



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY

WASHINGTON, D.C. 20460

DEC 18 2018

OFFICE OF  
LAND AND EMERGENCY  
MANAGEMENT

Kirsten B. Wielobob  
Deputy Commissioner for Services and Enforcement  
CC:PA:LPD:PR (REG-115420-18), Room 5203  
Internal Revenue Service  
PO Box 7604  
Ben Franklin Station  
Washington, DC 20044

**Subject: U.S. EPA Office of Brownfields and Land Revitalization Seeks Regulatory Clarifications and Improvements to Proposed IRS Rule Regarding “Investing in Opportunity Funds,” REG-115420-18**

Dear Ms. Wielobob:

On behalf of the U.S. Environmental Protection Agency’s (EPA) Office of Brownfields and Land Revitalization (OBLR), thank you for the opportunity to comment on the Department of Treasury’s Proposed Regulations §1400Z-2(a)-1, 2(c)-1, 2(d)-1, 2(e)-1 and Revenue Ruling 2018-29, regarding “Investing in Opportunity Funds.” EPA’s OBLR encourages the IRS to clarify and improve the proposed rule to better foster investment in blighted and contaminated properties, or “brownfield sites,” in designated Opportunity Zones.

The “Investing in Opportunity Act” has the potential to spur investment in communities where neighborhoods have long been plagued by concentrated distress and those left behind by the economic recovery following the Recession. Many of these communities struggle with stagnation and lack of access to capital, in part due to the challenges of remediating and redeveloping their brownfield sites. A brownfield is a property where the presence or potential presence of a hazardous substance, pollutant, or contaminant from the property’s former use complicates or inhibits the property’s expansion, redevelopment, or productive reuse. Brownfield sites often stigmatize neighborhoods and perpetuate blight and socio-economic distress.

EPA’s OBLR encourages the IRS to clarify in the final guidance that investments in the assessment, remediation, and redevelopment of brownfields properties located in Qualified Opportunity Zones (QOZs) are included within the scope of Qualified Opportunity Funds (QOFs). This clarification will provide an incentive to invest funds in the assessment, remediation, and reuse of brownfield properties. Assessing, remediating and redeveloping

brownfield sites in QOZs is integral to the primary purpose of the Investing in Opportunity Act provisions<sup>1</sup> because:

- **Brownfields remediation is often the first step to spurring revitalization within distressed communities.** In low-income areas which have often suffered a long history of noxious land uses, illegal dumping, closed industry facilities, and lack of health and safety enforcement, federal incentives for revitalization should prioritize ensuring that areas with blighted, underutilized and/or contaminated properties are safe and prepared for redevelopment as the first step towards renewal.
- **Public health and environmental protection are matters of primary concern to distressed communities.** Hazardous materials and other contamination on brownfield sites are associated with poor health outcomes (e.g. cancer, respiratory disease, diabetes, stroke, heart disease, injury) and higher mortality rates among infants and adults. Creating incentives to invest in remediation of brownfields will promote economic development and better health outcomes, saving costs and enabling a more productive workforce.
- **Brownfields properties are overwhelmingly concentrated in places of people of color, low-income populations, and otherwise marginalized communities,** which are heavily represented among the QOZs. Recently, EPA's OBLR conducted an analysis recently which found substantial overlap of known brownfield properties within designated QOZ census tracts. The IRS regulations should create incentives for investment in brownfield sites in order to help overcome stagnation, social inequity, and environmental justice concerns within the QOZs, as these factors create barriers to revitalization.
- **Brownfield redevelopment can transform abandoned and underused sites into community and economic assets** such as mixed-use developments, housing, and other productive reuses, without contributing to urban sprawl. Further, brownfield properties are often centrally located in areas where transportation and utility infrastructure are already available, which can make them valuable properties for development.
- **Brownfields remediation and redevelopment can take significant time,** beyond the development timeframes expected at greenfield projects or at properties with little or no contamination. A successful brownfields redevelopment usually involves environmental assessment and investigations, the development of remedial cleanup plans, coordination with neighborhood stakeholders to ensure that cleanup is protective of public health, and substantial involvement in regulatory approvals, often including approval and inspections of the remediation by state officials through what are typically called "Voluntary Cleanup Programs" established in state environmental agencies – all before the vertical development can occur. Thus, the time limitations proposed by IRS in the proposed regulations must be sensitive to the long timeframes often needed to address contamination issues at brownfield sites.

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<sup>1</sup> See H.R. Rept. 115-466, 537, which describes the intent to attract an influx of capital to designated low-income communities with impacts and outcomes in those areas including job creation, poverty reduction, and other metrics.

## **Clarification Requests and Comments:**

EPA's OBLR requests that the IRS make the following clarifications to the proposed guidelines. These clarifications will give Opportunity Fund investors confidence that QOF investment can be used to assess, clean up, and redevelop brownfields properties located in QOZs.

### **1. Brownfields Cleanup of Real Property Should Constitute "Original Use"**

EPA's OBLR requests that the IRS clarify the definition of "Original Use" so that the term applies to property that is a brownfield site as defined by section 101(39) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. 9601), which is the law that establishes the U.S. EPA brownfields program and guides brownfields considerations by many other federal departments and agencies. The IRS has used this definition of "brownfield" as well, under 26 U.S.C. Section 198(c), which permitted certain treatment of expenditures on "qualified environmental remediation" at a "qualified remediation site", which was defined as "any area . . . at or on which there has been a release (or threat of release) or disposal of any hazardous substance."

While most new investments assume that a property already meets applicable health and safety standards, brownfields properties are different in that they are complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant.

- Investment to assess and remediate environmental conditions at brownfield properties are required to make these properties financeable and developable.
- Essentially, all lenders and investors require environmental investigation and cleanup for properties which are brownfields to ensure they are safe for redevelopment.
  - Brownfields remediation can make previously unsuitable properties ready for investment by making them meet basic safety standards and safe for human health and the environment.
  - Making previously unsuitable properties located in QOZs ready for investment enables properties to "commence use" within the QOZ.

Defining "Original Use" to incorporate brownfields properties located in QOZs creates the best solution to enabling QOF investments in brownfields remediation and redevelopment. This clarification will address the concern that the 30-month window for substantial improvement is unrealistic for brownfields properties, which take longer than traditional vertical development projects due to the added challenges of contamination.

**Example:** A brownfields remediation firm purchases a contaminated brownfields property in a QOZ, where a former factory was once located, to remediate the land and sell the property for new use. This brownfield property should qualify as QOZ property under "original use."

- ### **2. Cleanup or Reuse of Vacant or Underutilized Property Should Constitute an "Original Use":**
- EPA's OBLR requests that the IRS clarify the definition of "Original Use" so that the term applies to property that is vacant or underutilized for a period of

one year or more. For purposes of Section 1400Z-2(d)(2)(D)(i), if property is vacant or underutilized for at least a one-year period, use prior to that period should be disregarded for purposes of determining original use. This borrows from the commonsense definition of “original use” for Enterprise Zone facility bonds in 26 CFR 1.1394-1(h) and adds “underutilized.”

“Underutilized” could be defined as it is in other federal statute, such as the definition of “underutilized” in 45 CFR 12a.1 (which defines underutilized as it relates to property owned by federal agencies), stating that “underutilized” should mean an entire property or portion thereof, with or without improvements which is used only at irregular periods or intermittently by the owner or operator for purposes of that owner or operator, or which is used for current purposes that can be satisfied with only a portion of the property.

The definition of original use should also permit QOZ investment in properties that contribute to blight or create barriers to economic vibrancy due to prolonged vacancy or underutilization. Defining original use to include new use of properties that are contributing to decay within distressed communities is clearly in line with purpose of the incentive.

**Example:** A developer purchases a property to rehabilitate for new use. The property has a factory on it that has been vacant for more than one year. Regardless of whether that property is reused for a similar manufacturing purpose, a new manufacturing purpose, or a different kind of development (such as commercial or residential), this property should qualify as QOZ Property under “original use.” The same should apply for a property that has a 5-acre factory on it where only 0.5 acres of space are currently in use.

3. **Foreclosed and Tax-Reverted Properties Held by Local Units of Government Should be Treated as “Underutilized or Abandoned Property”:** EPA’s OBLR requests that the IRS clarify that any property that has been foreclosed upon and reverted to a local unit of government or land bank should qualify as “vacant and underutilized” regardless of how long it has been vacant, abandoned or underutilized.

Local units of government often acquire brownfields and other blighted properties through tax delinquency, abandonment, bankruptcy, etc. A bright line test around status of ownership for properties in foreclosure, receivership, or involuntary transfer may be easier to determine than the historical use of the property and expedite investment in assembled properties, particularly in distressed urban areas.

4. **Brownfield Investments Should Count Toward Substantial Improvement:** EPA’s OBLR requests that the IRS clarify that improvements to land, including brownfields assessment, cleanup and other site preparation costs, are included as expenses that will meet the “Substantial Improvement” test for a QOZ Property. This aligns with the standard definition of “tangible property” (“land plus improvements”).

Without this clarification, it is unclear **how improvements to the land itself factor into a calculation of substantial** improvement, given that the adjusted basis in the example outlined in Rev. Rule 2018-29 pertains only to improvements to a building. While Rev. Rule 2018-29 indicates that the cost of the land on which the building is located is not included in the adjusted basis for the substantial improvement calculation, it is unclear what the calculation would be on a brownfields project for which the primary or sole improvements are improvements to the land itself, when vertical development is expected later.

Environmental assessment and remediation activities can make a property ready for redevelopment where it would otherwise be unsafe for reuse due to the presence or potential presence of environmental contamination. Unless the land is assessed, remediated to appropriate contaminant levels and exposures controlled (based on reuse of the property), any building and business investment will not occur on the property.

The following environmental assessment and remediation activities commonly occur at brownfield properties because they are necessary to enable safe reuse:

- Removing underground storage tanks when excavating for basement or parking
- Environmental site assessments (Phase I / II) to investigate potential contamination for due diligence purposes and admission into a state or tribal voluntary cleanup program
- Contamination cleanup of soil and groundwater on site
- Engineering controls/barriers that prevent exposure of environmental contamination
- Abating asbestos or lead paint when rehabilitating an existing building

**Example:** A developer purchases Property X, which is located in a QOZ, for \$1 million. Property X consists of a building previously used as a factory erected prior to 2018 and land on which the factory building is located. Sixty percent (\$600k) of the \$1 million purchase price for Property X is attributable to the value of the land and forty percent (\$400k) is attributable to the value of the building. QOF A intends to convert the factory building to residential rental property. The transformation will require \$800k in environmental remediation costs. Within 29 months after the date of QOF A's acquisition of Property X, QOF A invests \$800k in remediating the property and \$500k in additions to the building. Clarification is necessary to ensure that the expenses associated with remediating the land will count toward the substantial improvement calculation. The same is true for a similar scenario common at complex brownfield sites in which at the close of the 30-month period the only expenditures have been for remediation of the land.

5. **Gains from QOF Investment in Brownfield Improvements to Land Should Be Permitted to be Carried Over into Other QOZ Investments:** EPA's Brownfields and Land Revitalization Program requests that the IRS enable gains realized from the sale or exchange of QOZ Property to be deferred if they are reinvested in replacement QOZ Property within a 12-month period beginning on the date of the sale or exchange, with the QOF's basis in the replacement Property being equal to the QOF's basis in the QOZ Property at the time it was sold or exchanged. This carryover basis will preserve any

gains not recognized in the event that a subsequent sale is not followed by the reinvestment in replacement QOZ Property within a 12-month period.

Clarification on this issue is particularly pertinent to facilitating the ability for QOZ Businesses to remediate brownfields properties with QOF funds to sell to a vertical developer and still access the benefits of the step-up in basis. Without this clarification, using QOF funding for brownfields remediation and property improvement as the primary business activity might require the owners of the site to sit on the site for the duration of the ten years after remediation is complete in order to access the benefits of the Opportunity Zone incentive.

**Example:** On January 1, 2019 T, a calendar-year taxpayer, invested \$1 million of gain in B, an QOF partnership dedicated to brownfields cleanup that remediates properties to sell for future vertical development by other parties. B immediately makes a \$1 million investment in remediation and land improvements to a brownfields site that qualifies as QOZ Property. On January 1, 2023 (after four years), B sells the remediated QOZ Property to a vertical developer for \$1.5 million and reinvests all of the proceeds in replacement QOZ Property within 12 months. Clarification is necessary that if the entire \$1.5 million from the sale of QOZ Property is reinvested into replacement QOZ Property: 1) the deferral and reduction in basis timeclocks on the original \$1 million investment would not reset, and 2) the 10-year timeclock on would not reset for the \$500,000 in gain.

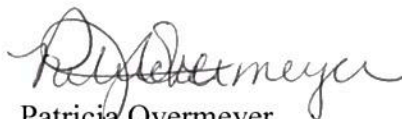
6. **Allow QOF Investments to be Stacked for Brownfield Properties that Require Remediation:** EPA’s OBLR requests that the IRS clarify that the 30-month window to demonstrate substantial improvement to the land via remediation and other site preparation activities is a separate 30-month window from follow-on vertical development.

Brownfields remediation and redevelopment often includes separate land improvement (horizontal development) and vertical development phases, and investors face regulatory risk of effectuating cleanup which enables the property to be financed. These factors make the substantial improvement 30-month window extremely difficult time frame in which to complete a redevelopment which involve remediation of environmental contamination.

Large redevelopment projects such as auto manufacturing site or former hospitals may require extensive demolition of existing buildings, excavation, cleanup and grading as early site preparations for the construction of the new structure. It is common to spend several years on existing structural demolition, earthmoving, and environmental cleanup on large sites, which almost guarantees that the finished building will not be completely operational by the end of the 30-month period for substantial improvement. Many “ground up” construction projects in cold weather climates will also face greater challenges in achieving occupancy within 30 months and will likely be a work in progress. Clarity is needed so that significant – and transformative - redevelopment projects can be pursued.

Thank you for considering our requests for clarifications. The clarifications we are requesting will give Opportunity Fund investors confidence that QOF investments can be used to assess, remediate, and redevelop brownfields properties located in QOZs. Subsequently, these clarifications may lead to the economic revitalization of many of our nation's disadvantaged communities. Should you want to discuss our comments and requests for clarification, please feel free to contact me at 202-566-2774 or [Overmeyer.patricia@epa.gov](mailto:Overmeyer.patricia@epa.gov) .

Sincerely,

A handwritten signature in cursive script, appearing to read "Patricia Overmeyer".

Patricia Overmeyer  
Deputy Director  
Office of Brownfields and Land Revitalization  
U.S. Environmental Protection Agency

