



NMTC Recapture Issues Capture Industry Attention

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Industry leaders are talking to and taking the pulse of potential investors for the New Markets tax credits (NMTC), and several areas of concern have arisen. One especially, the potential for recapture of the tax credits, has many new markets tax credit professionals seeking ways to mitigate such liability.

The recapture cost of NMTCs is more severe than the recapture cost of low-income housing tax credits (LIHC). An investor must increase its federal income tax liability in the year of recapture to the full extent that any NMTC produced a "tax benefit" to the investor in a prior taxable year (compared to recapture of only the one-third "accelerated portion" for LIHC). The impact of total recapture is amplified because the investor must also pay interest on the underpayment of tax for each prior taxable year, beginning on the due date of the tax return for such prior taxable year.

The recapture tax risk for NMTC (as compared to the low-income housing tax credit) is further exaggerated by its cliff effect nature. Full recapture occurs if the 85 percent "substantially all" test is failed. By comparison, the LIHC recapture for lower than promised low-income occupancy is generally proportional to the shortfall.

Because of these implications, the recapture provisions are important to CDEs and investors alike.

Industry professionals, including those from Hunter Chase & Company and Novogradac & Company LLP, have voiced their concerns to the IRS on this issue. It is felt that CDEs should be able to avoid recapture when unexpected circumstances or involuntary events occur, if and when steps are taken to correct the noncompliance or reinvestment occurs within a reasonable period of time. According to Thomas Tracy, managing director of investment banking firm Hunter Chase & Company, who appeared at the March 14, 2002 IRS hearing on temporary and proposed regulations on the New Markets tax credit: "In a controlled investment area, the uncontrollable event, involuntary conversion and other events that might occur that are outside the control of either the CDE or new markets business, there is an uncertainty that will affect price." To alleviate the uncertainty, he urged the IRS allow a reasonable cure period.

To receive all the latest NMTC news and materials for this important program as it develops, go to www.newmarketscredits.com, which features the most current information on IRS regulations and the Community Development Financial Institutions (CDFI) Fund, industry comment letters and transcripts of recent hearings and speeches.

The latest on regulations and credit allocation information will also be available at Novogradac & Company LLP's New Markets Tax Credit Conference June 5-7 in Washington, D.C. The conference is designed for investors, attorneys, developers, consultants, lenders, lawmakers and other tax credit professionals to gather and exchange ideas and opinions on this landmark new program. For more information visit www.newmarketscredits.com or call 415.356.8005. ❖

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