section 752(a)) is $120, the net basis. After the application of section 1400Z-2(b)(2)(B), A's basis in the qualifying investment is zero, plus its share of partnership debt under section 752(a).

(7)Eligible gains that a partnership elects to defer. A partnership generally is an eligible taxpayer under paragraph (b)(13) of this section and may elect to defer recognition of some or all of its eligible gains under section 1400Z-2(a)(2) and the section 1400Z-2 regulations.

(i) Partnership deferral election. If a partnership properly makes a deferral election, then-

(A) The partnership defers recognition of the eligible gain under the rules of section 1400Z-2 and the section 1400Z-2 regulations, that is, the partnership does not recognize gain at the time it otherwise would have in the absence of the deferral election; and

(B) The deferred eligible gain is not included in the distributive shares of the partners under section 702 and is not treated as an item described in section 705(a)(1).

(ii) Subsequent recognition. Absent any additional deferral under section 1400Z-2(a)(1)(A) and the section 1400Z-2 regulations, any amount of deferred gain that an electing partnership subsequently must include in income under sections 1400Z-2(a)(1)(B) and (b) and the section 1400Z-2 regulations is recognized by the electing partnership at the time of inclusion, is subject to section 702 and is treated as an item described in section 705(a)(1) in a manner consistent with recognition at that time.

(8)Eligible gains that the partnership does not defer.

(i) Federal income tax treatment of the partnership. If a partnership does not elect to defer some, or all, of its eligible gains, the partnership's treatment of any such amounts is unaffected by the fact that the eligible gains could have been deferred under section 1400Z-2 and the section 1400Z-2 regulations.

(ii) Federal income tax treatment by the partners. If a partnership does not elect to defer some, or all, of the eligible gains-

(A) The gains for which a deferral election are not made are included in the partners' distributive shares under section 702 and are treated as items described in section 705(a)(1);

(B) If a partner's distributive share includes one or more gains that are eligible gains with respect to the partner, the partner may elect under section 1400Z-2(a)(1)(A) and the section 1400Z-2 regulations to defer some or all of such eligible gains; and

(C) A gain in a partner's distributive share is an eligible gain with respect to the partner only if it is an eligible gain with respect to the partnership and it did not arise from a sale or exchange with a person that, within the meaning of section 1400Z-2(e)(2) and the section 1400Z-2 regulations, is related to the partner.

(iii) 180-day period for a partner electing deferral.

(A) General rule. If a partner's distributive share includes a gain that is described in paragraph (c)(8)(ii)(C) of this section (gains that are eligible gains with respect to the partner), the 180-day period with respect to the partner's eligible gains in the partner's distributive share generally begins on the last day of the partnership taxable year in which the partner's distributive share of the partnership's eligible gain is taken into account under section 706(a).

(B) Elective rule. Notwithstanding the general rule in paragraph (c)(8)(iii)(A) of this section, if a partnership does not elect to defer all of its eligible gain, the partner may elect to treat the partner's own 180-day period with respect to the partner's distributive share of that gain as being-

(1) The same as the partnership's 180-day period; or

(2) The 180-day period beginning on the due date for the partnership's tax return, without extensions, for the taxable year in which the partnership realized the gain that is described in paragraph (c)(8)(ii)(C) of this section.

(C) Example. The following example illustrates the principles of this paragraph (c)(8)(iii).

Example.

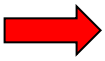
(1) Facts. Four individuals, A, B, C, and D, have equal interests in a partnership, P. P has no other partners, and P's taxable year is the calendar year. On January 17, 2019, P realizes a capital gain of $1000x that P decides not to elect to defer.

(2) Analysis of A's election. A is aware of the capital gain realized by P, and decides to defer its distributive shares of P's eligible gain. A invests $250x in a QOF during February 2020. Under the general rule in paragraph (c)(8)(iii)(A) of this section, this investment is within the 180-day period for A, which began on December 31, 2019, the last day of P's taxable year in which A's share of P's eligible gain is taken into account under section 706(a).

(3) Analysis of B's election. B is also aware of the capital gain realized by P, and decides to defer its distributive shares of P's eligible gain. B decides to make the election provided in paragraph (c)(8)(iii)(B)(1) of this section, and invests $250x in a QOF during February 2019. Under the elective rule in paragraph (c)(8)(iii)(B)(1) of this section, this investment is within the 180-day period for B, which began on January 17, 2019, the same day as P's 180-day period.

(4) Analysis of C's election. On March 15, 2020, P provides all of its partners with their Schedules K-1. Upon learning that its distributive share

of income from P included eligible gain, C decides to make a deferral election, and also makes the election provided in paragraph (c)(8)(iii)(B)(2) of this section. It then invests $250x in a QOF during June 2020. Under the elective rule in paragraph (c)(8)(iii)(B)(2) of this section, this investment is within the 180-day period for C, which began on March 15, 2020, the 180-day period beginning on the due date for P's tax return without extensions, for the taxable year in which P realized eligible gain.



(9)Passthrough entities other than partnerships.

(i) S corporations, nongrantor trusts, and estates. If an S corporation, a nongrantor trust, or a decedent's estate realizes an eligible gain, then rules analogous to the rules of paragraphs (c)(7) and (8) of this section apply to that entity and to its shareholders or its beneficiaries, as the case may be, to the extent they receive or are deemed to receive an allocable share of the eligible gain.

(ii) Grantor trusts. If a grantor trust realizes an eligible gain, either the trust or the deemed owner of the trust may make the election to defer recognition of the gain and make the qualifying investment under rules analogous to the rules of paragraphs (c)(7) and (8) of this section (other than the rule in paragraph (c)(8)(iii) of this section regarding the 180-day period), whether or not the gain is distributed to the deemed owner of the trust.

. . .