

Novogradac Report on Tax Credits
Transcript: February 23, 2010

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(Intro music)

Hello! It's Tax Credit Tuesday and I'm Michael Novogradac.

This Tax Credit Tuesday podcast is presented by Novogradac & Company, a national accounting and consulting firm. To learn more about the professional services we provide, I encourage you to visit us on the web at www.novoco.com slash services.

Today is Tuesday, February 23rd, 2010 and we have a lot in store for you this week.

This week I will describe a bill introduced in the House that would allow taxpayers who are otherwise eligible to receive a tax credit for producing renewable energy to treat the tax credit as a refundable tax payment.

The bill was introduced by Congressman Earl Blumenauer and he says the bill is designed to improve the existing Section 1603 renewable energy cash grant program that was created by the Recovery Act last year.

I will also review the proposed housing goals for government sponsored enterprises Fannie Mae and Freddie Mac. These goals were released last week.

The Housing and Economic Recovery Act of 2008, also known as HERA, gave the Federal Housing Finance Agency authority for establishing housing goals for the GSEs. FHFA is proposing a

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number of changes that would alter the way these goals have been set in the past.

But first, I have breaking news regarding the new markets tax credit.

Treasury Secretary Tim Geithner traveled to Raleigh-Durham, North Carolina last week where he met with small business NMTC recipients to discuss how the tax credits can be used to attract additional investments to help revitalize distressed communities.

Secretary Geithner toured the facilities at the Golden Belt Complex, a mixed-use property that was renovated with private financing that included NMTC equity. Secretary Geithner also participated in a roundtable discussion hosted by Self Help Ventures Fund. Self Help Ventures invested \$12 million in the renovation of the Golden Belt complex, including more than \$8 million in capital that it attracted with the help of the new markets tax credit. During the roundtable, the group discussed the challenges distressed communities face in attracting new investments, they also discussed how the new markets tax credits and other financing tools can help spur job creation and economic revitalization.

In remarks made following the roundtable, Secretary Geithner announced President Obama's proposal to improve, extend and broaden the new markets tax credit under the proposed 2011 budget.

Secretary Geithner said quote: "Distressed communities and their small businesses have a hard time attracting investments even in the best of times. The new markets tax credit helps these

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communities attract new investors and ensure they stay invested long enough for businesses to overcome obstacles and grow.” close quote

To restore demand and broaden the credit’s appeal, the President is asking Congress to change the NMTC so it can be used to offset the alternative minimum tax or AMT.

CDFI Fund Director Donna Gambrell said these latest enhancements are a part of a broader commitment on the part of the Obama Administration to increasing opportunities for small businesses and community development where it is needed most. She said and I quote: “Allowing the credit to off-set the AMT will help this tool to speed recovery in the hardest hit communities by greatly increasing its ability to attract private investors.” end quote

Secretary Geithner noted the President’s proposed 2011 budget asks for an additional \$5 billion in new markets tax credits for 2010 and another \$5 billion in 2011, for a combined amount of \$10 billion over two years.

In addition, the Treasury Department and the IRS are developing some additional guidance that could be quite helpful. This guidance includes:

1. a revenue ruling to clarify how the passive activity rules apply to investors,
2. guidance to clarify treatment of recourse loans,
3. new rules to support greater investment in institutions such as CDFIs that invest in small businesses, and
4. ways to ensure flexibility for CDEs to provide working capital and other short-term loans by weighing the effect

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of the requirement that “substantially all” of a CDE’s investments be deployed at all times.

At the North Carolina event, Secretary Geithner stressed that the Treasury Department is committed to making further enhancements to the new markets tax credit to encourage greater investment in small businesses. The following day, February 19th, senior Treasury Department officials participated in a conference call to discuss further details of Secretary Geithner’s announcement.

My partner Brad Elphick participated in the call. He reports that Gene Sperling, a counselor to Secretary Geithner, opened with comments about the commitment from Treasury. Mr. Sperling told listeners that the Administration sees these enhancements as a high priority, not a fringe issue. As evidence, he cited the fact that they are recommending extending the program at Recovery Act funding levels, or \$5 billion, instead of reducing the credit authority to the original \$3.5 billion per year provided in previous extensions. Sperling also emphasized during the call that the Treasury Department is focused on making the NMTC program work better for small businesses.

Sperling’s comments were followed by those of Assistant Secretary for Tax Policy Michael Mundaca who spoke about the three non-statutory issues that I mentioned a moment ago, namely:

1. providing clarification in the form of a revenue ruling on application of passive activity rules;
2. providing clarification in the form of a revenue ruling on the use of recourse loans in the leveraged structure; and

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3. a final longer term project to review the “substantially all” requirement and how guidance could be provided to help encourage shorter term investing.

Assistant Secretary Mundaca said the Treasury Department is specifically interested in receiving comments about the substantially all project, but it is also open to other comments.

The NMTC Working Group, which Brad Elphick, my partner, leads, is currently working on a number of comment letters on these and other issues. To learn more about the NMTC working group, simply go to www.nmtcworkinggroup.com.

We will follow these proposals and guidance projects closely and update we'll our listeners on future podcasts as developments warrant. We will also send out breaking news e-mail alerts, and post Twitter updates. On Twitter you can track my personal legislative updates, as well as updates from the firm.

Now, let's move on to a review the Renewable Energy Expansion Act.

On February 4th, Congressman Blumenauer of Oregon introduced H.R. 4599, also known as the Renewable Energy Expansion Act. This legislation would allow taxpayers to, in lieu of claiming certain energy tax credits, instead they'd be able to treat the amount of the tax credits they are eligible for as a direct payment of taxes. This direct payment approach is designed to be a substitute for the Section 1603 cash grant program that was created by the

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Recovery Act. As most of our listeners know, the Section 1603 cash grant program is currently set to expire on December 31st, 2010.

The Renewable Energy Expansion Act provides taxpayers the ability to use the new direct tax payment approach or they can continue to use the Section 1603 grant program until it expires. They get to pick the program that best meets their needs. Taxpayers, of course, could not qualify for both. Congressman Blumenauer says his bill also ensures the smooth continuation of the country's commitment to renewable energy by carrying forward the existing guidance under the cash grant exchange program, albeit applying it to the direct tax payment program. The new legislation would extend a taxpayer's ability to use the direct tax payment option until January 1st, 2013.

In addition, Congressman Blumenauer's proposal would make several technical improvements to the Section 1603 program.

First, the bill would eliminate an unintended consequence of the normalization rules that limit the ability of regulated utilities to develop renewable power facilities, even if the projects otherwise meet the prudence tests required by their public utilities commissions.

Second, the legislation would improve the investment climate for renewable energy projects by streamlining access to these investments by investment funds that have tax-exempt investors. Congressman Blumenauer says that the proportional disallowance rules that are part of the legislation provide an important balance between protecting federal investments while opening up increased sources of development capital for renewable power developers. In

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that same vein, this legislation adopts changes that will increase the ability of real estate investment trusts to access these investments thereby expanding the pool of available investment capital for these projects.

In introductory remarks about the bill, Congressman Blumenauer said it is important to emphasize that the regulatory guidance that has been developed under the Recovery Act's Section 1603 grant program will be adopted by this legislation. He said, and I quote, "It is important for the renewable energy industry—and for the investment community that supports it—to have certainty in the nature of the federal commitment. Having built a smoothly functioning guidance structure under the 1603 program, it provides no benefit to unsettle that understanding. It is my expectation that within 60 days of the enactment of this legislation, the Treasury Department will issue guidance integrating the existing guidance into this new framework." close quote.

This new direct tax payment approach does have some structural weaknesses. As noted by Greg Jenner, in a blog published by the Stoel Rives law firm, the bill treats the amount that would otherwise be paid as a grant as a payment of tax which can be refunded. The payment could be claimed as a refund on the claimant's tax return. However, as written, the refund would not be paid until 45 days after the tax return was due to be filed. This could mean that instead of receiving the refund under the cash grant program within 60 days of placement in service, as under the 1603 cash grant program, the claimant may have to wait as long as 15

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months. There would be no circumstance in which the waiting time would be shorter than 150 days as opposed to the current 60 days.

Upon introduction, the Renewable Energy Expansion Act was referred to the House Ways and Means Committee. At the time of this recording the bill had nine cosponsors. You can track the progress of the bill and review related information online at

www.energytaxcredits.com Simply click on Legislation in the main menu.

Finally for this week's podcast, let's consider the affordable housing goals that have been proposed for Fannie Mae and Freddie Mac.

On February 17th, the Federal Housing Finance Agency, or FHFA, released a proposed rule to establish new single-family and multifamily affordable housing goals for government sponsored enterprises Fannie Mae and Freddie Mac.

The proposed rule contains single-family home purchase goals and goals for single-family refinance mortgages. Separately, FHFA proposes multifamily goals for the GSEs for low- and very low-income families. The GSEs will also be required to report their funding levels for low-income units in small multifamily properties.

The Housing and Economic Recovery Act, or HERA, requires FHFA to consider the following six factors in setting multifamily special affordable housing goals:

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(1) national multifamily mortgage credit needs and the ability of the GSEs to provide additional liquidity and stability for the multifamily mortgage market;

(2) the performance and effort of the GSEs in making mortgage credit available for multifamily housing in previous years;

(3) the size of the multifamily mortgage market for housing affordable to low-income and very low-income families, including the size of the multifamily markets for housing of a smaller or limited size;

(4) the ability of the GSEs to lead the market in making multifamily mortgage credit available, especially for multifamily housing affordable to low-income and very low-income families;

(5) the availability of other public subsidies; and

(6) the need to maintain the sound financial condition of the GSEs.

The notice that FHFA released on February 17th includes a discussion of its analysis for each of these six factors. In its discussion regarding the fifth point about the availability of public subsidies the notice discusses the low-income housing tax credit's decline in value.

The 2010-2011 multifamily goals for Fannie and Freddie would be based on the numbers of affordable dwelling units financed, rather than being specified in minimum dollar terms. Following the release of these proposed goals, the National Council of State Housing Agencies invited interested parties to send comments on the proposal to Garth Rieman for inclusion in NCSHA's comments.

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In addition to the proposed housing goals, FHFA announced that it plans to issue two related proposed rules in the near future regarding affordable housing goals for the Federal Home Loan Banks and the GSEs duty to serve rule.

Novogradac & Company is reviewing the available information in more detail and we'll be reporting on the proposed goals and what they could mean for the affordable rental housing market in an upcoming edition of our flagship publication, the Novogradac Journal of Tax Credits.

If you have not had a chance to check out our monthly magazine about affordable housing, community development and renewable energy tax credits, I encourage you to send an email to products@novoco.com and request a free sample copy.

On the Tax Credit Calendar front, I note that this Thursday, February 25th, CDFI Fund Director Donna J. Gambrell will provide remarks at the Northside Community Development Fund's 3rd Annual Awards Luncheon in Pittsburgh, Pennsylvania.

We will be monitoring her remarks and we'll send tweets and breaking news e-mails to the extent her comments warrant.

Looking ahead I expect plenty of breaking news for the tax credit community on the horizon.

The House and Senate are back in session this week after returning from their district and state work periods, also known as

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recesses. In addition to jobs legislation, a number of lawmakers are pushing for a package of tax extenders, including the extension of the new markets tax credits that I discussed today. There's also the credit exchange grants and host of other provisions that we've discussed in prior podcasts.

Well, that brings me to the end of this week's report.

I'd like to remind our listeners that we really appreciate your emails, so keep them coming; send them to cpas@novoco.com.

This is Michael Novogradac and I'll be back next Tax Credit Tuesday.

Thanks for listening.

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