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STATE TAX CREDITS

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State Community Development Tax Incentives—Vital Companions

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Properly designed state community development tax incentives are vital companions to their federal versions. A financial hole often remains after developers and sponsors of community development projects line up equity from federal tax incentives, traditional loans and other soft financing sources (such as grants and below-market government loans). This is where state tax incentives, generally tax credits, come in: the equity they generate can help fill that hole.

Every year, governors and state legislators are better recognizing this, leading to the increasing enactment, expansion and extension of state tax incentive legislation across the nation. In 2023, two states added a historic tax credit (HTC) and four states added a low-income housing tax credit (LIHTC). Additionally, legislation was introduced but not enacted in six states to create a LIHTC, two had legislation proposing an HTC and three states had bills that proposed state-level new markets tax credits (NMTCs).

At the end of 2023, developers and sponsors in 38 states could seek state HTCs, in 30 states they could apply for LIHTCs and in 13 states, state NMTC-type financing is available.

Beyond state HTCs, LIHTCs and NMTCs, other tax incentives are available. For renewable energy, it's difficult to accurately determine the number of states with tax credits due to the wide variation of state approaches. The opportunity zones (OZ) incentive state-level benefits come primarily from being in conformity with the federal tax code (although Ohio has an OZ tax credit).

Only eight states don't have at a state HTC, LIHTC or NMTC equivalent. They are Florida, Idaho, New Hampshire, Oregon, South Dakota, Tennessee, Washington and Wyoming. Florida had, but repealed, a state-level NMTC. Thirty-one states have at least two of the statewide incentives and five states (Arkansas, Georgia, Illinois, Maine, Ohio) have all three.

Compared to a decade ago, there are 17 more states with a state-level LIHTC and three more states with an HTC. With Florida's elimination of its state NMTC, there are two fewer with that incentive than in 2014.

Variety of State Tax Incentives

While many state community development tax incentives closely mirror their federal counterpart, there are notable differences.

States often design and allocate their LIHTC to more narrowly target specific housing needs. Many states (such as California, Colorado and Indiana) also prioritize state housing credits to close financing gaps for developments that use private-activity bond cap and 4% LIHTCs to build new and/or renovate existing affordable rental housing.

States With State-Level Community Development Tax Incentives

STATE	LIHTC	HTC	NMTC
Alabama		✓	✓
Alaska			✓
Arizona	✓		
Arkansas	✓	✓	✓
California	✓	✓	
Colorado	✓	✓	
Connecticut	✓	✓	
Delaware		✓	
District of Columbia	✓		
Florida			
Georgia	✓	✓	✓
Hawaii	✓	✓	
Idaho			
Illinois	✓	✓	✓
Indiana	✓	✓	
Iowa		✓	
Kansas	✓	✓	
Kentucky		✓	✓
Louisiana		✓	✓
Maine	✓	✓	✓
Maryland		✓	
Massachusetts	✓	✓	
Michigan		✓	
Minnesota	✓	✓	
Mississippi		✓	✓
Missouri	✓	✓	
Montana		✓	
Nebraska	✓		✓
Nevada	✓		✓
New Hampshire			
New Jersey	✓	✓	
New Mexico	✓	✓	
New York	✓	✓	
North Carolina		✓	
North Dakota		✓	
Ohio	✓	✓	✓
Oklahoma	✓	✓	
Oregon			
Pennsylvania	✓	✓	
Rhode Island	✓	✓	
South Carolina	✓	✓	
South Dakota			
Tennessee			
Texas	✓	✓	
Utah	✓	✓	✓
Vermont	✓	✓	
Virginia	✓	✓	
Washington			
West Virginia		✓	
Wisconsin	✓	✓	
Wyoming			

Source: Novogradac

Some states set aside significant amounts for specific geographic regions, most commonly for rural developments or for economically disadvantaged counties. Many states prioritize the state LIHTC for properties that serve the lowest-income renters. Some state credits, such as in Minnesota and New Mexico, are dollar-for-dollar credits for donations that taxpayers make for affordable housing.

For state-level HTCs, most states offer credits worth 20% to 30% of qualified rehabilitation expenditures (QREs) to pair with the federal credit of 20%. There are a few outliers, such as Montana's 5% credit (25% of the federal amount) and New Jersey's 40% credit.

States also offer variations, such as Delaware's 10% bonus for affordable housing, New York's historic barn credit and South Carolina's credit for rehabilitating abandoned textile mill sites.

State NMTCs generally follow federal credit guidelines. Georgia's version (and several proposed state NMTCs in recent years) provide specificity: In Georgia, the credit applies to agribusiness and rural jobs.

Benefits of State Credits

States that offer their own version of federal community development tax incentives generally attract more development, since a well-designed state tax credit gives developers a resource to close financing gaps.

Ohio is a good example, since the state offers versions of the LIHTC, NMTC and HTC. An Ohio affordable housing developer can receive the federal LIHTC and a matching state credit, thus increasing potential equity. Similarly, a sponsor developing an HTC-eligible property in Ohio could receive the federal credit worth 20% of QREs and a 25% state credit (which bumps up to 35% for communities of less than 300,000 through the end of this year). A business receiving NMTC funding in Ohio, meanwhile, is eligible for the federal credit worth 39% of the qualified equity investment (QEI) and can compete for a state credit worth 39% of the QEI (although the state credit is taken later in the seven-year cycle).

State tax incentives mean more affordable housing, community development and historic preservation, and influence the types and areas for such development.

Industry Recommendations

With a range of states and credits, stakeholders over the years have produced guidelines for state-level versions of federal credits and there is significant overlap in these recommended practices.

In October 2023, the Affordable Housing Tax Credit Coalition (AHTCC) released its recommended practices for a state LIHTC, including:

- the ability to pair with the 9% or 4% LIHTC,
- geographical distribution between rural/metro areas and other factors,
- application timing and structure that mirrors the federal LIHTC when possible,
- application scoring that mirrors federal incentive,
- a minimum allocation total per development, and
- post-awards documentation requirements.

The report urged using the same infrastructure as the federal credit and authorizing sufficient tax credit authority to have a meaningful effect on the state's housing goals. The AHTCC guidelines recommend allowing bifurcation from the federal credit, offsetting a variety of state taxes and not requiring an IRS Form 8609 to be issued before claiming the credit.

Earlier in 2023, the National Trust for Historic Preservation issued its list of recommended practices for a state HTC, including:

- having a predictable (preferably with a high cap or uncapped) credit allocation,
- making the credit easily transferrable,
- having a credit percentage of at least 20%,
- offering predicable standards for eligibility, and
- being available to a wide variety of taxpayers.

The New Markets Tax Credit Coalition (NMTCC) issued suggestions for a state-level NMTC in 2016 that included:

- having the credit available on an open, competitive basis,
- mirroring federal rules for eligibility for community development entities and qualified active low-income community businesses, and
- including reporting requirements.

The common threads are an encouragement to mirror the federal version of the credit as much as possible and to make the credits as attractive to investors as possible.

What to do in 2024

As another legislative year starts, stakeholders should continue to advocate for new credits or legislation that enhances, extends or expands existing credits. In 2023, there was plenty of state-level legislation concerning credits: In addition to the legislation to create new credits, there were dozens of bills filed (many of which passed) to extend or make changes to the state incentives.

In 27 state legislatures, bills carry over from 2023, so advocates there should continue to promote worthy legislation. There are a few states that won't hold legislative sessions this year, but most other states require new legislation to be introduced. Advocates there should push for the introduction of bills to create, expand and/ or enhance state credits.

Community development national organizations (the A.C.T.I.O.N. Coalition for LIHTCs, the NMTCC for NMTCs and the Historic Tax Credit Coalition for HTCs) provide advocacy documents showing the economic benefit from state credits, including job creation, the amount of federal benefits that accrue and the number of properties that would not be completed but-for the state credit. Those should be shared with interested legislators and, of course, those involved in the LIHTC, HTC and NMTC worlds (as well as clean energy and OZs) should be aggressive about inviting legislators to see properties. Many elected officials are new to the community development tax incentive space. They may know about a project but be unaware of the importance of the federal and state tax incentives to help make it happen.

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