

Mixed Reviews for Tax Reform Proposals — LIHTC Could Suffer

By Michael J. Novogradac, CPA

On November 1, 2005, the President's Panel on Federal Tax Reform recommended two ways to remake the country's tax system. The first would greatly simplify the income tax, lowering rates somewhat, eliminating the alternative minimum tax (AMT) and doing away with or restricting most deductions and credits. The second would replace the existing income tax with a consumption-type tax that would be paid by filing an annual tax return. Each plan provides for new tax breaks for savings and investment.

According to many observers, the political system may not be ready for these changes. If they are enacted, it would be the most significant overhaul of the tax code since 1986, which produced the Low-Income Housing Tax Credit (LIHTC) program.

Gene Sperling, a senior fellow at the Center for American Progress and formerly national economic advisor in the Clinton administration, in the Daily Tax Report (DTR) praised the panel's recommendations for laying out the type of "real pain" that would be required for tax reform.

If enacted, the proposed recommendations would be more than painful to the affordable housing industry in general, and the LIHTC program in particular. While the panel did not address the LIHTC explicitly, it recommended nearly all tax preferences be eliminated. The panel then added back into its recommendations a modified mortgage interest deduction, a health-coverage incentive and an incentive for charitable giving. By its omission, the LIHTC appears to be eliminated.

However, the panel does not reject tax preferences out of hand. It would maintain tax benefits that provide incentives to change behavior in ways that benefit the economy and society, and the LIHTC does change behavior in such ways: in 2003, housing bond and tax credit programs generated 230,000 jobs, \$8 billion in wages and salaries, and more than \$4 billion in government revenue.

Washington Reaction

Reaction on Capital Hill to the panel's tax

reform recommendations was mixed. The chairman of the Senate Finance Committee, Sen. Chuck Grassley, R-Iowa, commended the report as a way to promote discussion on how to build taxpayer confidence in the tax system, and the chairman of the House Ways and Means Committee, Sen. Bill Thomas, R-Calif., noted that the recommendations were a foundation for congressional change to the tax code. The ranking Democrat on the Senate Finance Committee, Sen. Max Baucus, D-Mont., found some elements in the recommendations more desirable than others. "There are some great ideas here and some not-so-great ideas," he said. "If only this were a buffet. Unfortunately, it's a set menu, and I think overall it will not satisfy our hunger for reform and simplification." His colleague, Rep. Charles Rangel of New York, the top Democrat on House Ways and Means, called the recommendations "unfair and unwise," saying that the proposals if enacted "would hurt millions of hard-working Americans."

Industry Reaction

Mirroring congressional reaction, affordable housing leaders also gave the tax panel proposals mixed reviews. The National Council of State Housing Agencies (NCSHA) went on record as saying it is "deeply concerned" by the panel's proposed elimination of the LIHTC and "severe weakening" of housing bonds, by removing the incentive for corporations to buy them. "Housing credits and bonds are the most important tools we have for providing affordable housing to lower-income families, and the country cannot afford to lose them," said the organization in a news release dated November 2, 2005.

In addition to its concern that the LIHTC could be eliminated if the panel's recommendations were enacted, NCSHA noted the irony in panel's proposal to eliminate the housing credit and undermine housing bonds while Congress is turning to these programs to rebuild the affordable housing stock in the Gulf Coast disaster area. Additionally, the organization noted that it was just five years ago that Congress, with overwhelming bipartisan support, expanded housing credit and bond authority for the whole country by nearly 50 percent.

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David Gasson, executive director of the Housing Advisory Group, called the panel's recommendations somewhat unrealistic. "Even former Senator [John] Breaux, one of the panel's co-chairs, said that it was helpful in gaining consensus on the panel that none of the members was running for reelection," he wrote. The panel was asked for "bold, far-reaching" suggestions, and it complied, Gasson observed, but he said it is unclear what appetite the Administration or Congress will have for sweeping reform over the next year.

What's Next?

President Bush is not committed to adopting the commission's recommendations and has a free hand in developing his own proposals for Congress to consider. Indeed, he might have trouble backing many of the recommendations since he has been a committed and loud voice in calling for an "ownership" society; and many of the panel's recommendations may be viewed as discouraging an "ownership society."

Additionally, the prospects in Congress of limiting popular tax breaks are sure to be politically unpopular. "It's good to get those issues on the table, but their political viability is nil. You just can't see them happening," said Bob D. Scharin, editor of RIA's Practical Tax Strategist in an article in Market Watch. Evidence of uncertainty on the future of the panel's recommendations could be found in Treasury Secretary John Snow's comments when the panel delivered its final report. Snow called the recommendations a "starting point" for what the Treasury Department will recommend to President Bush, something he said he hoped would happen before the end of the year. There is some discussion that the president will use his 2006 State of the Union speech to present his tax reform proposals.

There is some doubt that the president's tax proposals could be ready that quickly. BNA reported on November 2 that paramount among the uncertainties that remain regarding the panels recommendations are the ways the proposals will change at the hands of Treasury and whether they will be made palatable enough to engage a bipartisan group of sup-

porters in Congress. Also in question is whether top Treasury tax-related vacancies will continue to hinder the ability to develop and advocate new tax policy — the assistant secretary of treasury for tax policy, the principal spokesperson for the Treasury Department regarding any new tax legislation, has been vacant since December 17, 2004. "It's critical that position be filled in order for Treasury to effectively assist the White House with tax policy," Gary Wilcox, Morgan Lewis & Bockius LLP partner and former IRS deputy chief counsel told BNA on November 1.

Taylor Griffin, Treasury spokesperson, said the technical assistance and analytical support work of the panel work is considered a high priority within the department and that team members meet regularly with Snow to discuss tax reform. The team of Treasury staff is led by Deputy Assistant Secretary for Tax Analysis Robert Carroll and Acting Deputy Assistant Treasury Secretary for Tax Policy Eric Solomon.

Additionally, natural disaster legislation is also commanding much of legislators' time; at the same time as Treasury is working on the panel's recommendations, Congress will be working to enact hurricane relief legislation. Any hurricane-related legislation will likely include many tax benefits, such as the LIHTC, that would be repealed if the panel's recommendations were enacted.

"With this report, it is as important as ever that we continue to work with [the members of] Congress to make certain they understand the importance of using the LIHTC as a primary tool to provide affordable housing," said Gasson. While continuing the general advocacy of the LIHTC, the affordable housing community and the nation await the next step by the Treasury Department and the White House. The next major cues will likely come in early to mid-January, as the President more discretely signals his key policy objectives for 2006. The President's State of the Union address will be most important next date in the national tax reform debate. If the President makes tax reform a key 2006 policy objective, then next year will be a turbulent time. ❖