Novogradac Report on Tax Credits
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(Intro music)

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

Today is Tuesday, March 9th, 2010.

This week I will discuss several legislative updates.

In addition to the tax extenders legislation that the Senate started considering last week, a number of bills were also introduced that are of interest to the renewable energy community.

Then, I'll share the findings of a report released last week about the impact of the federal historic tax credit.

The report found that the federal historic tax credit is a highly efficient job creator — accounting for the creation of 1.8 million new jobs over the life of the program.

I will also review California Assembly Bill 2046, which would affect affordable housing properties.

The bill, introduced last month, would affect like-kind exchanges and eminent domain transactions in California.

And finally, I will share a quick update on the implementation of the low-income housing tax credit tenant data collection initiative.

This initiative is required by the Housing and Economic Recovery Act, also known as HERA. HUD released a notice last week with specific information collection requirements.

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Now, let's get started with an update on the status of tax extenders legislation.

The Senate last week began consideration of a bill entitled "the American Workers, State and Business Relief Act of 2010." The bill is designed to provide assistance to American workers, to states and to American businesses. The bill would extend tax provisions that expired on December 31st, 2009, as well as address several provisions that expired on February 28th, 2010. Senate Finance Committee Chairman Max Baucus and Senate Majority Leader Harry Reid introduced the bill as an amendment, number 3336, to H.R. 4213.

If enacted, the bill would extend the Section 1602 low-income housing tax credit cash grant exchange program that was created by the Recovery Act. It would also extend for one year the new markets tax credit program at the $5 billion allocation level.

The bill is being described as a jobs bill. Unlike the Hiring Incentives to Restore Employment or HIRE Act, which was much smaller, it is expected that a considerable number of amendments will be proposed for this package of tax extenders.

For example, a bipartisan congressional delegation from Louisiana, Mississippi and Alabama comprised of Senators Mary Landrieu, David Vitter, Roger Wicker and Thad Cochran introduced Amendment No. 3335 to be included in the extenders package. The amendment would extend the placed in service deadline for LIHTC projects in the GO Zone an additional two years. Reports from the area indicate that more than 70 developments, yes 70 developments,

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that have been awarded GO Zone low-income housing tax credits are stalled and at risk of not being built. Estimates suggest that those developments represent more than 6,000 affordable units and $1 billion in construction activity.

These developments have a congressionally mandated deadline of December 2010 for completing construction and being placed in service. However, factors including the economic downturn have made it difficult for developers to close on project financing and allow construction to begin. Supporters say that this amendment would provide more time for state governments, developers and investors to overcome financial challenges and enable the use of the previously allocated low-income housing tax credits.

In a similar vein, Senator Evan Bayh proposed Amendment 3374, which would make GO Zone and Disaster Area low-income housing tax credits eligible for the 40 percent Section 1602 cash grant exchange program.

On the new markets tax credit front, we expect that Senator Rockefeller will push an amendment that would allow for the new markets tax credit to reduce the alternative minimum tax.

The overall extenders bill is still under consideration in the Senate and we are closely monitoring its progress. For real time updates, I encourage you to follow me on Twitter. You can find my tweets at twitter.com slash Novogradac.

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In addition to the tax extenders package, there were several legislative developments regarding renewable energy last week.

On March 3rd, Senators Olympia Snowe and Susan Collins introduced the Deepwater Wind Incentive Act. This bipartisan legislation would provide a long-term renewable production tax credit for developing deepwater wind facilities.

Deepwater wind is defined as wind harnessed in waters greater than 60 meters. Supporters of deepwater wind development say that deepwater wind avoids issues related to view shed.

The Deepwater Offshore Wind Incentive Act would provide a tax incentive of 3.04 cents per kilowatt production tax credit for the first 6,000 megawatts of deepwater offshore wind production in the United States. The tax credit would be in place until the year 2030.

Also on March 3rd, Senators Tom Carper and Sherrod Brown joined Senators Snowe and Collins to introduce legislation to provide the offshore wind industry with enhanced stability by extending production and investment tax credits for offshore wind until the year 2020. Offshore wind includes any wind turbine located in the inland navigable waters of the United States, including coastal waters and the Great Lakes.

Both bills were referred to the Senate Committee on Finance. Copies of each bill are available online at www.energytaxcredits.com.

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In related news, another legislative proposal that would affect the renewable energy community drew a lot of attention last week.

As regular listeners to this podcast will recall, concerns were raised late last year that some Section 1603 energy tax credit cash grant funding was going to foreign-based renewable energy manufacturers. The initial objections were about a proposed wind farm in Texas that was expected to rely on wind turbines built in China. Energy Secretary Steven Chu responded to those concerns in a letter to Senator Charles Schumer. Secretary Chu wrote last November that companies that supplied turbines to the wind farms that received funding had U.S. plants and that the actual wind farms would be located in the U.S., creating local installation jobs and tax revenue.

Last week, Senators Sherrod Brown, Charles Schumer, Bob Casey and Jon Tester sent a letter to the Obama Administration urging the suspension, yes the suspension, of the cash grant program until it can be ensured that stimulus funds are awarded to projects that will create jobs **in** the United States. The senators cite a report released in February that claims that the Section 1603 cash grant program has paid out more than **$1 billion** to foreign manufacturers.

In a letter to Treasury Secretary Tim Geithner, the senators pushed for a moratorium on all payouts from the Section 1603 program until Congress can consider Senate Bill 3069, the American

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Renewable Energy Jobs Act. Senator Schumer introduced that bill on March 3rd.

The bill would make projects that do not have a stimulus job impact in the United States ineligible for stimulus dollars. Under the "Buy American" provision contained in the Recovery Act, government projects financed in part by the stimulus must, with few exceptions, rely on iron, steel and manufactured goods produced in the United States. But the provision does not impose a similar requirement on private projects that seek Recovery Act grants. The proposal announced last week would apply the "Buy American" standard to all renewable energy projects, whether public or private, that seek stimulus funds.

In a statement that announced the bill's introduction, the senators referred to the proposed wind farm in West Texas and they call it quote "just the latest example of a larger trend" close quote. To support this claim, the senators cite a report released by the Investigating Reporting Workshop that found that 79 percent of the $2 billion in grants awarded under the Recovery Act so far have gone to foreign companies.

However, the *New York Times* reported last week that Matt Rogers, who is a senior adviser to Energy Secretary Steven Chu, told the Senate Energy and Natural Resources Committee that the report is quote "at best, misleading" and "factually false" close quote. The *Times* reports that Rogers told the committee that suspending renewable energy grants as suggested would hurt domestic job creation.

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Also on March 3rd, American Wind Energy Association CEO Denise Bode echoed that concern in a statement issued in response to the proposed legislation. She said and I quote:

"At a time when the construction unemployment rate is nearly 25 percent and the manufacturing unemployment rate is 13 percent, this proposal would cost 50,000 American workers their jobs. The truth is, by law, Recovery Act grants can only be used to finance projects that are being built in the United States. This proposal would torpedo one of the most successful job creation efforts of the Recovery Act, which has already preserved half of the 85,000 American jobs in the U.S. wind industry." end quote

The association reported last week that more than half of the value of wind turbines used in U.S. wind projects is domestically produced, and that percentage is increasing every year as more turbine makers build U.S. manufacturing capability. The U.S. does not have that capability today to produce 100 percent of wind turbine components in the United States.

Ms. Bode went on to say that the proposed moratorium and legislation would destroy tens of thousands of American jobs. And rather than pursue this action, she said Congress should enact policies that will create jobs by encouraging manufacturers to invest in U.S. plants, such as passing a Renewable Electricity Standard. She says that the U.S. could grow its manufacturing base and add 274,000 American jobs if Congress passes a strong Renewable Electricity Standard.

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The law firm Stoel Rives reported in an email alert last week that while it is too early to predict how the proposal will be received, it is being taken seriously. In addition to AWEA, other trade associations involved in renewable energy, such as the Geothermal Energy Association as well as the Solar Energy Industries Association are taking immediate action to register their opposition.

A copy of the Renewable Energy Jobs Act is available online at www.energytaxcredits.com. We will track the bill's progress there and post related information as it becomes available.

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

Last week the Historic Tax Credit Coalition, of which Novogradac & Company is on the board, released the "First Annual Report on the Economic Impact of the Federal Historic Tax Credit." The report was authored by researchers from the Center for Urban Policy Research at Rutgers University. The report found that the federal historic tax credit is a highly efficient job creator-accounting for the creation of 1.8 million new jobs over the life of the program.

The report found that historic tax credits generated jobs more efficiently than other stimulus options and the study concludes that the economic activity leveraged by the historic tax credit returns more tax revenue to the U.S. Treasury than the cost of implementing the program. The report is the first ever to provide a comprehensive examination of the economic impact of the federal historic tax credit.

While underscoring the success of the Historic Tax Credit program, the report recommends several improvements to modernize

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the program and ensure its continued efficacy. To download a copy of the report, I invite you to visit the Historic Tax Credit Resource Center online at www.novoco.com.

You can also read more about its findings in an upcoming issue of the Novogradac Journal of Tax Credits. John Leith-Tetrault is chairman of the Historic Tax Credit Coalition and he writes a monthly column for the Journal called History and The Hill. In the April issue of the Journal, John will provide a detailed review of the report and discuss its significance for the tax credit community.

Next, let's move on to the affordable housing topics for this week's podcast. First, we have an item of interest to California's affordable housing community. It's also of interest to other listeners outside of California as more than 10 percent of low-income housing tax credit properties are in California, and, for better or worse, other states often follow what happens in California.

On February 19th, California Assembly Member Juan Arambula introduced Assembly Bill 2046. The bill would affect like-kind exchanges and eminent domain transactions in the state of California. A 'like-kind exchange' refers to the disposal of one property and the acquisition of a similar property without generating tax liability.

Specifically, AB 2640 eliminates the exclusion of gain or loss from like-kind exchanges, and also eliminates the exclusion of gain or loss from involuntary conversions, such as eminent domain.

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As such, if the bill passes and becomes law, such transactions - these like-kind exchange or involuntary conversion transactions - would remain tax free for federal income tax purposes, but would become taxable for California income tax purposes.

This bill is seen an effort by the state of California to raise income taxes to help close the budget gap.

If passed, the bill would affect transactions completed after January 1st, 2010.

AB 2640 could have a negative impact on LIHTC property exchanges in several ways. If enacted as written, the bill would affect transactions currently in progress and most like-kind changes would be taxable.

Additionally, eminent domain transactions would be taxed. Cities and states frequently use eminent domain transactions to acquire properties for affordable housing. Stephen Ryan, an attorney in Cox Castle Nicholson's affordable housing group, tells us that AB 2640 would tax those transactions, making it more difficult to acquire land.

The bill would, however, create a new rule that would allow non-taxable exchange treatment where property is sold to tenant associations, not-for-profit organizations, for-profit organizations or individuals, or public agencies that maintain the affordability of the property for at least 30 years and the proceeds of the transaction are reinvested in residential real property within two years.

These three policies are a departure from the federal tax laws governing like-kind exchanges and involuntary conversions, and Mr.

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Ryan told us he is interested in seeing if the state itself will take a position on this assembly bill. He also said he would like to see clarification of some of the more vague parts of AB 2640, including how the bill would affect exchanges started before the bill was introduced. Mr. Ryan suggests that people involved in like-kind exchanges of low-income housing tax credit properties monitor AB 2640's progress as it moves through the assembly. As of February 22nd, the bill had been read once and was at the Assembly desk.

We will continue to monitor AB 2640's progress through the California State Assembly and we'll post updates on the Affordable Housing Resource Center web site. The full text of AB 2640 as introduced can be found by clicking the "Legislation" tab and choosing "State Legislation" at the novoco.com web site.

Our final topic for today is an update on the LIHTC tenant data collection initiative.

The U.S. Department of Housing and Urban Development announced last week that it will use a system similar to, and based on, the current Tenant Rental Assistance Certification System or TRACS to collect data about tenants of low-income housing tax credit properties. The Housing and Economic Recovery Act of 2008 requires each state agency to furnish HUD, not less than annually, information concerning the race, ethnicity, family composition, age, income, use of rental assistance under Section 8 or other similar assistance, disability status, and monthly rental payments of households residing in each property that receives low-income

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housing tax credits through the agency. On March 30th, 2009, HUD published a notice seeking early input on a methodology or approach for the data collection. HUD says it received approximately 25 comments from state housing finance and tax credit agencies; including tax credit property managers; housing trade associations; research institutes; and not-for-profit organizations.

In a notice in the March 3rd *Federal Register* HUD summarizes those public comments, HUD addresses the significant issues raised and issues specific information collection requirements. A copy of the notice is available online at www.taxcredithousing.com. We encourage everyone to take a moment to review those new requirements.

Speaking of LIHTC tenant data, it's time for this week's "Did You Know?" segment.

Did you know that Novogradac & Company offers a wide range of LIHTC property compliance services? As we start a new year, we also start a new compliance monitoring year for state agencies. State agencies are required, at minimum, to perform on-site inspections of at least 20 percent of the units and tenant files of their properties every three years. If your property hasn't been visited for two years, you should expect a visit from your state agency this year.

Just as you wouldn't take a crucial exam without studying, you don't want to enter a state agency review unprepared, especially since noncompliance is reported by the state to the IRS on IRS Form 8823 **whether you subsequently correct the noncompliance or**

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not. However, according to the IRS 8823 guide, noncompliance with the annual income certification requirements that are identified and corrected by the owner PRIOR to notification of the compliance review by the state agency need NOT be reported; i.e., the owner has demonstrated *due diligence* by addressing noncompliance issues independently.

One of the ways that owners can demonstrate due diligence is to have a third party review of their tenant files. If your property is on the list to be visited this year, time is of the essence in terms of scheduling a third-party review, because noncompliance needs to be identified AND corrected PRIOR to notification of the compliance review by the state agency so that it would NOT be reported to the IRS.

Novogradac & Company has performed thousands of compliance reviews throughout the United States and its territories, from Puerto Rico to Alaska. We can review your tenant files to help identify compliance deficiencies that should be corrected prior to the state agency review. Timely review of the tenant files provides owners and property managers an opportunity to correct problems before the state agency review.

It's also important to review the initial tenants' files in the first year of the tax credit period. The first year is critical, as most of our listeners know. Technical issues such as the two-thirds rule based on qualified occupancy as of the close of the first year, the weighted average occupancy in the first year, and the set-aside in the first year, are critical not only in terms of determining the credits in the first year,

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but have implications on how credits flow for the balance of the 15-year compliance period. Failing the set-aside in the first year can be fatal because your project will never qualify for tax credits. A simple error, like the wrong utility allowance, can disqualify all your units. The first year is also important in setting the tone and precedent for the balance of the compliance period. We can review files during the first year — and just after the close of the first year so that owners have an opportunity to correct problems early in the compliance period.

With a new year also springs new hope - in the form of tax credit and tax-exempt bond applications. Navigating the ever changing bond and tax credit rules can be difficult. A lot like short track skating, applications for tax credits are very competitive and the smallest mistake can disqualify your project. Novogradac & Company can guide you through the application process. We can assist you with preparing applications, reviewing applications, issuing reports required by state agencies on eligible basis and many other services. In addition to reviewing or assembling the application, our services related to applications also include eligible basis reports; 50 percent test reports; market studies; construction cost analyses and much more.

Novogradac & Company offers dozens of compliance and application services in addition to those that I've mentioned today. To learn more I encourage you to contact my partner Jim Kroger in our San Francisco office at 415-356-8000. You can also read about our services online at www.novoco.com slash services.

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

This week, my partner Dan Smith and I are speaking at the Affordable Housing Investors Council meeting in Washington D.C.

Meanwhile, also this week my partners Charlie Rhuda and Brad Elphick are speaking at the National Housing & Rehabilitation Association's annual meeting in Miami Beach, Florida on March 10th through the 13th.

On March 14th through the 16th, managers and owners of affordable multifamily housing will gather in Washington, D.C. for the National Affordable Housing Management Association's Winter meeting, that's NAHMA.

Also in D.C. this week, the National Housing Conference will hold its Annual Budget Forum on March 12th.

Looking ahead, community development professionals are encouraged to register for the Community Development Venture Capital Alliance's Annual Conference. The event will be held on Thursday and Friday, March 25th and 26th in New Orleans. To learn more about that event, we invite you to visit www.cdvca.org.

And finally, we've learned that the Financial Services congressional hearing on the future of housing finance that was originally scheduled for Tuesday, March 2nd, has been rescheduled for Tuesday, March 23rd. Committee Chairman Barney Frank has invited Treasury Secretary Tim Geithner and Housing and Urban Development Secretary Shaun Donovan to testify at the hearing.

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

Please join me again next week.

One of the topics I will discuss is last week's notice of funds availability for the inaugural application round of the Capital Magnet Fund. The Capital Magnet Fund was established through the Housing and Economic Recovery Act of 2008. Through the program, the CDFI Fund will make $80 million available to certified CDFIs and not-for-profit housing organizations to support the financing of affordable housing and related economic development activities and community service facilities. It is anticipated that awardees will leverage the $80 million of Capital Magnet Fund award dollars to support in excess of $800 million in aggregate costs. Capital Magnet Fund application materials are due to the CDFI Fund by April 15th. Tune in next week to learn more.

Next week we also will provide an update next week as to the expected timeline for applying for new markets tax credits in 2010.

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

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