

RESEARCH NOTES

OZ 2.0 Tax Verification

Four verified tax questions on 100% bonus depreciation, 10-year exclusion of depreciation recapture, QBI eligibility through a QOF/QOZB, and STR non-passive material participation.

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Indiana Dunes Club Development LLC · Indiana Dunes Club — The Lake Michigan Estates

Verification notes for the sponsor. Any figures or statements ultimately used in investor communications should be reviewed by the investor's own CPA and tax counsel. Nothing in this document constitutes tax, legal, or investment advice.

Question 1: Is 100% bonus depreciation actually available for 2026 vertical builds under OBBBA?

Answer: YES — 100% bonus depreciation is permanently reinstated for qualifying property acquired and placed in service after January 19, 2025.

Authoritative citations:

- Statutory basis: IRC §168(k), as amended by the One Big Beautiful Bill Act (OBBBA), Public Law 119-21, signed July 4, 2025.
- Effective date: January 19, 2025 acquisition/placed-in-service date (both must be met for the acquisition date test).
- IRS Guidance: IRS Notice 2026-11 provides implementation guidance.
- Rate: 100% first-year expensing (fully deductible in year 1) on qualifying short-life property (5-year, 7-year, 15-year MACRS classes).
- Optional election: Taxpayers may elect 40% instead of 100% for the first tax year ending after Jan 19, 2025 if beneficial (e.g., to preserve NOLs).
- Duration: Made permanent — no longer subject to TCJA phase-down.

Sources:

- [PKF O'Connor Davies — IRS Issues Guidance on Additional First-Year Depreciation Under OBBBA](#)
- [RSM US — The OBBBA Restores and Expands Bonus Depreciation](#)
- [Grant Thornton — OBBBA Offers New Ways to Accelerate Depreciation](#)
- [Reed Corp — Bonus Depreciation in 2026: 100% Restored by OBBBA](#)

Duneswalk implication:

On a \$1.2M vertical build with a proper cost segregation study identifying ~25% of basis into 5/7/15-year property (~\$300K), the investor gets a \$300K first-year depreciation deduction in Year 1 on top of straight-line 27.5-yr depreciation on the remaining \$900K building shell (~\$33K/yr). Combined first-year deduction: ~\$333K on a \$1.2M asset — 27.7% of basis expensed in Year 1.

Question 2: Does the OZ 10-year exclusion apply to depreciation recapture, or just capital gains?

Answer: YES — under the Final Regulations, the OZ 10-year exclusion covers ALL gains including depreciation recapture (§§1245 and 1250), EXCEPT gains from inventory sold in the ordinary course of business.

This is the most important finding of this research and it is CONTRARY to an earlier, superseded interpretation in the Proposed Regulations. Some older tax blogs still cite the outdated position.

Authoritative citations:

- Statutory basis: IRC §1400Z-2(c) — the 10-year fair market value basis step-up election.
- Regulatory basis: Treas. Reg. § 1.1400Z2(c)-1(b)(2)(ii)(A) — the asset sale election as finalized on March 13, 2020.
- Exact regulatory text (from 26 CFR § 1.1400Z2(c)-1):

> "If a taxpayer has held a qualifying investment in a QOF partnership or QOF S corporation for at least 10 years... and the QOF partnership or QOF S corporation or any partnership that is owned directly, or indirectly solely through one or more partnerships, by the QOF partnership or QOF S corporation sells or exchanges property, the taxpayer may make an election under this paragraph (b)(2)(ii)(A) to exclude from the taxpayer's income all gains and losses allocable to the qualifying investment that arise from all such sales or exchanges for the QOF partnership's or QOF S corporation's taxable year... gains and losses include all gains and losses other than gains or losses from the sale or exchange of any item of inventory, as defined in section 1221(a)(1), in the ordinary course of business."

- How the Final Regulations changed prior interpretation: The Proposed Regulations (2019) had said the asset sale election only excluded capital gains and required recognition of depreciation recapture and ordinary income. The Final Regulations (issued Dec 2019, effective March 13, 2020) explicitly broadened this to all gains and losses including §1245 and §1250 recapture.

Sources (BigLaw analysis):

- [Cornell Law — 26 CFR § 1.1400Z2\(c\)-1 Investments Held for At Least 10 Years-1](#) — full regulatory text
- [Proskauer Tax Talks — Final Regulations on Opportunity Zones](#) — confirms: "All gain on the sale of a QOF interest or underlying assets after 10 years is excluded, other than gain from ordinary course sales of inventory"

- [Gray Robinson \(PDF\) — Unpacking The Final Opportunity Zone Regulations, Part 1](#) — confirms: "The final regulations also clarify that upon an asset sale, the fair market value basis step up functions to exclude all types of gains and losses — including, for example, depreciation recapture under Sections 1245 and 1250 — except for gains and losses from the sales of inventory in the ordinary course of business"
- [Tax Notes / IRS Federal — IRS Publishes Final O-Zone Regs](#) — official Treasury publication

Compliance requirements to preserve the exclusion:

1. Investor must make the §1400Z-2(c) election on their tax return for each year gain from an asset sale is excluded. 2. The QOF is deemed to distribute the net proceeds from asset sales on the last day of its tax year, solely for purposes of determining qualifying investment amounts. 3. The 10-year holding period must be met on a per-qualifying-investment basis.

Duneswalk implication:

An investor who takes ~\$300K of cost-seg / bonus depreciation deductions in Year 1 (Scenario A build & STR) does NOT have to pay §1245 recapture on that depreciation at the Year 10+ home sale, provided:

- They hold the QOF interest at least 10 years
- The QOF/QOZB properly structures the sale
- The taxpayer timely makes the §1400Z-2(c) election
- The property qualifies as QOZBP (Qualified Opportunity Zone Business Property)

This is the "double dip": front-load the depreciation shield in the early years (against ordinary income), and shed the recapture obligation at exit under the OZ 10-year exclusion.

Question 3: Does STR income through a QOF/QOZB qualify for the §199A QBI deduction?

Answer: PROBABLY YES, but requires meeting the "trade or business" test under §162 or the §199A safe harbor. Not automatic; requires proactive structuring and documentation.

Authoritative citations:

- Statutory basis: IRC §199A, providing up to 20% deduction on qualified business income.
- Regulatory basis: Treas. Reg. §1.199A-1(b)(14) — rental activity qualifies for §199A in one of two ways: 1. It is a §162 trade or business 2. A commonly controlled trade or business is the lessee
- Safe harbor: IRS Notice 2019-07 — proposed safe harbor for rental real estate as a trade or business.

Safe harbor requirements under IRS Notice 2019-07:

- Separate books and records maintained for the rental activity
- At least 250 hours of rental services per year (post-2023: 250 hours in each of 3 of the past 5 years)
- Contemporaneous records of services performed
- Triple-net leases NOT eligible
- Property used as a residence under §280A NOT eligible if personal use exceeds greater of 14 days or 10% of days rented at fair rental — critical for STR/condotel structures
- Signed statement of safe harbor compliance attached to return

Sources:

- [IRS — Qualified Business Income \(QBI\) Deduction](#)
- [Journal of Accountancy — The QBI Deduction for Rental Real Estate Activity](#)
- [Condley CPA — Rental or Business? Navigating the Tax Treatment of Short-Term Rentals](#) — explicitly states STR income CAN qualify for QBI if it meets the trade or business test.
- [Tom Talks Taxes — Rental Activities and the §199A QBI](#)

Duneswalk implication:

STR income through the QOF/QOZB CAN qualify for the 20% QBI deduction if: 1. The management is active (property manager providing substantial services beyond a triple-net lease) 2. Personal use is kept under the §280A limits (14 days or 10% of rental days) 3. 250 hours of qualifying rental services are logged annually and documented 4. The investor's taxable income falls under the QBI phase-out thresholds (\$383,900 MFJ / \$191,950 single in 2025, indexed)

Recommend to investor: Structure engagement with the rental management company to include cleaning, guest services, marketing, maintenance coordination — pushing the activity firmly into "trade or business" territory. Keep contemporaneous logs.

Caveat: For high-net-worth Illinois investors above the QBI phase-out threshold, the QBI deduction is limited or unavailable. Model conservatively as 0-20% depending on investor income.

Question 4: Does the STR "7-day rule" make STR losses non-passive without needing Real Estate Professional Status?

Answer: YES — under Treas. Reg. §1.469-1T(e)(3)(ii)(A), a rental with average customer use of 7 days or less is **NOT** treated as a rental activity for passive-loss purposes. Material participation alone (without REPS) is sufficient to deduct losses against ordinary/W-2 income.

Authoritative citations:

- Regulatory basis: Treas. Reg. §1.469-1T(e)(3)(ii)(A) — the "7-day rule"
- Related regulation: Treas. Reg. §1.469-1T(e)(3)(iii) — computation of average period of customer use (total days rented ÷ number of separate rentals, per property, per tax year)
- Statutory basis: IRC §469 — passive activity loss rules

How it works:

1. If average guest stay is ≤ 7 days in the tax year, the activity is **NOT** a "rental activity" under §469.
2. Because it's not a rental activity, the standard §469 rental presumption (all rental income is passive) does **NOT** apply.
3. To make the losses non-passive, the taxpayer must simply satisfy **ONE** of the seven material participation tests — REPS is not required.

The seven material participation tests (only one needs to be met):

1. 500-hour test: 500+ hours per year on the activity
2. Substantially all test: Taxpayer does substantially all the work
3. 100-hour test: 100+ hours AND nobody else (including professional managers) does more
4. Significant participation: 500+ hours across multiple significant participation activities
5. 5-of-10-years test: Material participation in 5 of the last 10 years
6. Personal service: Material participation in a personal-service business for 3+ prior years
7. Facts-and-circumstances: Catch-all, rarely usable

Sources:

- [Cost Seg Smart — Material Participation Test for STR Owners \(IRC §469\)](#) — comprehensive walk-through with citations

- [The Real Estate CPA — Using Short-Term Rental Losses to Reduce Active Income](#)
- [Morkel Financial — Short-Term Rental Loophole: Offset W-2 Income](#)
- [Cherry Bekaert — Short-term Rental Tax Rules Explained](#)

Duneswalk implication:

For a Duneswalk investor building an STR home: 1. Average stay must be ≤ 7 days for the tax year — achievable for a beach STR with typical weekly rental cadence but may fail if rented for extended monthly stays in shoulder seasons. Track carefully. 2. The investor must materially participate. The 100-hour test is the most achievable path — the investor logs 100+ hours per year AND participates more than the property manager (which is nontrivial to demonstrate if using a full-service PM). 3. Alternative for investors who use full-service management: Some investors self-manage the marketing/guest communication side (Airbnb messaging, review responses, tax filings) which counts as active participation.

Combined benefit: If the investor meets both the 7-day rule and the 100-hour material participation test, then all cost-seg / bonus depreciation losses in Year 1 (~\$300K) can be deducted against W-2 income or other active income sources — saving up to ~\$111K in federal tax (at 37% bracket) in Year 1 alone.

Summary Table — What Duneswalk Can State With Confidence

| Claim | Confidence | Regulatory Citation | |---|---|---| | 100% bonus depreciation on qualifying short-life property, Year 1 | HIGH | IRC §168(k) as amended by OBBBA P.L. 119-21; IRS Notice 2026-11 | | Cost seg reclassifies 20-30% of building basis into short-life | HIGH (industry standard) | Rev. Proc. 87-56; DOL/IRS guidance on cost segregation studies | | OZ 10-year exclusion covers ALL gains including recapture | HIGH | Treas. Reg. §1.1400Z2(c)-1(b)(2)(ii)(A); IRC §1400Z-2(c) | | STR 7-day rule enables non-passive treatment | HIGH | Treas. Reg. §1.469-1T(e)(3)(ii)(A) | | Material participation via 100-hour test (not REPS required) | HIGH | Treas. Reg. §1.469-5T(a); IRC §469 | | QBI deduction available if STR is trade/business | MEDIUM — requires proactive structuring | Treas. Reg. §1.199A-1(b)(14); IRS Notice 2019-07 safe harbor | | §199A safe harbor for STR (250 hours, no personal use) | MEDIUM — depends on facts | IRS Notice 2019-07 |

Recommended Language for Investor Documents

Strong claim (well-supported): > Under IRC §168(k) as reinstated by the OBBBA (P.L. 119-21, effective Jan 19, 2025), 100% first-year bonus depreciation is available on qualifying short-life property (5-, 7-, and 15-year MACRS classes) placed in service in 2026 and later. A cost segregation study on the Duneswalk vertical build typically reclassifies 20-30% of the building basis into these short-life categories — meaning an investor can expense roughly \$300K of a \$1.2M build in Year 1, in addition to straight-line depreciation on the remaining \$900K building shell.

Strong claim (well-supported): > The Final Regulations under Treas. Reg. §1.1400Z2(c)-1(b)(2)(ii)(A) provide that a taxpayer holding a qualifying QOF investment for at least 10 years may make an asset-sale election to exclude from income all gains and losses allocable to the qualifying investment — including depreciation recapture under IRC §§1245 and 1250 — except gains from inventory sold in the ordinary course of business. This means Duneswalk investors who claim large depreciation deductions in early years do not owe recapture on those deductions at the Year 10+ home sale, provided the QOF/QOZB structure and elections are properly maintained.

Strong claim (well-supported): > Under Treas. Reg. §1.469-1T(e)(3)(ii)(A), the Duneswalk vacation home — with typical weekly rental cadence keeping average guest stay at or below 7 days — is not a "rental activity" for §469 passive-loss purposes. An investor who materially participates (most commonly via the 100-hour test) can deduct all bonus depreciation and cost-seg losses against W-2, business, and other active income — without needing Real Estate Professional Status.

Cautious claim (requires structuring): > The STR activity MAY qualify for the 20% §199A QBI deduction if it rises to a Section 162 trade or business — which typically requires active management services beyond a triple-net lease, at least 250 hours of qualifying rental services per year documented contemporaneously, and personal use kept below the §280A thresholds (14 days or 10% of rented days). Investors should work with their CPA to structure the STR management engagement to preserve this benefit.

Two Follow-Up Items for Sponsor Attention

1. Property manager engagement structure: Draft the Duneswalk rental management agreement so that either (a) it explicitly enables investor material participation (self-managed marketing/comms), or (b) the QOZB itself is structured such that management fees flow properly and the investor's participation via the QOF meets §469 tests. Coordinate with tax counsel.
2. QOF/QOZB operating agreement: Ensure the OA explicitly (a) commits to making §1400Z-2(c) asset-sale elections at Year 10+, (b) restricts inclusion events, (c) provides for proper cost

segregation study on placed-in-service, and (d) allocates depreciation deductions to investors in a way that maximizes their utility (special allocation to the investor providing the equity, subject to §704(b) substantial economic effect rules).

REFERENCE · KEEP THIS HANDY

Acronym & term legend

Every OZ term used across the Indiana Dunes Club investor materials, defined once. Investors familiar with OZ rules can skip. On the website (indianadunesclub.pplx.app) these definitions appear on hover.

OZ VEHICLES & ENTITIES

QOF	Qualified Opportunity Fund. The entity (LLC taxed as partnership, or corporation) that receives your rolled capital gain and invests it into the project.
QROF	Qualified Rural Opportunity Fund. A QOF whose project sits in a rural OZ tract (population <50K per OBBBA). Rural QROFs receive a 30% basis step-up at Year 5 (vs. 10% for urban QOFs) and only 50% substantial-improvement threshold (vs. 100%). Indiana Dunes Club is a QROF — all four LaPorte County OZ tracts are rural.
QOZB	Qualified Opportunity Zone Business. The project-level LLC (owned by the QOF) that owns the parcels and improvements. The two-tier QOF → QOZB structure unlocks the 31-month working-capital safe harbor.
QOZ	Qualified Opportunity Zone. A federally designated census tract. Indiana Dunes Club sits in Tract 430 (Michigan City, IN).
OZ 2.0	The permanent Opportunity Zone program enacted by the One Big Beautiful Bill Act (July 2025), effective January 2027. Restores rolling deferral, adds 30% basis step-up at Year 5 for rural QROFs (10% for standard urban QOFs), and 100% federal tax exclusion at Year 10.
OBBBA	One Big Beautiful Bill Act. The July 2025 tax law that made the OZ program permanent and introduced rural QROF benefits.
IRC §1400Z-2	Section of the Internal Revenue Code that authorizes the OZ tax benefits.
§1031	Like-kind exchange. Real-estate-only vehicle that defers capital gains when full sale proceeds are reinvested into replacement property. Any cash kept ("boot") is taxed immediately. Unlike OZ 2.0, §1031 defers indefinitely but never permanently eliminates the tax during the investor's life — basis carries forward until a taxable sale or the §1014 step-up at death.

TAX TERMS

LTCG	Long-Term Capital Gains. The federal rate applied to gains on assets held over one year. 20% federal + 3.8% NIIT = 23.8% for high earners.
NIIT	Net Investment Income Tax. A 3.8% surtax on investment income for high earners, added on top of the 20% federal LTCG rate.
IRS	Internal Revenue Service. The federal tax authority.
IRC	Internal Revenue Code. The federal tax law.

FEDERAL FORMS FILED

Form 8996	Annual self-certification the QOF files with its first partnership return to confirm the 90% asset test.
Form 8949	The investor's tax form used to elect deferral of the rolled capital gain in the year of investment.
Form 8997	The investor's annual tax form used to report their QOF investment holding each year.
K-1	IRS Schedule K-1. The annual tax form a partnership issues to each member showing their share of income, deductions, and credits.
EIN	Employer Identification Number. The federal tax ID required to open a bank account for the QOF LLC.

DEAL & OFFERING TERMS

LLC	Limited Liability Company. The standard legal entity used for both the QOF and the QOZB.
JV	Joint Venture. The sponsor-investor partnership structure that owns the project.
GP / LP	General Partner (sponsor) and Limited Partner (investor). The GP manages the project and earns promote above the preferred return; the LP contributes capital and receives the preferred return.
Reg D 506(c)	SEC Rule 506(c) under Regulation D. The private-offering exemption that allows general solicitation to verified accredited investors only.
NDA	Non-Disclosure Agreement. The confidentiality agreement executed before the offering package is delivered.

UNDERWRITING METRICS

MOIC	Multiple on Invested Capital. Total dollars returned divided by dollars invested. A 2.0× MOIC means the investor doubled their money.
IRR	Internal Rate of Return. The annualized rate of return on the investment, expressed as a percentage.
NOI	Net Operating Income. Property revenue minus operating expenses, before debt service, taxes, and capital reserves.
LTV / LTC	Loan-to-Value and Loan-to-Cost. Ratios of the loan amount to appraised value or total project cost, respectively.
DSCR	Debt Service Coverage Ratio. NOI divided by annual debt service. Lenders typically require 1.20×–1.35×.
IO	Interest-Only. A loan structure where the borrower pays only interest during the term, with principal due at maturity.

STR

Short-Term Rental. Nightly or weekly rental income (typically via VRBO or Airbnb) used to underwrite operating cash flow.

Illustrative planning summary. Not tax, legal, or investment advice. Investors should consult their own qualified tax counsel before making any Opportunity Zone election. Indiana Dunes Club Development LLC. indianadunesclub.pplx.app · invest@dunesreserve.com.