

Novogradac Report on Tax Credits **Summary: August 31, 2010**

Michael J. Novogradac, CPA, shares an update on tax extenders; reviews the recently released report from the Tax Reform Subcommittee of the President's Economic Recovery Board; summarizes recently updated guidance released by the Treasury Department regarding recapture under the Section 1602 low-income housing tax credit cash grant program; discusses some upcoming, critical deadlines for new markets tax credit allocates, and a bill being considered in California to create a state NMTC; highlights the Maryland Sustainable Communities Rehabilitation Tax Credit Program; examines a report that details the impact of three major renewable energy subsidies; and closes with tax credit tidbits.

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TAX EXTENDERS UPDATE

- As a follow-up to our discussion last week, word has it that Senate Finance staff hope to have a draft extenders bill out by the end of this week.
- As our listeners know, a couple of weeks ago, we heard that staff wanted to get a draft out by the end of the month.
- That date has slipped to a goal of before Labor Day.
- We hear that the draft bill will include the extenders that are of most concern to our listeners, including:
 - the extension of the Section 1602 LIHTC cash grant program
 - extension of the New Markets Tax Credit through 2010 with \$5 billion in allocation authority
 - and AMT relief for QEIs issued between March 15, 2010 and January 1, 2012.
- We believe one of the reasons for the delay are efforts to identify acceptable revenue raisers that will allow the extenders bill to be fully paid for.
- Prior versions of the tax extenders were fully paid for, but some of those “pay fors” were used to pay for the \$26.1 billion state fiscal aid bill that recently became law.
- Congress is still scheduled to return on September 13th, and we expect that the small business bill will be debated in the Senate first, then, hopefully shortly thereafter, consideration will be given to the extenders bill.
- Stay tuned. We will provide updates on Twitter and through breaking news e-mails as developments warrant.
- We will also discuss the status of extenders in next week’s Tax Credit Tuesday podcast.

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OTHER NEWS

PERAB Tax Reform Subcommittee

- The President's Economic Recovery Advisory Board (PERAB) held a public meeting on Friday, August 27 via conference call.
- The meeting was open to the public via live audio stream on the White House web site.
- The purpose of the meeting was to continue discussion of the issues impacting the strength and competitiveness of the nation's economy.
- The discussion included an update on the research and preparatory work conducted in a PERAB subcommittee.
- PERAB has been considering tax reform proposals for more than a year and last week the tax reform subcommittee presented a report during the meeting on those proposals.
- The report discusses the pros and cons of a spectrum of reform ideas relating to tax reform, without taking a position on those ideas.
- The PERAB voted unanimously in favor of presenting the report from the tax reform subcommittee as formal advice to the President.
- It is important to reiterate that presenting the report to the president does not mean the board supports any of the proposals included in the document.

Tax Expenditures

- There are a number of proposals included in the report but the item of most direct relevance to listeners is the discussion of reducing or eliminating tax expenditures.
- Tax expenditures are generally defined as reductions in income tax liabilities that result from special, targeted tax provisions or regulations that provide tax benefits to particular taxpayers.
- This category includes the low-income housing tax credit (LIHTC), new markets tax credit (NMTC), historic tax credit (HTC), renewable energy tax credit (RETC) and similar tax credit programs.
- Each year the Joint Committee on Taxation staff publishes a report on tax expenditures
 - According to the most recent JCT report, the low-income housing tax credit program is expected to cost approximately \$30 billion dollars during the five year period between 2009 and 2013.
 - That \$30 billion estimate for LIHTC expenditures *includes* \$3.4 billion for the estimated cost of the LIHTC cash grant election created by the American Recovery and Reinvestment Act.
 - The federal expenditure for RETC programs under Section 45 and Section 48 is estimated at \$7.9 billion.
 - The estimated federal expenditure for the HTC program between 2009 and 2013 is \$3.6 billion.

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- The expenditure for the NMTC program under Section 45D is estimated at \$3.5 billion.
- In its report, the tax reform subcommittee specifically addresses the low-income housing tax credit in the tax expenditure discussion, noting that some experts suggest that other federal aid, such as housing vouchers, would assist low-income households at a lower cost.
- This is an idea I have debated in the past; to hear my arguments against this position I encourage you to download the archived Tax Credit Tuesday podcast from November 10, 2009.
- I also discuss tax expenditures and the proposals that are being considered to change them in my Washington Wire column in the September issue of the Novogradac Journal of Tax Credits.
- You can read that column online at www.novoco.com/journal.
- Please share your thoughts on the topic, by sending me an email at michael.novogradac@novoco.com.

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LOW-INCOME HOUSING TAX CREDIT NEWS

Section 1602 Recapture Guidance

- In a survey of all state housing finance agencies participating in the Tax Credit Assistance Program (TCAP) and Section 1602 cash grant exchange program, the Government Accountability Office (GAO) found that those state agencies would like more guidance on recapture.
- In response, the Treasury 1602 program team released a guidance document on August 25 that discusses recapture under the Section 1602 program.
- The guidance document:
 - defines a recapture event,
 - explains how to determine the amount of funds owed,
 - describes state agencies' obligations to enforce the provisions of the program,
 - discusses due diligence and avoiding noncompliance,
 - lists possible actions a state agency could take in the event of noncompliance, and
 - instructs state agencies on how they should report noncompliance.
- In the guidance, the Treasury Department says that in the event of noncompliance the state agency has the discretion to work with the building owner to avoid recapture and bring the building into compliance.
- Treasury provided a list of actions it says are meant to assist state agencies in determining best practices. Some of those actions are:
 - working with subawardees to create a plan with milestones and schedules to remedy an incidence of noncompliance,
 - looking for a new owner who will bring the building into compliance,
 - sending a written demand notice to the owner requiring repayment in full, or
 - agreeing to a repayment plan if the state agency determines that is the best means to obtain payment.
- If, despite the efforts of the state agency, an owner does not bring the building into compliance or the state agency is unable to find a new owner to take over the building, Treasury says it expect the state agency to take reasonable action to recapture the funds.
- Reasonable action, according to Treasury, depends on the remedies available under state law as well as the particular facts and circumstances of the situation.
- An item of particular interest is that the guidance clarifies that if the state agency is unable to collect the recapture amount from the liable party, the Treasury Department would not, that's right, **NOT** require the state agency to return the recapture penalty, provided the state agency took all appropriate actions to collect the funds.
- A copy of the guidance can be downloaded from www.taxcredithousing.com. Simply click on Hot Topics in the News menu.

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- Questions about Section 1602 compliance can be directed to my partner Mike Morrison in Novogradac & Company's San Francisco office. He can be reached at (415) 356-8000. Or by e-mail at michael.morrison@novoco.com.

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NEW MARKETS TAX CREDIT NEWS

Upcoming Deadlines for Existing New Market Tax Credit Allocatees

- Section 3.2 of the allocation agreement sets out the authorized uses of a new markets tax credit allocation for investments or reinvestments.
- NMTC allocatees are generally required under Section 3.2(e) of the allocation agreement to have issued at least 60 percent of the total dollar amount of their qualified equity investments or QEIs related to its NMTC allocation by September 30.
- This means that allocatees who received NMTC awards in the 5th round of tax credit allocations in 2007 must have issued at least 60 percent of their QEIs by September 30, 2010—that is just one month from the time of this recording.
- If allocatees think they will have trouble meeting this deadline, we encourage them to contact the CDFI Fund to let them know.
- Looking ahead,
 - allocatees from the 6th who were awarded tax credits in 2008 will have to meet this 60 percent QEI issuance threshold by September 30, 2011, and
 - 7th round allocatees will have to satisfy this requirement by September 30, 2012.
- If an allocatee still needs to issue QEIs to meet this requirement, they are encouraged to communicate the status of any pending commitments to the CDFI Fund as soon as possible to at least start a dialogue with the CDFI Fund.
- Any allocatee who has not satisfied this requirement or is unsure of their status is advised to contact their tax advisor as soon as possible.
- Similarly, the new markets tax credit program regulations require allocatees to issue 100 percent of their QEIs within 5 years of the date the CDE enters into an allocation agreement.
- So, Round 3 allocatees should be aware of this deadline in relation to when they signed their allocation agreements.
- If you have any questions or if you are uncertain about the status of your QEI issuance, I invite you to call one of Novogradac & Company's new markets tax credit professionals.
- You can find information about the firm's NMTC services online at www.novoco.com. Simply click on the Services button and then choose the link to Brochures and Flyers.

Turning to the State of California for a moment, the California State Legislature is considering a California State New Markets Tax Credit

- On August 12, Senate Bill 1316 passed out of the Senate Appropriations Committee with a 7 to 4 vote.

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- The bill is authored by Senator Gloria Romero and would establish a new tax credit program modeled after the federal New Markets Tax Credit program,
- S.B. 1316 would provide \$44 million in tax credit investments in schools, small businesses and real estate throughout California in low-income communities in rural and urban areas if the bill becomes law.
- The new program would be funded by taxing, for California income tax purposes, federal Section 1031 like-kind exchanges, when a California property owner exchanges their business property for a property located outside of California.
- Based on results in other states that have enacted similar programs, supporters of the measure say the advantage of creating a state NMTC in California is that it will help attract more federal NMTC investments in California. Supporters expect the additional investment in California will exceed the tax cost of the California state NMTC.
- For some states this ratio has been reported to be as high as 13 to 1.
- At least nine other states have already enacted similar programs to help attract, and therefore leverage, more federal NMTC dollars to their states. These nine states are:
 - Ohio,
 - Florida,
 - Missouri,
 - Louisiana,
 - Mississippi,
 - Kentucky,
 - Illinois,
 - Oklahoma, and
 - Connecticut.
- Links to those programs can be found online at www.newmarketscredits.com.
- The bill now goes to the Senate floor, where if successful it will move to the Assembly.
- A copy of S.B. 1316 can be found online at www.newmarketscredits.com.
- We'll keep you updated in future podcasts if the bill makes progress.

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HISTORIC TAX CREDIT NEWS

Maryland Sustainable Communities Rehabilitation Tax Credit

- Applications are now being accepted for a total of \$10 million in tax credits for qualified commercial building rehabilitation projects in Maryland.
- The Maryland Sustainable Communities Rehabilitation Tax Credit Program was created in April with the passage of House Bill 475.
- The new law replaces the former Maryland Heritage Structure Rehabilitation Tax Credit by expanding the tax credit beyond historic building renovations to broader areas of revitalization, including commercial properties in Main Street areas.
- The new tax credit is also one of the first in the nation to link LEED high-performance green building standards with historic preservation.
- The tax credit is available for income-producing properties including office, retail, and rental housing, at different credit levels based on property type:
 - 20 percent credit for certified historic structures;
 - 25 percent credit for certified historic structures that are high-performance buildings (LEED Gold certified or the equivalent); and
 - 10 percent credit for non-historic qualified rehabilitated structures.
- The total amount of Commercial Rehabilitation Tax Credits distributed each year is based on an annual appropriation in the state's operating budget.
- The *Baltimore Business Journal* reported last week that the program is garnering tepid interest despite the state broadening it to include more projects.
- However, Rodney Little, executive director of the Maryland Historic Trust, which administers the program, tells Novogradac & Company that the Trust typically doesn't receive 90 percent of applications until the last two days before the deadline, so he was not surprised to have only a handful of applications at this point.
- He did acknowledge that they have received fewer inquiries about the program so far this year than in previous years, however he attributes this dampened interest to the recession rather than the program change.
- He says developers are having trouble finding outside financing that would allow them to take advantage of the credits.
- Mr. Little encourages developers to consider applying. He says for those who are familiar with the past program, it has not changed in any ways that make it more onerous. He also encourages developers that may be eligible for new components to consider applying.
- The Maryland Historical Trust will accept commercial rehabilitation tax credit applications until September 15, 2010.
- Details about the tax credit and instructions for applying can be found online at mht.maryland.gov.

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- Questions can also be directed to my partner Charlie Rhuda, in Novogradac's Boston and Maryland offices. He can be reached at (617) 330-1920 or send an e-mail to CPAs@novoco.com

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RENEWABLE ENERGY TAX CREDIT NEWS

Sample Annual Report for Section 1603

- Last week the Treasury Department posted a sample annual performance report and certification for the Section 1603 renewable energy tax credit cash grant program.
- All applicants that receive awards under the Section 1603 program are required to report certain information annually to the Treasury Department for a period of five years.
- Reports are due annually, 30 days after the anniversary date of the date the property was placed in service.
- The form used to submit this report is completed and submitted through the online application system.
- The Treasury Department says applicants will receive a reminder notification via email 30 days before the report is due.
- A copy of the sample report and related information can be found online at www.energytaxcredits.com.

Report on Recovery Act Programs

- On August 25 Vice President Joe Biden unveiled a new report, "The Recovery Act: Transforming the American Economy through Innovation."
- The report finds that the Recovery Act's \$100 billion investment in innovation is not only transforming the economy and creating new jobs, but helping accelerate significant advances in science and technology that cut costs for consumers, save lives and help keep America competitive in the 21st century economy.
- The report cites three programs that are driving the manufacturing and deployment of renewable energy technology:
 - the 1603 Payments-In-Lieu-Of-Tax-Credits program,
 - the 48C Manufacturing Tax Credit program, and
 - loan guarantees.

Section 1603 Program

- To date more than \$3 billion in payments-in-lieu-of-tax -credits have been made to more than 500 projects in 44 states to support renewable energy generation projects
- These fund support more than 10,000 construction jobs and more than 2,000 ongoing operating and maintenance jobs.
- The report says the Section 1603 program leverages \$2 of private capital for every \$1 of tax credits and has brought more than 4 GW of new renewable energy online

Section 48C Manufacturing Tax Credits

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- More than \$2 billion in tax credits have been allocated to 183 projects in 43 states for clean energy manufacturing projects
- The report notes that competition for the program was more than 3 times oversubscribed
- And like Section 1603, the Section 48C program leverages \$2 of private capital for every \$1 of tax credits.

Loan Guarantees

- The report discusses \$2 billion in conditional or closed loan guarantees
- The funded projects are expected to create or save more than 5,000 construction and permanent jobs, lead to more than 3 GW of clean power generating capacity, and avoid more than 30 million tons of CO2 per year, according to company estimates.
- The report says the loan guarantees leverage more than \$4 of debt and equity for every \$1 of loan guarantee subsidy.

More information

- A copy of the report can be found online at www.energytaxcredits.com.
- Questions about leveraging these programs to develop or invest in renewable energy can be directed to my partner Stephen Tracy at (415) 356-8000.

Recent Energy Legislation

- On August 20th, Senator Kent Conrad met with the management and employees of Minnkota Power Cooperative to discuss legislation he introduced to encourage investment in energy from clean coal sources.
- Senator Conrad's Coal Energy Bridge Act would expand the use of clean coal technology.
- The legislation — authored with Sen. Orrin Hatch — creates tax incentives to encourage private investment into clean coal technology.
- Specifically, it creates a 30 percent investment tax credit for coal facilities that utilize advanced technologies to capture and reduce carbon dioxide emissions from their facilities.
- A copy of the bill can be found online at www.energytaxcredits.com.

Legislative Fix Sought to Remedy PACE Situation

- BNA reported last week that proponents of Property Assessed Clean Energy, or PACE, bond financing of energy-efficiency retrofits are working to include a provision in prospective government-sponsored enterprise reform legislation to resolve concerns that the programs pose a threat to home mortgages.
- As most listeners will recall, the PACE program is designed to assist homeowners and small businesses in securing funding to make their properties more energy efficient.

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- Property owners repay the costs of energy improvements through assessments spread out over a decade or more.
- Fannie Mae and Freddie Mac characterized PACE assessments as loans that must be subordinate to their own mortgages.
- The Federal Housing Finance Agency affirmed Fannie and Freddie's decision on July 6 and urged state and local governments to reconsider and pause these programs until concerns could be addressed.
- A provision to clarify the relationship between home mortgages and state or local tax financing supported by PACE bonds was adopted by the House in June 2009 as part of American Clean Energy and Security Act, but has not yet been addressed in the Senate.
- We'll continue to monitor the situation and keep you updated in future podcasts.

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TAX CREDIT TIDBITS

Report: Build America Bonds

- The Internal Revenue Service (IRS) generally processed the initial requests for payment of the Build America Bond federal subsidies accurately, timely, and without indications of fraudulent or erroneous disbursement, according to a new audit report publicly released last week by the Treasury Inspector General for Tax Administration.
- The Build America Bonds program was created by the American Recovery and Reinvestment Act, and allows the federal government to partially offset state and local governments' cost of paying bond interest.
- The Treasury Inspector General of Tax Administration reviewed more than \$110 million in direct subsidy payments for the initial 80 bond issuances requesting subsidy payments.
- The review revealed that the controls and procedures developed and implemented by the IRS's Tax Exempt Bonds office assured that all 80 federal subsidy payments were accurate.
- A copy of the report can be found online at www.treas.gov.

AHP Funds Available

- Applications are currently being accepted for the Federal Home Loan Bank of San Francisco's Affordable Housing Program.
- The Affordable Housing Program is one of the largest sources of private funding for the construction and preservation of affordable housing in the country.
- The bank encourages financial institutions that are members of the Federal Home Loan Bank of San Francisco to apply for Round B of the 2010 funding competition.
- The bank also recommends that interested community groups contact a bank member early in their planning process about sponsoring an application,
- The Federal Home Loan Bank of San Francisco's Community Investment staff is available to help identify local members.
- The deadline for submitting an application for Round B is Friday, October 1, 2010.
- Round B application materials are available on the bank's web site at www.fhlbsf.com.
- For more information about submitting an application, contact Thomas Stagg or Jim Kroger in Novogradac & Company's San Francisco office at (415) 356-8000.