NOVOGRADAC
TAX CREDIT TUESDAY
PODCAST

Summary: September 11, 2018

In this week's Tax Credit Tuesday Podcast, Michael J. Novogradac, CPA, discusses Tax Reform 2.0 could mean for various tax credit communities. He also provides an update on the confirmation of a new IRS commissioner, as well as a letter the U.S. Conference of Mayors sent to Treasury requesting guidance on the opportunity zones incentive. Then he shares a brief report on the recent House committee hearing on the cost of multifamily housing development regulations. After that, he talks about a report released by the National Council of State Housing Agencies on the cost of developing LIHTC properties. Next, he reviews a recent house hearing on efforts to reform or unwind Fannie and Freddie, as well as FY 2019 fair market rents. Before closing, he shares rural housing news and announcements from HUD and the CDFI Fund.

Summaries of each topic:

GENERAL NEWS

Tax Reform 2.0

- In breaking news, yesterday, so real breaking, the House Ways and Means Committee Chairman Kevin Brady announced the introduction of three bills.
- These three bills make up the Tax Reform 2.0 package we've been talking about for so many weeks and months.
- The three bills were co-sponsored by all Republicans on the Ways and Means Committee.
- Now these three bills include provisions to make permanent some provisions from last year's tax reform bill, as well as includes some new areas of reform.
    - Now as regards last year's tax reform bill, Tax Reform 2.0 would make permanent (or as you know, I like to say more accurately, make indefinite) the individual and small business tax cut provisions.
    - Now these provisions are currently set to expire in the year 2025.
    - And then as regards to new areas of reform, the bills include provisions to reform savings-related and education-related tax provisions.
    - There aren't any new reform provisions with respect to tax credits.
- Now Brady said that the Ways and Means Committee will take up the bills this Thursday.
    - And I do think that there's a good chance the bills will pass.
    - Now he said he expects the package to go to a floor vote in September.
- So what is the big takeaway for the affordable housing, community development, historic preservation and renewable energy communities?
- There was a fear that private activity bond repeal may be back on the table.
    - Well, the big takeaway is there is not a big takeaway.
    - The bills do not contain any provisions that directly affect affordable housing, community development, historic preservation or renewable energy communities.
- I would say there was a collective sigh of relief in these various communities.
- Now I have included links to all three bills in today's show notes and I will keep you updated in the podcast and on Twitter with any developments.

Rettig Nomination

- In other tax news, Senate Majority Leader Mitch McConnell's office confirmed in an email to Bloomberg Tax that the Senate would vote this week on the nomination of Charles Rettig as the next IRS commissioner.
- The move signals that McConnell has enough votes to confirm Rettig.
- Now there is a possibility that Michael Desmond, the nominee for chief counsel at the IRS, could be confirmed, as well.
- Now the IRS has not had a confirmed commissioner in 10 months since John Koskinen's term ended last November.
- David Kautter is in office as acting commissioner until a new commissioner is confirmed.
    - You may recall, David Kautter is also the Treasury Assistant Secretary for Tax Policy, so he's been working two jobs ever since.
- I'll keep you posted on the status of his confirmation hearing.
- It would be nice to have Assistant Secretary for Tax Policy David Kautter being able to focus on his one job versus both jobs.

Mayors OZ Letter

- We also have an additional comment letter to report on, on Opportunity Zones.
- This time, it's coming from the U.S. Conference of Mayors.
- The U.S. Conference of Mayors last month wrote a letter requesting IRS guidance on implementing the opportunity zones incentive.
- Now the signatories on the letter said that their constituents and communities are excited about the new community development tool.
    - Investors and local leaders are already putting business and community plans in place, per the letter.
- However, the mayors said that a lack of guidance from the IRS could discourage broader investor participation.
    - That's something we've been talking about for a while in this podcast, how we need more guidance to increase investor participation.
- Now the letter calls for guidance in five specific areas, including providing enough time for opportunity funds to assemble meaningful investment portfolios.
    - Basically, how long can an opportunity fund hold cash for the rest investor to invest in businesses.
- No I'm not going to detail all five areas of the requested guidance, but I do want to highlight a few that are particularly relevant to our listeners.
- One is a request for guidance to clarify that residential rental real estate property qualifies as qualified opportunity zone property.
- We certainly think it does. It would take a somewhat tortured reading of the code for it not to qualify, but having the IRS say residential real estate qualifies would help quite a bit.
- Now the U.S. Conference of Mayors believes that Congress did intended for low-income neighborhoods with housing shortages to benefit from the opportunity zones.
- And as a consequence, residential rental real estate should qualify.
- Now another area where the letter requests IRS guidance is for Treasury to affirm that the low-income housing tax credit (LIHTC), new markets tax credit (NMTC), historic tax credit (HTC) and other development incentives can be used in conjunction with qualified opportunity fund investments.
- Similarly, we at Novogradac are of the opinion that is allowable, but confirmation from the IRS would be helpful.
- Now you can find a link to the Conference of Mayors' letter in today's show notes.
- Now these requests are consistent, as I've noted, with the requests submitted by the Opportunity Zones Working Group, which Novogradac leads.
- We've submitted comments in previous submissions in the last several months.
- Now the U.S Impact Investing Alliance also sent a letter concerning the opportunity zones incentive.
- Their letter went to Treasury Secretary Steven Mnuchin, asking him to instruct the IRS or another agency to collect and provide data on opportunity funds.
- The letter gives specific information that should be collected that would be helpful.
- Members of the alliance want that information to be collected at least annually, then made available to opportunity fund managers.
- There's a link to that letter in today's show notes, as well.
- I'll also send out a tweet with the links.
- Finally, I want to mention that Novogradac on Friday of last week launched two online tools to help those interested in opportunity zone investments.

- Now these tools detail how each state's personal income tax and corporate income tax regulations conform with the federal opportunity zones provisions.
- Now whether and how a state's tax code conforms with the federal opportunity zones incentive is important.
- Investors residing in states that conform with the federal incentive will generally receive state income tax incentives similar to those available at the federal level.
- Conversely, investors residing in non-conforming states may be unable to defer and reduce their state income taxation on initial gains invested in opportunity zones.
    - Furthermore, investors in non-conforming states might be required to recognize gain for state tax purposes on their eventual sale of their opportunity fund investment, even if such gain is not taxable for federal purposes.
- Suffice to say, a state's income tax code is a very important consideration when investors decide whether to realize gains and invest in an opportunity fund, as well as which states opportunity funds will choose to invest in.
- Now if you have any specific questions about how your state conforms to federal opportunity zones provisions, or you have any information to share with us about that, please contact my partner John Sciarretti.
- I'll include his contact information, as well as links to both opportunity zones state conformity tools in today's show notes.
- And as you can guess, I'll also tweet out a link.

Cost of Affordable Housing

- Let's now turn our focus to two notable events that occurred last week that addressed the cost of affordable housing.
- The first was a hearing last Wednesday on the cost of regulating affordable multifamily development.
- The hearing focused on how various federal, state and local regulations and policies affect affordable multifamily housing development.
- Some of the key takeaways from the hearing are that housing trends will change dramatically over the next 25 years as more individuals opt to rent rather than own homes.
- Another takeaway that's no surprise but is worth repeating: higher regulatory costs hinder development and further exacerbate affordable housing problems.
- One of the witnesses was Sue Ansel on behalf of the National Multifamily Housing Council and the National Apartment Association.
- Ansel said that local regulations and red tape often put affordable multifamily production at a disadvantage.
    - Something familiar to many of our listeners.
- Furthermore, a recent study by the National Multifamily Housing Council and the National Association of Home Builders found that 32 percent of multifamily development costs are associated with local, state and federal regulations compliance.
    - 32 percent.
- Ansel made a host of recommendations to reduce multifamily housing development barriers, and she included in that list expanding, enhancing and streamlining the low-income housing tax credit, as well as creating a middle-income housing tax credit, much like Sen. Wyden recently introduced.

- Now the other notable event last week about the cost of affordable housing was the release by the National Council of State Housing Agencies of a report on the development costs for LIHTC properties.
- The importance of this NCSHA report is going to be amplified soon by the fact that the Government Accountability Office will be releasing a report on a similar topic.
- Now the NCSHA report analyzed a database of 160,000 homes built from 2011 through 2016.
    - These homes were in all 50 states and all territories–places where the LIHTC is used.
- Now there were some significant conclusions that were made in the NCSHA report.
- One is that those properties that are considered cost outliers–and by that, we mean those with extremely high costs–are a very low percentage of LIHTC properties.
- Another highlight of the study is that the cost of credit-financed housing and market-rate housing is relatively even nationally.
    - That's a very key finding.
- Also, the study revealed that in some cases, the cost to develop affordable housing is actually rising <u>slower</u> than the cost of developing market rate housing.
- The NCSHA study indicated that the primary factors that drive development costs for all apartment properties, whether affordable or market rate, are the same.
- Once again, not a surprise, but it's nice to have it formally documented in a study.
    - These costs include:
        - land,
        - labor and
        - materials.
    - Now the report said that those items are driven by market forces, and not state agency administration, such that state agencies don't have much control over the costs of land, labor and materials.
- Now the report also pointed out that local regulations that increase costs are also beyond state allocating agency control.
- Well who conducted the study?
- Well the study by Abt Associates, and they analyzed, as I noted earlier, a nationwide database.
- There were 2,500 housing credit properties in the database during this six-year period.
    - Now the properties, as I also noted earlier, more than 160,000 units.
        - So a pretty wide sample size.
- The median total development costs per unit in that sample size was just less than $165,000, adjusted for inflation.
    - And that $165,000 number includes soft costs.
- Now data available on <u>all</u> apartments built in the same period showed that the cost averaged just more than $150,000.
    - However, that number does <u>not</u> include all the soft costs that the tax credit unit calculation did.
- Now while we'll wait to see what the GAO report says, this report does indicate what many of us, affordable housing advocates, already knew:
    - Prices are rising for all multifamily construction.
    - The NCSHA study shows that LIHTC costs and market-rate costs grew at roughly the same annual average.
        - That growth rate, by the way, was about 8 percent a year – pretty high.

- And there's a foreword written by NCSHA executive director Stockton Williams to the report that says that housing credit development costs are generally consistent with overall apartment development costs and have grown at the same rate, if not slower, as overall apartment development costs in recent years.
- I suspect that foreword to be quoted quite a bit, as it's a nice summary of the overall report.
- Now I've included a link to the report in today's show notes and I'll also tweet a link to the GAO report when it's released.
- And I'll tweet out a link to the NCSHA report as well, though I have retweeted some of NCSHA's tweets already.

Reforming Fannie Mae and Freddie Mac

- As I did note at the beginning of the podcast, the House Financial Services Committee also held a hearing last Thursday on reforming Fannie Mae and Freddie Mac.
- With last year marking 10 years since Fannie and Freddie were put into conservatorship in the aftermath of the housing crisis, it was a good time for a hearing on Fannie Mae and Freddie Mac.
- The hearing reviewed the conservatorship of these government-sponsored enterprises over the past decade and more importantly, looked at possible next steps for Fannie and Freddie.
- One of the witnesses was Ed DeMarco.
- Ed DeMarco is a former acting director of the Federal Housing Finance Agency.
- DeMarco recommended winding down, then ending Fannie and Freddie as government-sponsored enterprises.
- He called for a housing finance system that would facilitate the return of private capital and strengthen underwriting standards.
- Now pressure is mounting on Congress and the Trump administration to act on GSE reform.
- I would note, a coalition of 30 trade associations did send an open letter to the administration and Congress to make permanent the GSE reforms placed during conservatorship.
- That letter said that any efforts to change the role played by GSEs must contain safeguards against higher costs and market disruption.
- Now by the way, two bills that include GSE reform are close to being introduced, and we'll be watching them closely.
- Rep. Jeb Hensarling, a Republican from Texas, is an author of both.
    - And you may also recall that he is stepping down from Congress and not running for reelection.
- Now Hensarling and Democratic Rep. John Delaney of Maryland released a draft proposal of The Bipartisan Housing Finance Reform Act last week.
- Now this legislation, emphasis on bipartisan, would repeal the charters of Fannie and Freddie within five years.
- So what would be there instead?
- The legislation would separate Ginnie Mae from HUD and make Ginnie Mae the primary government backer of mortgages.
- Hensarling also said that he does plan to re-introduce the Protecting American Taxpayers and Homeowners Act.

  - The so-called PATH Act.
- Now that's an update to a bill he introduced in 2013 that didn't advance.
- I'll keep you posted in future podcast episodes about any movement on the GSE front, and most notably, the extent to which more support expands for this bipartisan bill to reform, or I should say wind down Fannie Mae and Freddie Mac, and turn Ginnie Mae into the primary government backer of mortgages.

FY 2019 FMRs

- Now in last week's podcast, I had noted that HUD had released fiscal year 2019 fair market rents, or to commonly call them, FMRs.
- And as promised, this week I have more details for you about 2019 FMR trends.
- Now FMR trends to a certain extent can reflect general trends as to market rents, subject to the vagaries as to how FMRs are collected.
- Now in general, FMRs for 2019 continued an upward trend over the past few years.
- FMRs increased by 2.49 percent, just under 2.5 percent, or about $23 on average.
- This increase is slightly less than the increase in 2018.
- The 2018 increase was just over 3 percent at 3.03 percent, or $26 to be accountant accurate.
- Metro areas tended to have larger increases in 2019 than non-metro areas.
- The average increase for metro areas was just over 3.5 percent at 3.56 percent.
- And that compares to an average increase of 1.73 percent in non-metro areas.
- Now, to look at major areas with the greatest increases and decreases:
  - Now with areas with a population greater than 100,000 people, the Santa Cruz-Watsonville, Calif., MSA saw the largest increase in FMRs at 24 percent, actually over 24 percent, 24.12 percent, in Santa Cruz-Watsonville, Calif., MSA.
  - Now of areas with a population greater than 100,000, the area that saw the greatest <u>decrease</u> was the San Francisco HMFA at a decrease of 10 percent compared to 2018.
    - That's right, 10 percent decrease compared to 2018 in San Francisco.
- I'll also note that public housing authorities may ask HUD to reevaluate FMRs for a certain area if the public housing authority thinks that the FMRs do no accurately reflect the rents in the area.
- So, if you have a LIHTC property, how do these FMRS affect your LIHTC property's income and rent limits?
- Well, when determining LIHTC income and rent limits, HUD applies what's called a high housing cost adjustment.
  - This adjustment increases income limits for areas where housing costs are abnormally high compared to the median income for the area.
  - The adjustment is based on HUD's FMR for a two-bedroom unit.
- So I apologize for getting so wonky here, but when we apply the high housing cost adjustment to the 2019 FMR, there are 75 areas with a LIHTC income limit that's greater than the 2018 LIHTC limit.
  - And the average adjustment increase is 5.53 percent.
- So if you're in one of the 75 areas, you definitely want to know about this.
- So if you want to read a summary of this FMR analysis, go to our Notes from Novogradac blog post.
- I'll include a link in today's show notes and send out a tweet.

- But more importantly, I'd encourage you to reach out to my partner Thomas Stagg in our Washington state office, if you have any questions on these adjustments, or would like more analysis as to the effect of these adjustments on your particular tax credit properties.

OTHER NEWS

- Thank you for staying with the podcast, it's a little bit longer podcast this week.
- There are a handful of other items I wanted to make sure to share with you.
- First, the Housing Assistance Council has published a report on the USDA's rural rental housing portfolio.
    - This report points out that rental housing options in rural America are declining.
    - USDA Section 515 direct loans are an important source that funds that housing and the number and availability of those loans has dropped.
        - In fact, few properties have been financed through the Section 515 program for the past several years.
    - Now the HAC report also says that the Midwest and South are disproportionally affected by this decrease in affordable rental stock.
    - Properties financed with Section 515 direct loans can exit the program after paying off the loan.
    - And the report says an average of nearly 1,800 units per year will leave the program over the next decade.
    - The report includes policy recommendations including incentives to keep owners in the Section 515 program.
    - Now I've included a link to the report in today's show notes.
    - Send us an email with your thoughts.
- And in other affordable housing news, HUD did award nearly $100 million to 285 public housing authorities recently.
    - These funds are to provide housing to non-elderly people with disabilities.
    - The awards?
    - Well they're through the Section 811 Mainstream Housing Choice Voucher program.
    - The goal of the Section 811 Mainstream Housing Choice Voucher program is to help people with disabilities live in the most integrated setting.
- And staying with HUD for the moment, the agency yesterday launched an enhanced RAD Resource Desk.
- A desk that users can use to more easily manage their rental assistance demonstration transactions.
    - HUD said the enhanced resource desk has easier site navigation and can more efficiently process RAD transactions.
    - Let us know your thoughts as well by sending an email to cpas@novoco.com and let us know if you're finding it handy.
- And then finally, let's close out with community development news, where the CDFI Fund announced last week that its Community Investment Impact System, CIIS, is officially retired.
    - This means all reports from award recipients, going forward, go to the new Award Management Information System, or AMIS.
    - This really does just simplifies the system hopefully.
    - All CDFI Fund programs are now managed, administered and monitored through their life cycle in AMIS.
    - A blog post by CDFI Fund director Annie Donovan stressed that one of the main benefits is that AMIS is more user-friendly to its customers.

RELATED RESOURCES

Tax Reform 2.0 Legislation

- H.R. 6760 Protecting Family and Small Business Tax Cuts Act of 2018
- H.R. 6757 Family Savings Act of 2018
- H.R. 6756 American Innovation Act of 2018

Conference of Mayors Letter

- **Letter**
- U.S. Impact Alliance Letter
- State Tax Code Conformity - Personal Income
- State Tax Code Conformity - Corporate Income
- Email John Sciarretti

House Financial Services Committee Hearings

- The Effect of Regulation on Affordable Multifamily Housing
- A Failure to Act: How a Decade without GSE Reform Has Once Again Put Taxpayers at Risk

FY 2019 FMRs

- "Upward Fair Market Rents Trend Continues"
- Email Thomas Stagg

NCSHA Report

- "Variation in Development Costs for LIHTC Projects"

HAC Report

- Rental Housing for a 21st Century Rural America: A Platform for Preservation

Section 811 Awards

- HUD Awards $99 Million to Provide Affordable Housing to People With Disabilities

RAD

- RAD Resource Desk

AMIS Live

- CDFI Fund Retires CIIS—Compliance Reporting is Now Live in AMIS