Summary: July 23, 2019

In this week's Tax Credit Tuesday Podcast, Michael J. Novogradac, CPA, talks about the agreement on discretionary spending levels and debt limit suspension. He also discusses guidance issued last week by the Securities and Exchange Commission and the North American Securities Administrators Association concerning investments in opportunity zones. He moves on to IRS final regulations about Section 50(d) income. He then closes out with news on a New Markets Tax Credit Coalition report, the ADVANCE Act of 2019, a new chapter in the HUD Housing Choice Voucher Guidebook, an advocacy letter to Congress asking to extend the investment tax credit and Pennsylvania conforming to the Internal Revenue Code for OZ investments.

Summaries of each topic:

GENERAL

Budget Talks

- We have news that was breaking last night about the budget and spending caps negotiations that we've been talking about for the past few weeks, really the last few months.
- President Trump announced, guess where, on Twitter, that Congress and the White House reached an agreement on a two-year deal on discretionary spending levels and a debt-limit suspension.
- There is also an agreement on a two-year debt ceiling increase.
- Now this is a significant development.
    - Just a few weeks earlier, there was widespread expectation that these agreements wouldn't happen until after Congress returned from its August recess.
    - That was because Treasury was expected to be able to employ "extraordinary measures" to avoid breaching the debt limit until late September or October.
    - However, as we discussed last week, Treasury Secretary Steven Mnuchin reported that Treasury might breach the debt limit before Congress returned in September, which started the ball rolling.
- The details of the agreement aren't public yet, or at least as I'm recording this podcast.
- However, the agreement reportedly includes an increase in top-line spending numbers for both defense and nondefense spending for the 2020 and 2021 fiscal years.
    - Specifically, the defense spending cap for 2020 would be $738 billion and the 2021 cap would be $740.5 billion
    - The nondefense spending cap for 2020 would be $632 billion and the 2021 cap would be $634.5 billion.
    - Those amounts represent a 3.1 percent increase in defense spending and 4.5 percent increase in nondefense spending from 2019 levels.
    - For some context, the nondefense cap increase of 4.5 percent is less than what the House has been using to write its 2020 spending bills.
    - The House 2020 THUD spending bill provides HUD a roughly 7 percent increase, which likely means the final THUD bill will be less than what the House has provided to date.
- The agreement suspends the debt limit until July 31, 2021.
- That's well after the 2020 elections.
- Some details still are not public.
- One is the issue of offsets.
    - When Congress last passed a two-year budget deal with the Bipartisan Budget Act of 2018, only $38 billion of about $300 billion in spending cap increases for both fiscal years 2018 and 2019 were offset.
    - The House leadership and White House reportedly agreed to increase the amount of the offset to spending cap increases to $77 billion.
    - <u>But,</u> they have reportedly *not* agreed to what those offsets will be.
    - Which is obviously crucial to any deal.
    - According to Politico, many of the administration's original proposed offsets were "nonstarters" with the House of Representatives.

- The other key issue is the House request for $22 billion in Veterans Administration health care spending outside the proposed nondefense spending caps.
- If there is agreement on these issues, there's a slim possibility that tax provisions may be added to the legislation, possibly including tax extenders.
    - That could include the new markets tax credit, as well as
        - the renewable energy production tax credit,
        - the Section 45L credit for energy-efficient multifamily and single-family homes as well as
        - the Section 179D deduction for energy-efficient commercial and multifamily buildings.
- Again, we don't know about that yet and there has been no reporting that extenders are included.
- And a reminder that while raising the debt limit and increasing the spending caps are connected, they are two separate and distinct issues.
    - The debt limit increase will allow Treasury to continue to operate, to continue to borrow to fund the federal government.
    - The spending caps must be raised or else there will be more than $120 billion in draconian cuts to defense and nondefense spending from their fiscal year 2019 levels when they pass a budget for 2020.
- There's a possibility that something could go wrong and the entire package won't sail through, in which case there will pressure to raise the debt ceiling.
    - That's because, as I noted earlier, Treasury could run out of money before Congress returns from its August recess in September.
- If Congress and the administration agree to the offsets and the VA health care spending in the debt limit and spending cap deal, the plan for now is for the House and Senate to vote on the agreements this week.
- This week is the final week before the House is scheduled to begin its August break on Friday.
    - The Senate is scheduled to meet through the following Friday, Aug. 2.
- This is a crucial time for supporters of expired and expiring tax provisions, as well as the minimum 4 percent for the low-income housing tax credit because the debt ceiling/spending cap deal is likely to be one of the few must-pass bills of the year.
    - And, as we've said before, must-pass legislation is traditionally the best vehicle for tax provisions.
- If tax provisions are added to the deal, it will be crucial to reach out to your Congressional delegation to ask them to reach out to leadership on adding the new markets tax credit, production tax credit, energy efficiency incentives and 4 percent floor to the legislation.
- And, even if tax provisions are not added to the deal, it is important for leadership to hear from members that community development tax credits are priority so that there is a better chance of them being added to the next "must-pass" bill.
- I will keep you posted on Twitter.
    - As you know, my handle is @Novogradac.

SEC, NASAA on OZs

- Now let's turn to opportunity zones.

- The Securities and Exchange Commission and the North American Securities Administrators Association issued a statement last week concerning opportunity zones investments.
    - The agencies oversee investment regulations and compliance in the United States.
- The joint statement explained how state and federal securities laws apply to qualified opportunity funds.
- The statement also provided guidance for so-called Main Street investors to participate in the opportunity zones incentive.
- Here are the top-level issues addressed by the SEC and NASAA:
    - Investments in qualified opportunity funds generally fit the definition of securities, which mean the funds must comply with applicable regulations.
    - Investors can invest in opportunity zones in a manner compliant with existing securities laws.
    - Main Street investors, by which they mean individual investors–in a contrast to so-called Wall Street investors–have a more difficult path, particularly if they live in the opportunity zones in which the investments are made.
- In a statement by SEC chairman Jay Clayton, he called for an effort to reduce the complexity of the path for Main Street investors to participate in the opportunity zones incentive.
- The qualified opportunity fund investors should assume registration with the SEC is required unless they are confident an exemption applies to their investment.
- There are some exemptions.
    - Proper structuring of the qualified opportunity fund may avoid the fund having to register as an investment company with the SEC.
        - For example, under Regulation D, known as Reg D, transactions not involving a public offering may need not be registered with the SEC.
            - In that case, the investor must still file a Reg D disclosure with the SEC and state laws may still apply.
    - The statement addresses whether a qualified opportunity fund, or QOF, is considered an "investment company."
    - An investment company is defined as a corporation, partnership, LLC or business trust engaged in the business of investing the pooled capital of investors in financial securities.
        - One exclusion from the definition of investment company is the Section 3(c)(1) exception for private investor funds.
            - Private investor funds are outstanding securities owned by less than 100 persons and where there is no public offering.
    - A second exclusion from the definition of investment company is the Section 3(c)(7) exception for qualified purchaser funds.
        - That is when there is not a public offering and the securities are owned by qualified purchaser as defined in the Act.
- The statement also clarifies whether an adviser to a QOF is subject to the Adviser Act or similar state laws.
- The statement and other documents from the SEC and the NASAA are in today's show notes.
- And I'd recommend that you contact your own securities law advisor or attorney for guidance with respect to any clarification need with respect to these rules.

Section 50(d) Regulations

- In historic tax credit news, the IRS issued final regulations last week concerning the income inclusion rules under Section 50(d).
- The regulations focus on the lessee of an investment credit property when the lessor elects to pass the tax credits through to the lessee.
- The final regulations mirror the temporary regulations that were posted nearly three years ago to the day.
- As a side note, temporary regulations only are in effect for three years so it's not a coincidence that they were finalized nearly three years from when they were released.
    - Those temporary regulations ended a period of uncertainty over how to handle Section 50(d) income.
    - That was partly because Revenue Procedure 2014-12, which provided a safe harbor for historic tax credit transactions, was silent on Section 50(d) income.
- The final regulations provide that:
    - Section 50(d) income is a partner item and not a partnership item.
    - Section 50(d) income does not increase an investor's basis in its partnership interest.
- Under the final regulations, Section 50(d) income being a partner items means:
    - a partnership doesn't allocate the 50(d) income among its partners.
    - Instead, the 50(d) income is reported by the ultimate credit claimant.
- These regulations apply to investment credit property placed in service after Sept. 18, 2016, which was the applicability date of the temporary regulations.
- In the same final rule, the IRS asked for comments on whether additional guidance is needed to coordinate recapture of the historic tax credit after changes made by tax reform legislation at the end of 2017.
    - That legislation, you'll recall, required the historic tax credit to be taken ratably over five years.
- If you have questions about your historic tax credit property–or even your renewable energy investment tax credit property–call a Novogradac partner.
- You can filter partners by tax credit specialty at www.novoco.com/partners.

Other News

- In other news, the New Markets Tax Credit Coalition last week released its annual progress report, based on a survey of community development entities.
    - This year's report featured feedback from more than 70 CDEs about their activity in 2018.
    - According to the report, those surveyed used $3.2 billion in allocation authority to finance 286 developments with $61 billion in aggregate investment.
    - That's a huge multiplier.
    - The coalition's report also said the new markets tax credit created more than 58,000 jobs in 2018.
    - There's a link to the report in today's show notes and I'll also tweet a link to it from my Twitter account.
- In other community development news, 10 members of the House introduced a bill to increase investment in underserved communities and Indian Country.
    - The ADVANCE Act of 2019 would require the CDFI Fund to create an outreach program for underserved communities.
    - The bill would also essentially require at least one CDE with a focus on Indian Country receive a new markets tax credit allocation in each round.
- In affordable housing news, HUD published a new chapter for its Housing Choice Voucher Guidebook last week.
    - HUD is doing an ongoing, incremental update to the guidebook and this chapter is on payment standards.
- And in renewable energy news, nearly 1,000 solar companies sent a letter to Congress asking for an extension of the investment tax credit.
    - The Solar Energy Industries Association led the effort, which also included a request for Congress to extend the Section 25D credit for residential energy-efficient property.
    - The renewable energy investment tax credit begins a phasedown next year, dropping from the current 30 percent to 10 percent beginning in 2022.
    - There's a link to the letter in today's show notes.
    - I'll also tweet it out as well.
- And finally, in state-level news, Pennsylvania's tax code now conforms to the federal Internal Revenue Code when it comes to opportunity zones investments.
    - That language was included in a bill signed by Gov. Tom Wolfe.
    - The change begins for tax years that start after Dec. 31, 2019.

RELATED RESOURCES

SEC, NASAA Statement on Opportunity Zones

Staff Statement on Opportunity Zones: Federal and State Securities Laws Considerations

SEC Guidance on Regulation Crowdfunding for “Main Street Investors”

Statement from SEC Chairman Jay Clayton on Opportunity Zones

Final Regulations on 50(d) Income

Treasury Decision 9872

New Markets Tax Credit Coalition Annual Report

New Markets Tax Credit Progress Report 2019

ADVANCE Act of 2019

H.R. 3664, Aiding Development of Vital Assets in native Communities and Environments (ADVANCE) Act of 2019

New HUD Housing Choice Voucher Chapter

HUD Housing Choice Voucher Program Guidebook

SEIA-Sponsored Letter to Congress on ITC Extension

Sign-on Letter to Congress Requesting Extension of Investment Tax Credit

Pennsylvania Bill to Conform State to Federal ITC on OZs

Pennsylvania H.B. 262, Amending Pennsylvania Tax Reform Code of 1971

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