

Novogradac Report on Tax Credits
Transcript: January 5, 2010

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(Intro music)

Happy New Year! I'm Michael Novogradac and it's Tax Credit Tuesday.

Today is Tuesday, January 5th, 2010. This week I will discuss a recent federal tax court decision regarding the treatment of a state tax credit investor as a member of a partnership. The court's decision is positive news for many investors in state income tax credits.

I will also share news about the Kansas state historic tax credit. And finally, I have a quick update on the new markets tax credit program.

But first, I commend the National Housing Trust for an excellent end of the year perspective on 2009.

In an e-mail that they sent out, they noted that although it seems like all that's being discussed in Washington, D.C. these days is health care reform, there have been a number of developments that bode well for affordable housing preservation. They go on to note the following holiday gifts:

First, Congress and President Obama approved a 2010 omnibus appropriations bill with funding for HUD programs. The project-based Section 8 program received \$8.5 billion - a 15 percent increase over 2009 - and enough, in their judgment, to protect all

Novogradac Report on Tax Credits
Transcript: January 5, 2010

Section 8 apartments up for renewal in 2010. In addition, the bill renews existing authority for a number of tools that will help preserve project-based Section 8 apartments.

Second, Fannie Mae announced new underwriting standards that should help preserve project-based Section 8 apartments. The changes are the result of recommendations from the National Housing Trust on how Fannie Mae can better meet its duty to serve affordable housing preservation. The National Housing Trust notes that new Fannie Mae underwriting considerations could potentially save hundreds of thousands of dollars in a typical Section 8 preservation transaction. Among the changes:

- in making debt decisions, Fannie Mae has agreed to accept the annual appropriations risk for Section 8 contracts;
- in certain cases, Fannie Mae will no longer require a re-stabilization reserve;
- also in certain cases, Fannie Mae will underwrite to the higher of the Section 8 or low-income housing tax credit rent.

These changes will help preserve and improve literally hundreds of thousands of apartments affordable to very low income households in America. Now that, notes the National Housing Trust, is something to celebrate.

Looking to 2010, Senators and members of the House do not get back in session until January 19th, although their staff are

Novogradac Report on Tax Credits
Transcript: January 5, 2010

around. Most commentators do not expect a jobs or mini stimulus bill to move through Congress until late January or February and possibly not until March.

However, there is a real focus on the Hill and within the Administration on jobs creation, particularly through small business. To the extent the low-income housing tax credit, new markets tax credit and energy tax credit communities can successfully explain how their legislative initiatives create jobs, then their legislative agenda should have some legislative vehicles.

The actual vehicles will be subject to much maneuvering. So stay tuned to future podcasts, and we'll cover the matter as developments warrant. We also encourage you to read the Novogradac Journal of Tax Credits.

On a specific legislative matter, late last month, on December 23rd, Senator Chuck Grassley of Iowa introduced The Heartland Disaster Tax Relief Extension Act of 2009.

This bill would extend key provisions of the Heartland Disaster Tax Relief Act. The Heartland Disaster Tax Relief Act was signed into law over 15 months ago on October 3rd, 2008. The act gave additional temporary tax relief to people living in the Midwestern disaster area, an area that experienced severe floods and tornadoes in the spring of 2008.

The Heartland Disaster Tax Relief Extension Act of 2009 would extend the authorization of Midwestern disaster states to issue debt

Novogradac Report on Tax Credits
Transcript: January 5, 2010

service tax credit bonds. These tax credit bonds provide bond investors credits against federal income tax instead of interest payments. Senator Grassley says this extension would give these states the additional time that is needed to provide assistance to communities that cannot meet their debt service requirements as a result of the flooding, tornadoes and severe storms. This extension would be through January 1st, 2011.

The bill would also remove limitations on deducting casualty losses due to natural disaster. The disaster relief legislation enacted in 2008 expanded the casualty loss rules to allow more disaster victims to claim individual property losses.

The Heartland Disaster Tax Relief Extension Act would also further expand the casualty loss rules by extending for one more year a provision that allows taxpayers to claim casualty losses or qualified disaster expenses for five years rather than two years. That is they can carry them back five years rather than two years. When taxpayers carry losses back to prior years, they get a refund of the taxes that they paid in the earlier year. Senator Grassley says this prompt refund can help them reinvest in their businesses or make ends meet in the aftermath of a disaster. The Heartland Disaster Tax Relief Extension Act of 2009 would extend the provision for one more year into 2010.

The measure would also extend for one year the provision that allows businesses that suffered damage as a result of the Presidentially-declared disasters to claim an additional depreciation

Novogradac Report on Tax Credits
Transcript: January 5, 2010

deduction. The deduction is equal to 50 percent of the cost of new real and personal property investments made in the Presidentially-declared disaster area.

A copy of the bill, which was introduced as S. 2928 can be found online at www.taxcredithousing.com. In the News menu section, simply click on Hot Topics, and then follow the link to Disaster Relief - 2008 Midwestern Storms.

In additional legislative news, the National Association of Home Builders reported last month that it had sent a letter to Senate leaders in support of an extension of the Low-Income Housing Tax Credit exchange program and the New Energy Efficient Homes Credit under Section 45L. NAHB urged the Senate to include the extensions in legislation that would extend other tax provisions that expired at the end of 2009. The letter also voiced a strong opposition to a change in the taxation of carried interest as a way to pay for for the tax extenders package.

At the time of this recording, the Senate had not yet made its tax extenders bill public, but NAHB says it will continue to press for inclusion of the LIHTC consensus proposals and the 45L credit in the package, while it reiterates its strong opposition to using a change in the taxation of carried interest as the revenue offset.

Now, let's get started with our first topic, which is good news for state tax credit investors.

On December 22nd the U.S. Tax Court ruled that state historic tax credit investors were partners for federal income tax purposes,

Novogradac Report on Tax Credits
Transcript: January 5, 2010

rather than purchasers of state tax credits. The name of the case is Virginia Historic Tax Credit Fund 2001 LP versus the IRS. In the case, the U.S. Tax Court also upheld the business purpose of the transaction and denied the IRS' assertion that the transaction was a mere sale of state tax credits.

The decision is a welcome development among state tax credit investors, because the IRS had asserted that in the case at hand, the state tax credit investor was not a partner in the partnership. Rather, the IRS argued that in substance, the investor had purchased the tax credits from the partnership and, as a consequence, the partnership could not report the amount received from the investor as a non-taxable capital contribution. The IRS argued that the investor's purported capital contribution should actually be reported as income from the sale of state tax credits. By ruling against the IRS, the court ruled that the partnership could record the amount received from the investor as a capital contribution and did not have to report the amount as taxable income.

While this case is certainly very welcome news, the historic tax credit community is still awaiting a ruling in another case. That case is the Historic Boardwalk Hall LLC v. Commissioner. This is another case where the IRS is asserting that the tax credit investor was not a partner in the partnership.

A copy of the Virginia Historic Tax Credit Fund case can be found online at www.novoco.com. Simply click on the Historic Tax

Novogradac Report on Tax Credits
Transcript: January 5, 2010

Credit Resource Center button and then click on the Resources link. A copy of the decision can be found under the Court Rulings heading.

**Speaking of state tax credits, I have related news from
Kansas about their state historic tax credit.**

The *Wichita Eagle* reported on December 24th that support is gathering in Kansas to address a recent change to the state's historic tax credit. This recent development demonstrates how significant the historic tax credit at the state level is across the nation. You see, in the spring of 2009, lawmakers in Kansas capped the amount of state tax credits that could be redeemed in 2010 and 2011. The cap was \$3.75 million per year. Supporters of the state historic tax credit are report that the new limits have put many developments on hold.

The *Wichita Eagle* reports that eliminating the cap is one of the city of Wichita's top goals during the current legislative session. Jeff Fluhr, president of the Wichita Downtown Development Corporation, told the *Eagle* that developers have used the historic tax credit on about 20 buildings in Wichita. The Wichita Downtown Development Corporation also supports restoring the tax credit program.

Kansas state Senator Carolyn McGinn has been working with groups on the tax credit program and she told the *Wichita Eagle* that while the intent was to save the state money during a revenue downturn, the change had an unintended consequence. Wichita Mayor Carl Brewer cited projects such as the Carnegie Library and the Broadview Hotel that have been put on hold as a result of the credit being capped.

Novogradac Report on Tax Credits
Transcript: January 5, 2010

State Senator McGinn warned that the tax credits might not be restored to their original level, but did say that lawmakers did not want to destroy a program that was helping with economic development.

Details of a potential fix were still being worked out at the time of this recording, but we are keeping an eye on the situation and I'll report back on any developments in future podcasts and in the state tax credit section of the Novogradac Journal of Tax Credits.

Let's shift gears now to the new markets tax credit program.

The Community Development Financial Institutions Fund has made debriefing documents available to community development entities that applied for new markets tax credits but did not receive an allocation in the last allocation round. The debriefing documents provide applicants with information about the strengths and weaknesses of their applications identified during the review process.

Applicants can access their debriefing materials through their myCDFIFund accounts at www.cdfifund.gov. These debriefing documents can be very useful tools for applicants wishing to reapply in future rounds. Unfortunately, debriefing materials are only available to unsuccessful applicants. If you'd like additional assistance from Novogradac & Company LLP assessing how you can change your application in future rounds, just give us a call at (415) 356-8000 and ask for Owen Gray, or ask for me, Mike Novogradac.

Novogradac Report on Tax Credits
Transcript: January 5, 2010

This brings us to this week's look at the Tax Credit Calendar.

If you *were* successful in a previous allocation round, I invite you to learn how to stay in compliance when completing new markets tax credit deals with Novogradac & Company's NMTC Compliance Webinar on January 12th.

Alternatively, if you'd like to learn more about the NMTC allocation award process, I invite you to join Novogradac & Company for a Pre-Conference Workshop on the NMTC Basics. The next new markets tax credit basics workshop will be presented on Wednesday, January 27th in San Diego, Calif.

The workshop precedes our next New Markets Tax Credit Conference, which will take place on Thursday and Friday, January 28th and 29th, also in San Diego. Panel discussions will cover topics including the capital markets, tips for closing transactions, combining the new markets tax credit with the historic tax credit, and much more.

And these are just three of the more than 25 events that Novogradac & Company will present over the course of this year. And to make it easier for tax credit professionals to attend multiple conferences throughout the year, we've created a season pass.

If you purchase a 2010 season pass you can attend any and all of Novogradac and Company LLP's conferences for the entire year for the cost of the season pass. A personalized coupon code will be emailed to you if you register for the pass, and when you register

Novogradac Report on Tax Credits
Transcript: January 5, 2010

online for any conference in 2010, simply enter that coupon code and the registration fee is automatically waived.

To learn more about the season pass, or to register for one of our upcoming events, please visit us online at www.novoco.com/slash/events. The pass is a real bargain and we invite you to give it some serious consideration.

I also remind our listeners that we're going to be in Miami next week hosting our annual Florida low-income housing tax credit conference. I will be there in attendance and hope to see you there.

This brings us to the end of this week's report.

Please join me again next week for more of the latest news and analysis on affordable housing, community development and renewable energy.

We also invite you to comment on the podcast. Send us an email at CPAs@novoco.com or to me, Michael.novogradac@novoco.com.

This is Michael Novogradac and I'll be back next Tuesday.
Thanks for listening.

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Novogradac Report on Tax Credits
Transcript: January 5, 2010

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