

December 18, 2018

CC:PA:LPD:PR (REG-115420-18)  
Internal Revenue Service  
Room 5203  
P.O. Box 7604  
Ben Franklin Station  
Washington, DC 20044

Dear Sir/Madam:

On behalf of the approximately 140,000 members of the National Association of Home Builders (NAHB), I am writing to offer comments on the proposed regulations regarding investing in qualified opportunity zones.

Thank you for the incredible amount of work that has gone into issuing the regulations necessary to implement new section 1400Z-2 of the Internal Revenue Code. The majority of the regulations are logical, fair, and thoughtful. NAHB recommends that the Treasury Department and Internal Revenue Service further clarify issues related to the “working capital safe harbor.” NAHB also has comments regarding the “original use” requirement as it pertains to vacant or abandoned property.

In summary, NAHB encourages the agencies to:

- Provide a longer working capital safe harbor period for projects that require significant regulatory approvals. The proposed 31-month safe harbor may not be long enough for certain projects that require a lengthy approval process.
- Further define within the requirements of the safe harbor “substantially complies” to allow for uncontrollable or unforeseen delays, such as due to weather, labor and supply shortages, or other delays beyond the control of the developer.
- Define “original use” to differentiate between property that is currently economic productive, and subject to the substantial improvement requirement, and property that is vacant or abandoned. Vacant and abandoned property are not contributing to the economic vitality of a QOZ and should be viewed within the definition of “original use.”  
NAHB believes that the regulations should focus on how the tangible property is being used at the time of acquisition and not just where the property is being used.

#### Working Capital Safe Harbor

The statutory requirement under Section 1400Z-2(d)(1) requiring a Qualified Opportunity Fund (QOF) to invest in qualifying assets within 6 months is unrealistic when compared with the average length of time it takes to complete a typical single-family or multifamily project. NAHB supports the agencies’ proposal to create a “working capital safe harbor,” which would allow cash held for the purposes of acquisition, construction, or substantial improvement to qualify as meeting the 90-percent asset test. The proposed working capital safe harbor recognizes the statutory intent of promoting investment in an opportunity zone while balancing the reality of how long it takes to build or renovate real property.

The 2017 Survey of Construction (SOC) from the Census Bureau shows that the average completion time of a single-family house is around 7.5 months, which usually includes almost a month from authorization to start and another 6.5 months to finish the construction.<sup>1</sup> The time from authorization to completion varies across the nation and depends on the geographic location, metropolitan status, and whether the house is custom-built. According to the 2017 SOC, it takes anywhere from less than a month to 77 months to build a single-family home (measured from obtaining a permit to completion).

For multifamily construction, the 2017 SOC found an average construction time, after obtaining authorization, of 15.7 months.<sup>2</sup> This has been on an upward trend since 2013, increasing by approximately one month each year.

The average time to build multifamily homes varies with the number of units in the building. In 2017, buildings with 20 or more units took the longest time (17.6 months) to build after obtaining authorization. Properties with 5 to 9 units required 15.7 months; 10 to 19 units finished in 15.1 months; and lastly, 2 to 4 units came in at 13.5 months.

The agencies' proposal to allow for a 31-month safe harbor for cash used to acquire, construct, or rehabilitate tangible personal property is appropriate to meeting the congressional intent of Section 1400Z-2. In general, as the 2017 SOC data shows, the 31-month window is sufficient to construct a typical multifamily or single-family project. However, this duration may be inadequate depending on the time needed to obtain authorization prior to start of construction. For example, according to a 2002 study, a builder who requires a Section 404 permit under the Clean Water Act faces an average delay of 788 days for an individual permit or 313 days for a "streamlined" permit.<sup>3</sup> Delays from zoning board hearings or due to local community concerns are likewise unpredictable.

This unpredictability raises an issue that NAHB requests the agencies to clarify. Amongst the requirements to qualify for the safe harbor, the business must have a written schedule for how the property will be used, and the business must "substantially comply" with the written schedule.

There are few certainties in life, and even fewer in real estate development. Even the most experienced and well-prepared developer will face unanticipated delays related to permitting, labor availability, weather conditions, supply availability, or community engagement, amongst other potential sources for delay. As a result, NAHB requests that the IRS and Treasury clarify what "substantially complying" means. Specifically, delays that result from external factors, such as weather, permits and environmental reviews, should not be factored into whether a builder is "substantially complying," as such delays fall outside of the control of any builder. In residential real estate, even the best laid plans can and do go awry.

Furthermore, to encourage investment in opportunity zones that are difficult to develop, such as areas that require additional environmental review and approval, NAHB would recommend that the 31-month clock be suspended or paused for projects requiring lengthy federal regulatory approvals.

#### Original Use Requirement

Section 1400-Z2(d)(1)(D)(i)(II) requires that for tangible property to be an eligible investment, the original use of the property must commence with the Qualified Opportunity Fund. Alternatively, the statute allows properties to qualify if the QOF substantially improves the property. A property is considered substantially improved when its additional basis is increased so as to exceed its purchase price.

NAHB believes that the regulations should delineate between tangible property that is already contributing to the economic activity of the Qualified Opportunity Zone—and therefore subject to the substantial improvement

---

<sup>1</sup> <http://eyeonhousing.org/2018/07/time-needed-to-build-a-single-family-home-in-2017/>

<sup>2</sup> <http://eyeonhousing.org/2018/07/apartment-construction-times-lengthened-in-2017/>

<sup>3</sup> David Sunding and David Zilberman, "The Economics of Environmental Regulation by Licensing: An Assessment of Recent Changes to the Wetland Permitting Process," 2002

test—and vacant or abandoned property. Vacant and abandoned property are not contributing to the economic vitality of a QOZ and should be viewed within the definition of “original use.”

Congress created two different requirements for qualifying property as an eligible investment to recognize two different investment scenarios. In our opinion, the original use requirement is intended to ensure the investment creates economic activity where none currently exists. On the other hand, the substantial improvement requirement allows a QOF to invest in an existing asset already contributing to the economic foundation of a QOZ, but only if there is a significant additional investment. Each of these requirements fits the intent of spurring new investment, but create different qualifying thresholds depending on the current use of the qualifying property.

Congress chose to use the terminology of “original use” versus specifically requiring that eligible investments be of new construction or manufacture. As a result, NAHB believes that the regulations should focus on how the tangible property is being used at the time of acquisition and not just where the property is being used. A property not currently in use can still have “original use” within a QOZ if the QOF restores it to active use. Vacant or abandoned property would therefore not be subject to the substantial improvement requirement but rather viewed as an “original use.”

There is a significant consequence for investors dependent upon whether a property qualifies under “original use” or requires a “substantial improvement.” In certain circumstances, the substantial improvement requirement acts as a barrier to investment. For example, affordable housing is extremely sensitive to the capital investment costs, and it may not be possible to create affordable housing due to the substantial improvement requirements. For that matter, investors may avoid market-rate projects if the substantial improvement requirements prove too costly.

The purpose of the substantial improvement requirement is not to deter investments, but rather to ensure that investors do not simply absorb tangible property that is already performing economically. But for property that is sitting vacant or abandoned, there is no current economic benefit to a QOZ. NAHB believes that “original use” is meant to be applied more broadly than just for new construction to include properties that are not currently in use. As such, the regulations should allow a “reset” for abandoned or vacant property that allows it to qualify as “original use” when acquired by a QOF, if the QOF returns that property to an economically usefully state. A strict interpretation of the original use requirement would not serve to benefit distressed communities that the legislation seeks to benefit if investors look past vacant and abandoned buildings.

Sincerely,



J.P. Delmore  
Assistant Vice President, Government Affairs