

LIHC MONTHLY REPORT

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TAMs Cause Wariness Among LIHC Syndicators, Investors

By Jennifer A. Hurley, Staff Writer

DALLAS—The Technical Advice Memorandums (TAMs) released last fall by the Internal Revenue Service (IRS) are thwarting many low-income housing tax credit (LIHC) transactions and causing wariness among tax credit syndicators and investors, said panelists at Novogradac & Company LLP's Credit & Bond Financing for Affordable Housing Conference on May 17.

The IRS issued five TAMs last October in response to questions that arose during the audit of a low-income housing developer. Conflicting with current industry practice, the TAMs severely limit what costs can be included in a property's eligible basis, which is used to determine the amount of credit that property can receive. (See June 2001 *LIHC Monthly Report*, p.1.) The advice presented in a TAM is limited to the taxpayer for whom the TAM is requested and is not intended to be used as a precedent, but it does provide guidance regarding the IRS' thinking on specific issues.

Local Impact Fees

The TAMs stunned the affordable housing industry with the assertion that local impact fees—which include fees for water service, wastewater service, roads, schools, law enforcement and fire protection—cannot be included in eligible basis. The IRS stated in the TAMs that because local impact fees constitute a separate, nondepreciable, intangible asset to the taxpayer, they are not includable in eligible basis of the buildings to which the payments relate or in the basis of the land.

Determining whether or not an impact fee is non-recurring and therefore nondepreciable can be problematic. "If you would have to pay the [impact] fee again [if the land were redeveloped], that fee can be included in eligible basis," said Michael Novogradac, managing partner of Novogradac & Company LLP. "Would you have to pay the fee again in 40 years? This question is hard to answer."

Developers who follow the TAMs and do not include impact fees in eligible basis are struggling to make tax-exempt private activity bond and LIHC transactions pencil out. "In areas that have large impact fees, such as California or Florida, [the TAMs] are devastating," said Randall Alligood, a partner in the Orlando office of the law firm Broad and Cassel. "Even in states without large impact fees, there is sometimes a devastating impact on deals."

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TAMs

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Landscaping Costs

Another contentious issue for the industry is the TAMs' statement that landscaping costs can be included in eligible basis only if the landscaping must be replaced in the case that the buildings are replaced. Landscaping costs such as top soil, seeding, finish grading and planting of shrubbery and ornamental trees cannot be included in eligible basis, according to the TAMs. The provision would require that architects, contractors and subcontractors break down their fees in terms of time spent landscaping the perimeter of the building versus time spent on other landscaping—thus creating huge record-keeping burdens.

"If a developer talks with the landscaper about a bush outside the perimeter [of the building], those fees are not includable," said Alligood.

Syndicators and Investors

Because the TAMs have created so much uncertainty within the industry, some syndicators are expressing hesitancy to buy LIHCs. For some transactions, syndicators have requested additional guarantees or have collateralized the guarantees, according to Alligood.

Moreover, some LIHC investors want to hold back equity until the TAMs issue is resolved. "They don't want to give [equity] to you until Congress gives a favorable ruling [on the TAMs]," Alligood stated. "These items will have to be excluded from eligible basis entirely."

All in all, the TAMs are provoking investors to get more involved in the details of LIHC transactions due to the fear of financial losses. "The investor parameters are changing," said Alligood. "The investors are getting much more involved in the deals that they used to let syndicators take care of."

"Ultimately, investors want certain guarantees," he added. "The syndicator will bridge that gap by making guarantees."

Impending Legislation

House Ways and Means Committee member Nancy Johnson (R-Conn.) and Ways and Means ranking minority member Charles Rangel (D-N.Y.) are reportedly on the verge of introducing a bill that would identify costs that would qualify for inclusion in eligible basis. (See April 2001 *LIHC Monthly Report*, p. 24.)

Industry practitioners strongly urge that proposed legislation be retroactive, which would mean that the new concept of eligible basis would apply to existing LIHC properties. "These rules [about what qualifies as eligible basis] aren't new rules and should not be interpreted as new rules," stated Novogradac. "We've got to push for retroactivity or some statement acknowledging that the rule isn't new. Otherwise, the IRS will say that Congress passed [the TAM legislation] because it wasn't law before."

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Industry Dealmakers

Washington Mutual, Inc. has acquired Fleet Mortgage Corp., which was part of FleetBoston Financial Corp. As a result of the acquisition, Washington Mutual becomes the nation's largest mortgage lender. Fleet Mortgage's mortgage servicing portfolio raises Washington Mutual's portfolio to approximately \$456 billion, as of March 31, 2001. Seattle-based Washington Mutual is a national financial services company that operates more than 2,300 consumer banking, mortgage lending, commercial banking, consumer finance and financial services offices.

Multifamily capital provider Red Capital Group recently provided \$14.8 million to refinance mortgage loans for two apartment projects. Bel Air Court Phase II, a 208-unit project located in Columbus, Ohio, obtained \$8 million in financing. Colorado Court, a 250-unit project located in Denton, Texas, obtained \$6.8 million in financing.

Red Capital Group also provided a \$8.4 million financing package comprised of bond underwriting, remarketing services, and Fannie Mae DUS bond credit enhancement for a tax-exempt refunding bond issue, as well as a conventional Fannie Mae DUS second mortgage loan to benefit a multifamily project in Midvale, Utah. Candlestick Lane Apartments is a 299-unit project located in the Salt Lake City area. Twenty percent of the units are restricted to low- and moderate-income tenants.

TAMs

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To access sample letters to Congress urging a remedy for the TAMs, visit Novogradac & Company LLP's Affordable Housing Resource Center at www.novoco.com/sampleletters.htm. To access TAMs 200043015-17 and TAMs 200044004-5, visit www.novoco.com/private_letter_rulings.htm. ❖

How the TAMs Are Impacting Key Industry Players

Accountants	<ul style="list-style-type: none"> • Choose to ignore, follow or distinguish the TAMs in connection with carryover 10 percent test, cost certifications and tax returns • Most are choosing to continue their current position with the addition of more factual certifications from clients
Syndicators	<ul style="list-style-type: none"> • More closely scrutinize what makes up eligible basis in each transaction • Modify tax credit adjuster provisions • Beef up tax credit delivery guarantees
State Housing Agency	<ul style="list-style-type: none"> • Determine whether to allow certain items in basis for initial application, carryover and cost certification purposes • Provide disclaimers in application forms
IRS Agent	<ul style="list-style-type: none"> • More confidence in making audit assertions • Appeal officers may feel politically obligated to follow the TAMs
Developer	<ul style="list-style-type: none"> • Plan for worst-case scenario (IRS audit) • Check with your accountant to make sure you know his or her position on impact fees, etc. • Cleanse development documents • Obtain factual support that the costs are includable in basis at the time costs are incurred • Watch out for 95 percent test in bond deals

Source: Novogradac & Company LLP