

Novogradac Report on Tax Credits
Transcript: March 2, 2010

Total Word Count: 2966

(Intro music)

Hello! I'm Michael Novogradac. Welcome to another Tax Credit Tuesday.

Today is Tuesday March 2nd, 2010.

This week I will discuss the Administration's Healthy Food Financing Initiative.

The proposal announced last month would provide access to nutritious foods in underserved communities using a number of financial incentives, including \$250 million in New Markets Tax Credit allocation authority.

I will also review Freddie Mac's summary of its fourth quarter and full-year 2009 financial results.

In a press release last week, Freddie Mac revealed that it wrote down the carrying value of its low-income housing tax credit investments to zero as of December 31st, 2009, as it will not be able to realize any value either through reductions to its tax liabilities or through a sale to a third party.

And finally, I will share a summary of a letter that California Governor Arnold Schwarzenegger sent to the Treasury Department about the eligibility of certain types of geothermal

Novogradac Report on Tax Credits
Transcript: March 2, 2010

projects for the Section 1603 renewable energy cash grant program.

His letter asks for specific guidance on Hudson Ranch Power, which is a 49-megawatt geothermal project being developed near the Salton Sea in Imperial County, California.

But first, this week's top story is tax extenders legislation.

After passing a pared down jobs bill last week, it's likely that the Senate will turn this week to a tax extenders bill that would address tax provisions that expired in 2009. On February 24th, Senator Harry Reid circulated an extenders proposal called the American Workers, State, and Business Relief Act of 2010.

The package would extend the Section 1602 low-income housing tax credit cash grant exchange program that was created by the Recovery Act. The bill would also extend the new markets tax credit for one year. The package of tax extenders is estimated to cost about \$31 billion over 10 years. One of the cost offsets included in the bill is codification of the economic substance doctrine. Also in the bill is an extension of the new markets tax credit.

The Housing Advisory Group reports that there is some thought that the extenders bill will continue to focus primarily on expired provisions. This would make it more difficult to include any additional provisions from the LIHTC agenda of consensus proposals.

However, the group does expect that there will be additional legislative vehicles that could carry the two consensus proposals that

Novogradac Report on Tax Credits
Transcript: March 2, 2010

are not currently included in the extenders bill, namely the two 5-year carryback provisions and changes to passive activity tax benefit limitation rules. For example, Senator Reid has already expressed his intent to move several additional jobs-related bills, and the Housing Advisory Group reports that the House is exploring a jobs bill that would focus more on tax incentives.

**In related news, on February 24th, California
Congresswoman Linda Sanchez introduced H.R. 4687, the Low
Income Housing Tax Credit Exchange and Job Creation Act of
2010.**

This legislation would include housing tax credits arising from tax-exempt multi-family housing bonds in the Section 1602 cash grant program. The bill would also clarify that states have the option to loan the exchange funds, not just grant them. Supporters say this change would correct misinterpretations of congressional intent under Section 1602 by various federal agencies and the unintended tax problems and additional wage costs that arose from those misinterpretations.

H.R. 4687 would also make any Internal Revenue Service recapture of exchange funds proportional to the number of units and amount of time over which the units were not serving eligible LIHTC households.

The bill would also clarify that tax credit allocating committees can charge additional fees to administer the Section 1602 program. This change would allow allocating agencies to hire additional help to

Novogradac Report on Tax Credits
Transcript: March 2, 2010

process these awards while also running their existing LIHTC programs.

Reports indicate that the bill is intended to be part of the jobs bills that Congress is already considering, so it's not expected to take the traditional path to enactment that a stand-alone bill would take. Instead, supporters hope that the leaders of key congressional committees will make the case for these provisions to be included in the next piece of jobs legislation.

Stay tuned to our web site and follow me on Twitter for ongoing updates as these bills progress. On Twitter, just search for Novogradac -n-o-v-o-g-r-a-d-a-c- and you will find me. I send periodic tweets on affordable housing, renewable energy and community development tax news, as conditions warrant.

Now, let's move on to the latest new markets tax credit news.

On February 19th the Obama Administration released details of a Healthy Food Financing Initiative. The initiative is designed to expand access to nutritious foods in underserved communities that are not served by grocery stores or other healthy food retailers. The initiative will make available more than \$400 million in federal tax credits, below-market rate loans, loan guarantees and grants to attract private sector capital, all of which are expected to more than double the total investment. Included in this mix of financing tools is

Novogradac Report on Tax Credits
Transcript: March 2, 2010

\$250 million in authority for the New Markets Tax Credit program devoted to helping finance healthy food options.

Through the joint initiative, which was included in the President's proposed budget for 2011, the departments of Treasury, Agriculture, and Health and Human Services would make available financial and technical assistance to community development financial institutions, not-for-profits and businesses with sound strategies for addressing the healthy food needs of communities.

Communities without access to grocery stores or other healthy food retailers are sometimes called "food deserts." The Administration says its proposal builds on the CDFI Fund's history of supporting these kinds of investments through the NMTC program. In fact, the January issue of the Novogradac Journal of Tax Credits features an article about how the NMTC has helped bring grocery stores to food deserts. A copy of that article is available in the Archive section of the Journal web site at www.novoco.com slash journal.

The U.S. Department of Agriculture estimates that nationwide 23.5 million people, including about 6.5 million children, live in low-income areas that are more than a mile from a supermarket. With the first year of funding, the Administration says its initiative will leverage enough investments to begin expanding healthy foods options into as many as one-fifth of the nation's food deserts.

The administration says that well-targeted financial and technical assistance can create viable businesses that not only improve food options, but also create jobs, help revitalize distressed

Novogradac Report on Tax Credits
Transcript: March 2, 2010

communities, and open up new markets for farmers to sell their products, all of which can provide an economic boost to rural America.

To learn more about the Healthy Food Financing Initiative, I encourage you to visit www.newmarketscredits.com where we have posted a description of the proposal. For additional information, I also encourage you to contact my partner Owen Gray, at owen.gray@novoco.com. Owen works extensively in the new markets tax credit area.

Next, let's move on to the low-income housing tax credit and consider Freddie Mac's summary of its fourth quarter and full-year 2009 financial results.

Freddie Mac last week reported a net loss of \$6.5 billion for the quarter that ended December 31st, 2009, and a total net loss of \$21.6 billion for the full-year 2009.

Freddie Mac reports that these loss amounts included a 4th quarter write-off of its Low-Income Housing Tax Credit portfolio of \$3.4 billion, and a full 2009 year write-off of \$4.2 billion.

Yes, that is \$4.2 billion dollars in additional 2009 losses from the write-off of their entire LIHTC portfolio.

In its statement, Freddie Mac says it played a critical role in supporting the nation's housing market in 2009 by providing \$548.4 billion of liquidity to the mortgage market, helping finance

Novogradac Report on Tax Credits
Transcript: March 2, 2010

approximately 2.2 million conforming single-family loans and approximately 253,000 units of multifamily rental housing.

Before it was placed in conservatorship, Freddie Mac also supported the LIHTC market as a nationwide investor. The company's presence in multi-investor funds enabled smaller investors to participate in much larger pools of projects and helped to attract investment capital to areas that would not otherwise have seen such investments. As most listeners know, Freddie Mac currently has no ability to use the tax credits on its tax returns, hence the write-off of its LIHTC portfolio, and accordingly did not invest in any LIHTC partnership investments in 2008 or 2009.

Freddie Mac says that during the third quarter of 2009, it expected that its ability to realize the carrying value in its LIHTC investments was limited to its ability to execute sales or other transactions related to its partnership interests. This determination is based on a number of factors, including continued uncertainty in its future business structure and its inability to generate sufficient taxable income in order to use the tax credits and operating losses generated. As a result, Freddie Mac says it determined that individual partnerships whose carrying value exceeded fair value were other-than-temporarily impaired and should be written down to their fair value.

As many listeners also know, during 2009 Freddie Mac requested approval from Treasury to resyndicate existing LIHTC investments.. Freddie Mac says the resyndication was designed to

Novogradac Report on Tax Credits
Transcript: March 2, 2010

recover substantially all of the carrying value of its LIHTC investments. In November 2009, the Federal Housing Finance Agency, or FHFA, notified the company that the Treasury Department, based on broad overall taxpayer issues, would decline - yes decline - to authorize the transaction. However, Freddie Mac says it was encouraged by FHFA to consider other options that would allow the company to realize the carrying value of its investments consistent with its mission and to minimize its losses from carrying these investments. Freddie Mac says it estimated that its LIHTC investments had a total fair value of \$3.4 billion at December 31st, 2009, absent -that's right absent - any restriction on sale of the assets.

On February 18th, 2010, Freddie Mac received a letter from the acting director of FHFA stating that the agency had determined that any, that's right any, sale of the LIHTC investments by Freddie Mac would require Treasury's consent under the terms of the purchase agreement. The letter also stated that FHFA had presented other options for Treasury to consider, including allowing Freddie Mac to pay senior preferred stock dividends by waiving the right to claim future tax benefits of the LIHTC investments. However, after further consultation with Treasury and consistent with the terms of the purchase agreement, FHFA informed Freddie Mac that it could not, that's right not, sell or transfer the assets and that FHFA saw no other disposition options. As a result, Freddie Mac says it wrote down the carrying value of its LIHTC investments to zero as of December 31st,

Novogradac Report on Tax Credits
Transcript: March 2, 2010

2009, as it will not be able to realize any value either through reductions to its tax liabilities or through a sale to a third party. The company recognized the write-down of the LIHTC investments as a loss of \$3.4 billion.

Freddie Mac says that it will fulfill all contractual obligations under the LIHTC partnership agreements, and continue to hold and manage the LIHTC assets in support of multifamily affordable housing as directed by FHFA. As of December 31st, 2009, Freddie Mac reports that it has obligations in the amount of \$217 million to continue to fund its existing LIHTC partnership interests over time, obligations that it is contractually obligated to make.

Additional information about Freddie Mac's LIHTC investments and obligations is available from the company's web site at www.freddiemac.com.

We here at Novogradac & Company welcome listener feedback as to what they think the consequences of this write-down is on the broader LIHTC investor market. Please send your emails to CPAs@novoco.com.

To learn more about the future of Freddie Mac and its role in the affordable housing market, I invite you to join Novogradac & Company on May 13th and 14th for our Affordable Housing Conference in New Orleans. Please save the date on your calendar and stay tuned for details about the event in future podcasts.

Novogradac Report on Tax Credits
Transcript: March 2, 2010

Our final topic for today is guidance requested last month by Governor Arnold Schwarzenegger about the eligibility of geothermal projects for the Section 1603 renewable energy cash grant program.

On February 5th, Governor Schwarzenegger wrote a letter to Treasury Secretary Tim Geitner seeking assistance in California's efforts to generate more renewable energy. In his letter, the Governor requests the Department of Treasury to verify the Hudson Ranch Power project's eligibility for the Section 1603 cash grant program, which was created by the Recovery Act. Governor Schwarzenegger also asks Treasury to issue clarifying program guidance about the eligibility of these types of geothermal projects.

Hudson Ranch Power is a \$350-million, 49-megawatt geothermal project being developed near the Salton Sea in Imperial County, California. Governor Schwarzenegger says the project is a critical economic development initiative in Imperial County, which has the highest unemployment rate in the entire United States. According to Imperial County and the project's developers, construction was ready to begin last month. Construction for the project is expected to span 21 months and create 125 full-time equivalent jobs. Governor Schwarzenegger says that power production operations would commence in November 2011 with 40 full time equivalent jobs.

Under the Treasury Department's Program Guidance for the Section 1603 program, if the property is placed in service after December 31st, 2010, then the documentation submitted to Treasury

Novogradac Report on Tax Credits
Transcript: March 2, 2010

must be able to show that construction began on or after January 1st, 2009. Furthermore, construction is considered to have commenced “when physical work of a significant nature begins” and that “physical work” does not include preliminary activities such as planning or designing, securing financing, exploring or researching.

In his letter, Governor Schwarzenegger urges the Treasury Department to issue clarifying language to define eligible, drilling-related pre-construction costs. His letter seeks guidance verifying that geothermal power wells drilled as part of required exploratory resource verification meet this exclusion and don't trigger the “commencement of construction” yet.

It appears at this project that some of this work had been done prior to January 1st, 2009 and investors were concerned that such pre-drilling work, or early drilling work, could trigger commencement of construction and therefore make the project ineligible for the Section 1603 program.

The Governor says that without the Section 1603 cash grant eligibility clearly established, the Hudson Ranch Power project cannot commence construction financing. We'll keep you posted on any additional guidance that we receive from Treasury with respect to the definition of commencement of construction.

**Next we have a new feature for the Tax Credit Tuesday
Podcast called “Did You Know?”**

Novogradac Report on Tax Credits
Transcript: March 2, 2010

Did you know that Novogradac & Company offers a variety of services to support applicants for Section 1603 renewable energy cash grants? As part of a Section 1603 application, applicants must submit documentation to support the cost basis claimed for the renewable energy property. For properties that have a cost basis in excess of \$500,000, applicants must submit an independent accountant's certification attesting to the accuracy of all costs claimed as part of the basis of the property. Novogradac has extensive experience certifying project costs that are eligible and includable in energy basis. The Novogradac team can also assist in the preparation of the required application and registration to ensure the information submitted is complete and satisfactory. For more information, please contact my partner Stephen Tracy in our San Francisco office, at 415-356-8000.

In addition, Section 1603 applicants that are lessors of energy property may elect to pass through the grant payment to a lessee. The election will treat the lessee as having acquired the property for an amount equal to the independently assessed fair market value of the property on the date the property is transferred to the lessee. Novogradac & Company can provide applicants with the required independent assessment of fair market value conducted in accordance with the requirements of the Section 1603 program. For more information on our Section 1603 valuation services, please contact one of my partners in our Maryland valuation office. Contact either Blair Kincer or Brad Weinberg, at 240-235-1701.

Novogradac Report on Tax Credits
Transcript: March 2, 2010

Listeners can also see a full menu of Novogradac & Company's renewable energy services online at www.novoco.com slash services.

Before we wrap up this week's podcast, let's look at the Tax Credit Calendar.

We learned last week that the House Financial Services hearing entitled "Housing Finance and the Path to Reform" that was originally scheduled for today, March 2nd, has been postponed to a date and time to be announced later. The hearing is expected to be one of the first steps in the legislative process to determine the future of housing finance and the federal government's role in responsible homeownership and the supply of affordable rental housing. We will update you in a future podcast when the hearing is rescheduled.

Also this week, the National Conference of State Historic Preservation Officers is holding its National Historic Tax Credit Conference. Tomorrow, March 3rd through Friday, March 5th, historic tax credit stakeholders will meet and discuss how to make sense of current circumstances and how to position historic tax credit projects and the historic preservation industry for recovery.

Looking ahead, the federal bank and thrift regulatory agencies and the Community Development Financial Institutions Fund announced last week that they will host a National Interagency Community Reinvestment Conference in New Orleans, Louisiana, from March 14th to the 18th. This biennial conference is designed to

Novogradac Report on Tax Credits
Transcript: March 2, 2010

offer participants from around the country the opportunity to learn about the Community Reinvestment Act, or CRA, and its related regulations, as well as the chance to discuss best practices and emerging challenges in community development. Details are available online at www.occ.gov.

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

Please join me again next week for more of the latest tax credit news.

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

(outro music)

Editorial material in this transcript is for informational purposes only and should not be construed otherwise. Advice and interpretation regarding tax credits or any other material covered in this transcript can only be obtained from your tax advisor.

© Novogradac & Company LLP, 2010 All rights reserved.

Reproduction of this publication in whole or in part in any form without written permission from the publisher is prohibited by law. For reprint information, please send an e-mail to cpas@novoco.com.