Attachment 13-BA

Depending on the Task Force's decisions at the September 13, 2013 meeting, this draft Update will be subject to further revision and additional basis for conclusions will be necessary.

FINANCIAL ACCOUNTING SERIES

FASB ACCOUNTING STANDARDS UPDATE

No. 2013-XX
September 2013

Investments—Equity Method and Joint Ventures (Topic 323)

Accounting for Investments in Qualified Affordable Housing Projects

a consensus of the FASB Emerging Issues Task Force

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

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Accounting Standards Update

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Accounting Standards Update 2013-XX

Investments—Equity Method and Joint Ventures (Topic 323)

Accounting for Investments in Qualified Affordable Housing Projects

September 2013

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Summary ~~and Questions for Respondents~~

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The objective of this ~~proposed~~ Update is to provide guidance on accounting for investments in affordable housing projects that qualify for the low income housing tax credit.

The low income housing tax credit program is designed to encourage investment of private capital for use in the construction and rehabilitation of low income housing. This program is an indirect tax subsidy that allows investors in a flow-through limited liability entity, such as a limited partnership or limited liability company that manages or invests in a qualified affordable housing project, to receive the benefits of the tax credits allocated to the entity that owns the qualified affordable housing project. The Revenue Reconciliation Act of 1993, enacted in August 1993, retroactively extended and made permanent the low income housing tax credit. Investors in entities operating qualified affordable housing projects receive tax benefits in the form of tax credits and tax deductions from operating losses. The tax credits are allowable on the tax return each year over a 10-year period as a result of renting a sufficient number of units to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. Those credits are subject to recapture by the Internal Revenue Service over a 15-year period starting with the first year tax credits are earned.

Investments in qualified affordable housing projects through flow-through limited liability entities have different risks and rewards than traditional equity investments. Generally, investors in qualified affordable housing project investments seek a majority of their return through the receipt of tax credits and other tax benefits (such as operating losses). Accordingly, the principal risk associated with qualified affordable housing investments is potential noncompliance with the tax code requirements resulting in unavailability or recapture of the tax credits (for example, failure to rent property to qualified tenants may result in loss of low income housing tax credits) and other tax benefits.

Currently, under U.S. generally accepted accounting principles, a reporting entity that invests in a qualified affordable housing project may elect to account for that investment using the effective yield method if all the conditions in paragraph 323-740-25-1 are met. For those investments that are not accounted for using the effective yield method, paragraph 323-740-25-2 requires that those investments be accounted for in accordance with Subtopic 970-323, Real Estate—General—Investments—Equity Method and Joint Ventures, which results in the investments being accounted for under either the equity method or the cost method. Some stakeholders have said that the conditions requiring the availability of tax credits to be guaranteed by a creditworthy entity and the projected yield based solely on the cash flows from guaranteed tax credits to be positive in order to use the effective yield method are restrictive and therefore should be reconsidered. To these stakeholders, those conditions prevent many investments from qualifying for the use of the effective yield method, which they believe provides users with a better understanding of the returns from such investments.

Who Is Affected by the Amendments in This Update?

The amendments in this ~~proposed~~ Update ~~would~~ apply to all reporting entities that invest in a qualified affordable housing project through a limited liability entity that is a flow-through entity for tax purposes.

What Are the Main Provisions?

The amendments in this ~~proposed~~ Update ~~would~~ permit reporting entities that invest in a qualified affordable housing project through a limited liability entity to elect to account for the investment using the ~~effective yield~~proportional amortization method if all of the following conditions are met:

1. It is probable that the tax credits allocable to the investor will be available.
2. The investor retains no ~~operational influence~~ substantive participating rights in ~~over~~ the investment ~~other than protective rights~~, and substantially all of the projected benefits are from tax credits and other tax benefits (for example, tax benefits generated from the operating losses of the investment).
3. The investor's projected yield based solely on the cash flows from the tax credits and other tax benefits is positive.
4. The investor is a limited liability investor in the ~~affordable housing project~~limited liability entity for both legal and tax purposes, and the investor's liability is limited to its capital investment.

Transactions between the investor and the limited liability entity other than the investment in the limited liability entity shall not be considered when determining whether the conditions are met provided that:

1. The reporting entity is in the business of entering into such other transactions (for example, a financial institution that regularly extends loans to other housing projects).

2. ~~The~~Such other transactions are entered into at market rates commensurate ~~to~~with rates offered to other counterparties with similar credit quality.

3. The reporting entity does not acquire substantive participating rights as a result of ~~these~~such other transactions.

A reporting entity shall only evaluate whether the conditions have been met to elect to apply the proportional amortization method to an investment in an affordable housing project through a limited liability entity at the time of initial investment or upon occurrence of an event that changes the nature and design of the entity.

An investment in a qualified affordable housing project through a limited liability entity shall be tested for impairment if an event occurs or circumstances change that would indicate that it is no longer probable that the original amount of tax credits allocable to the investor will be available.

For those investments in qualified affordable housing projects not accounted for using the ~~effective yield~~proportional amortization method, the investment should~~would~~ be accounted for as an equity method investment or cost method investment in accordance with Subtopic 970-323.

The decision to apply the ~~effective yield~~proportional amortization method of accounting will continue to be an accounting policy decision rather than a decision to be applied to individual investments that qualify for use of the ~~effective yield~~proportional amortization method.

A reporting entity should~~would~~ disclose information that enables users of its financial statements to understand the following:

1. The nature of its investments in qualified affordable housing projects

2. The effect of the measurement of ~~the~~ its investments in ~~a~~ qualified affordable housing projects and the related tax credits on ~~the~~ its financial position and results of operations~~ of the reporting entity~~.

To meet these objectives, a reporting entity may consider disclosures such as the following:

1. The amount of affordable housing tax credits recognized during the year

2. The balance of the investment recognized in the statement of financial position

3. For qualified affordable housing project investments accounted for using the proportional amortization method, the amount recognized as a component of income taxes attributable to continuing operations

4. For qualified affordable housing project investments accounted for using the equity method, the amount of investment income or loss included in pretax income

~~3. Whether the qualified affordable housing project is currently subject to any regulatory reviews and the status of such reviews (for example, investigations by the housing authority)~~

~~4~~5. Any commitments or contingent commitments (for example, guarantees or commitments to provide additional capital contributions), including the amount of equity contributions that are contingent commitments related to qualified affordable housing project investments and the year or years in which contingent commitments are expected to be paid

~~5~~6. The amount and nature of the write-downs during the year resulting from the forfeiture or ineligibility of tax credits or other circumstances. These write-downs may be based on actual property-level foreclosures, loss of qualification due to occupancy levels, compliance issues with tax code provisions, or other issues.

How Do the Main Provisions Differ from Current U.S. Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

Under current U.S. GAAP, an entity that invests in a qualified affordable housing project through a limited partnership investment may elect to account for the investment using the effective yield method (described in paragraphs 323-740-35-2 and 323-740-45-2) provided all of the following conditions are met:

1. The availability (but not necessarily the realization) of the tax credits allocable to the investor is guaranteed by a creditworthy entity through a letter of credit, a tax indemnity agreement, or another similar arrangement.
2. The investor's projected yield based solely on the cash flows from the guaranteed tax credits is positive.
3. The investor is a limited partner in the affordable housing project for both legal and tax purposes, and the investor's liability is limited to its capital investment.

For those qualified affordable housing project investments that are not accounted for using the effective yield method, paragraph 323-740-25-2 requires that those investments be accounted for in accordance with Subtopic 970-323, which results in qualified affordable housing project investments being accounted for under either the equity method or the cost method.

The~~ proposed~~ amendments~~ would~~ modify the conditions that an entity must meet to elect to use a method other than the equity or cost method ~~the effective yield method for~~ to account for qualified affordable housing project investments and will~~would~~ allow the entity to use a proportional amortization method and amortize the initial cost of the investment in proportion to the amount of tax credits received and over the period that the investor receives tax credits~~both cash flows from the tax credits and other tax benefits for the calculation of the investor's projected yield~~. Additionally, the ~~proposed~~ amendments ~~would~~ require recurring disclosures about investments in qualified affordable housing projects. The Task Force concluded~~s~~~~believes~~ that the ~~proposed~~ amendments~~ would~~ should enable more entities to qualify to elect ~~the effective yield~~a proportional amortization method to account for investments in qualified affordable housing projects, which provides a presentation of the investment's performance net of taxes. In addition, the ~~proposed~~ amendments should~~would~~ help financial statement users understand the nature of qualified affordable housing project investments and their effect on the financial position and results of operations of the reporting entity.

When Will the Amendments Be Effective?

The amendments in this~~ proposed~~ Update should~~would~~ be applied retrospectively. Early adoption is~~would be~~ permitted as of the beginning of the fiscal year of adoption for financial statements not yet issued. The amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2014.~~The effective date will be determined after the Task Force considers stakeholder feedback on the proposed Update.~~

How Do the Provisions Compare with International Financial Reporting Standards (IFRS)?

IFRS does not contain any guidance specific to accounting for investments in qualified affordable housing projects.

Amendments to the *FASB Accounting Standards Codification*®

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs ~~x~~2–~~x~~5. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~.

~~**[Please use the following examples to model your document.]**~~

Amendments to Subtopic 323-740

2. Amend paragraphs 323-740-05-2 through 05-3, 323-740-15-3, 323-740-25-1 through 25-2, add paragraphs 323-740-25-1A through 25-1B, amend paragraphs 323-740-25-5, 323-740-30-1, 323-740-35-1 through 35-2, add paragraph 323-740-35-3 and 35-4, and amend paragraphs 323-740-45-1 through 45-2, with a link to transition paragraph 323-740-65-1, as follows:

Investments—Equity Method and Joint Ventures—Income Taxes

Overview and Background

Qualified Affordable Housing Project Investments

323-740-05-2 The Qualified Affordable Housing Project Investments Subsections provide income tax accounting guidance on a specific type of investment in real estate. This guidance applies to investments in limited ~~partnerships~~ liability entities that ~~operate~~manage or invest in qualified affordable housing projects and are flow-through entities for tax purposes.

323-740-05-3 The following discussion refers to and describes a provision within the Revenue Reconciliation Act of 1993; however, it shall not be considered a definitive interpretation of any provision of the Act for any purpose. The Revenue Reconciliation Act of 1993, enacted in August 1993, retroactively extended and made permanent the affordable housing credit. Investors in entities operating qualified affordable housing projects receive tax benefits in the form of tax deductions from operating losses and tax credits. The tax credits are allowable on the tax return each year over a 10-year period as a result of renting a sufficient number of units to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. These credits are subject to recapture over a 15-year period starting with the first year tax credits are earned. Corporate investors generally purchase an interest in a limited ~~partnership~~ liability entity that ~~operates~~manages or invests in the qualified affordable housing projects.

Scope and Scope Exceptions

Qualified Affordable Housing Project Investments

> Transactions

323-740-15-3 The guidance in the Qualified Affordable Housing Project Investments Subsections applies to investments in limited ~~partnerships~~ liability entities that ~~operate~~manage or invest in qualified affordable housing projects and are flow-through entities for tax purposes.

Recognition

Qualified Affordable Housing Project Investments

323-740-25-1 An entity that invests in a qualified affordable housing project through a limited ~~partnership investment~~liability entity may elect to account for the investment using the ~~effective yield~~ proportional amortization method (described in paragraphs 323-740-35-2 and 323-740-45-2) provided all of the following conditions are met:

a. ~~The availability (but not necessarily the realization) of the tax credits allocable to the **investor** is guaranteed by a creditworthy entity through a letter of credit, a tax indemnity agreement, or another similar arrangement.~~ It is **{add glossary link to 2nd definition}probable{add glossary link to 2nd definition}** that the tax credits allocable to the **investor** will be available.

aa. The investor retains no ~~operational influence over~~substantive **{add glossary link to 2nd definition}**participating rights**{add glossary link to 2nd definition}** in the investment ~~other than **{add glossary link to 2nd definition}protective rights{add glossary link to 2nd definition}**~~, and substantially all of the projected benefits are from tax credits and other tax benefits (for example, tax benefits generated from the operating losses of the investment).

b. The investor's projected yield based solely on the cash flows from the ~~guaranteed~~ tax credits and other tax benefits is positive.

c. The investor is a limited liability investor~~partner~~ in the ~~affordable housing project~~limited liability entity for both legal and tax purposes, and the investor's liability is limited to its capital investment.

323-740-25-1A Other transactions (for example, bank loans) between the investor and the limited liability entity shall not be considered when determining whether the conditions for the effective yield method are met, provided that all three of the following are true:

a. The reporting entity is in the business of entering into such other transactions (for example, a financial institution that regularly extends loans to other housing projects).
b. ~~The~~Such other transactions are entered into at market rates commensurate ~~to~~with rates offered to other counterparties with similar credit quality.
c. The reporting entity does not acquire substantive participating rights as a result of ~~these~~such other transactions.

323-740-25-1B A reporting entity shall only evaluate whether the conditions in paragraph 323-740-25-1 have been met to elect to apply the proportional amortization method to an investment in an affordable housing project through a limited liability entity at the time of initial investment or upon occurrence of an event that changes the nature and design of the entity.

323-740-25-2 For ~~a limited partnership~~ an investment in a qualified affordable housing project through a limited liability entity not accounted for using the ~~effective yield~~proportional amortization method, the investment shall be accounted for in accordance with Subtopic 970-323. In accounting for such an investment under that Subtopic, the requirements of this Subsection that are not related to the ~~effective yield~~proportional amortization method shall be applied.

323-740-25-3 A liability shall be recognized for delayed equity contributions that are unconditional and legally binding. A liability also shall be recognized for equity contributions that are contingent upon a future **event** when that contingent event becomes probable. Topic 450 and paragraph 840-30-55-15 provide additional guidance on the accounting for delayed equity contributions.

323-740-25-4 The decision to apply the ~~effective yield~~proportional amortization method of accounting is an accounting policy decision rather than a decision to be applied to individual investments that qualify for use of the ~~effective yield~~proportional amortization method.

323-740-25-5 Immediate recognition at the time the investment is purchased of the entire benefit of the tax credits to be received during the term of ~~a limited partnership~~ an investment in a qualified affordable housing project through a limited liability entity is not appropriate (that is, affordable housing credits shall not be recognized in the financial statements before their inclusion in the investor's tax return).

Initial Measurement

Qualified Affordable Housing Project Investments

323-740-30-1 Paragraph 323-740-25-5 prohibits immediate recognition of tax credits, at the time of investment, for the entire benefit of tax credits to be received during the term of ~~a limited partnership~~ an investment in a qualified affordable housing project through a limited liability entity. See paragraph 323-740-35-2 for the required subsequent measurement calculation methodology when an entity uses the ~~effective yield~~proportional amortization method of accounting for ~~a limited partnership~~ an investment in a qualified affordable housing project through a limited liability entity.

Subsequent Measurement

Qualified Affordable Housing Project Investments

323-740-35-1 This guidance addresses the methodology for measuring the periodic net benefit of an affordable housing tax credit when ~~a limited partnership~~ an investment in a qualified affordable housing project through a limited liability entity is accounted for using the ~~effective yield~~proportional amortization method.

323-740-35-2 Under the ~~effective yield~~proportional amortization method, the investor recognizes tax credits and other tax benefits as they are allocated ~~realized~~ and amortizes the initial cost of the investment ~~in~~ ~~to provide a constant effective yield~~ over the period that the investor receives the tax credits ~~and other tax benefits~~ ~~are allocated to the investor~~. ~~The effective yield is the internal rate of return on the investment, based on the cost of the investment and the guaranteed~~ ~~probable~~ ~~tax credits~~ ~~and other tax benefits~~ ~~allocated to the investor.~~ The amortization amount shall be calculated as follows:

a. The gross investment balance multiplied by:

b. The percentage of tax credits allocated to the investor in the current period (Actual tax credits allocated to the investor in the current period divided by the total estimated tax credits expected to be received during the life of the LIHTC investment).

~~Any expected residual value of the investment shall be excluded from the effective yield calculation. Cash received from operations of the limited partnership or sale of the property, if any, shall be included in earnings when realized or realizable.~~

323-740-35-3 Any expected residual value of the investment shall be excluded from the ~~effective yield~~ proportional amortization calculation. Cash received from operations of the limited ~~partnership~~ liability entity or sale of the property, if any, shall be included in earnings when realized or realizable.

323-740-35-4 An investment in a qualified affordable housing project through a limited liability entity shall be tested for impairment if an event occurs or circumstances change that would indicate that it is no longer probable that the original amount of tax credits allocable to the investor will be available.

Other Presentation Matters

Qualified Affordable Housing Project Investments

323-740-45-1 This guidance addresses the income statement presentation of the affordable housing tax credit when ~~a limited partnership~~ an investment in a qualified affordable housing project through a limited liability entity is accounted for using the ~~effective yield~~proportional amortization method.

323-740-45-2 Under the ~~effective yield~~proportional amortization method, the tax credit allocated and any other tax benefits, net of the amortization of the investment in the limited ~~partnership~~ liability entity, is recognized in the income statement as a component of **income taxes** attributable to continuing operations. ~~Any other tax benefits received shall be accounted for pursuant to the general requirements of Topic 740.~~

3. Add paragraphs 323-740-50-1 through 50-2 and their related headings, with a link to transition paragraph 323-740-65-1, as follows:

Disclosure

Qualified Affordable Housing Project Investments

323-740-50-1 A reporting entity that invests in a qualified affordable housing project shall disclose information that enables users of its financial statements to understand the following:

a. The nature of its investments in qualified affordable housing projects
b. The effect of the measurement of ~~the~~ its investments in ~~a~~ qualified affordable housing projects and the related tax credits on ~~the~~ its financial position and results of operations~~ of the reporting entity~~.

323-740-50-2 To meet the objectives in ~~the preceding~~ paragraph 323-740-50-1, a reporting entity may consider disclosures such as the following:

a. The amount of affordable housing tax credits and other tax benefits recognized during the year
b. The balance of the investment recognized in the statement of financial position
c. For qualified affordable housing project investments accounted for using the ~~effective yield~~proportional amortization method, the amount recognized as a component of income taxes attributable to continuing operations~~ and the yield used to calculate that amount~~
d. For qualified affordable housing project investments accounted for using the equity method, the amount of investment income or loss included in pretax income

~~c. Whether the qualified affordable housing project is currently subject to any regulatory reviews and the status of such reviews (for example, investigations by the housing authority or review by the Internal Revenue Service)~~

~~d~~e. Any commitments or contingent commitments (for example, guarantees or commitments to provide additional capital contributions), including the amount of equity contributions that are contingent commitments related to qualified affordable housing project investments and the year or years in which contingent commitments are expected to be paid

~~e~~f. The amount and nature of the write-downs during the year resulting from the forfeiture or ineligibility of tax credits or other circumstances. Those write-downs may be based on actual property-level foreclosures, loss of qualification due to occupancy levels, compliance issues with tax code provisions, or other issues.

4. ~~Amend~~ Remove paragraphs 323-740-55-4, 323-740-55-6, and 323-740-55-10~~, with a link to transition paragraph 323-740-65-1,~~ as follows:

~~Implementation Guidance and Illustrations~~

~~Qualified Affordable Housing Project Investments~~

~~**323-740-55-1** This Section is an integral part of the requirements of this Subtopic.~~

~~> Illustrations~~

~~> > Example 1: Application of Accounting Guidance to a Limited Partnership Investment in a Qualified Affordable Housing Project~~

~~**323-740-55-2** This Example demonstrates the application of the cost, equity, and effective yield methods of accounting for a limited partnership investment in a qualified affordable housing project.~~

~~**323-740-55-3** The following are the terms for this Example.~~

Date of investment	January 1, 19X1
Purchase Price of Investment	$ 100,000

~~**323-740-55-4** This Example has the following assumptions:~~

- ~~a. All cash flows (except initial investment) occur at the end of each year.~~
- ~~b. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).~~
- ~~c. The **investor** made a $100,000 investment for a 5 percent limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.~~
- ~~d. The partnership finances the project cost of $4,000,000 with 50 percent equity and 50 percent debt.~~
- ~~e. The annual tax credit allocation (equal to 8 percent of the project's original cost) will be received for a period of 10 years.~~
- ~~f. The investor's tax rate is 40 percent.~~
- ~~g. The project will operate with break-even pretax cash flows including debt service during the first 15 years of operations.~~
- ~~h. The project's taxable and book loss will be equal to depreciation expense. The cumulative book loss recognized by the investor under the equity method of accounting is limited to the $100,000 investment.~~
- ~~i. Deferred taxes are provided for the difference between the book and tax bases of the investment. Deferred taxes are provided for losses in excess of the at-risk investment.~~
- ~~ii. Under the effective yield method, other tax benefits included in the calculation of the yield include the tax effect of depreciation on the underlying assets.~~
- ~~j. The investor will maintain the investment for 15 years (so there will be no recapture of tax credits).~~
- ~~k. The investor expects that the estimated residual value of the investment will be zero.~~
- ~~l. Under the effective yield method, all of the conditions described in paragraph 323-740-25-1 are met a letter of credit or similar guarantee exists to qualify the investment for the use of the effective yield method.~~

~~**323-740-55-5** The investor's cash flow analysis follows.~~

Year	Purchase of Investment (1)	Tax Depreciation (2)	Tax Credit (3)	Taxes Saved (4)	Cash Saved (Spent)
1	$ 100,000				$ (100,000)
1		$ 7,273	$ 16,000	$ 18,909	18,909
2		7,273	16,000	18,909	18,909
3		7,273	16,000	18,909	18,909
4		7,273	16,000	18,909	18,909
5		7,273	16,000	18,909	18,909
6		7,273	16,000	18,909	18,909
7		7,273	16,000	18,909	18,909
8		7,273	16,000	18,909	18,909
9		7,273	16,000	18,909	18,909
~~10~~		~~7,273~~	~~16,000~~	~~18,909~~	~~18,909~~
11		7,273		2,909	2,909
12		7,273		2,909	2,909
13		7,273		2,909	2,909
14		7,273		2,909	2,909
15		7,273		2,909	2,909
Total		$ 109,095	$ 160,000	$ 203,635	$ 103,635

(1) Assumed investment for a 5 percent limited partnership interest in the project.

(2) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.5 years.

(3) 8 percent tax credit on $200,000 tax basis of the underlying assets.

(4) (Column [2] x 40% tax rate) + Column (3).

~~**323-740-55-6** A summary of the net income effect of the cost, equity, and effective yield methods follows. This summary is based on the detailed analyses of the cost method with amortization, the equity method, and the effective yield method, which appear after the following summary.~~

Summary of Net Income Impact

	Cost Method			**Equity Method**			**Effective Yield Method**				
Year	**Income (Loss) Continuing Operations**	**Income Tax Expense (Benefit)**	**Net Income**	**Income (Loss) Continuing Operations**	**Income Tax Expense (Benefit)**	**Net Income**	**Income (Loss) Continuing Operations**	**Income Tax Expense (Benefit)**		**Net Income**	
1	$ (10,000)	$ (20,000)	$ 10,000	$ (7,273)	$ (18,909)	$ 11,636		~~$ (12,164)~~	$ (13,246)	~~$ 12,164~~	$ 13,246
2	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(11,795)~~	(12,852)	~~11,795~~	12,852
3	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(11,392)~~	(12,401)	~~11,392~~	12,401
4	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(10,949)~~	(11,886)	~~10,949~~	11,886
5	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(10,464)~~	(11,297)	~~10,464~~	11,297
6	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(9,932)~~	(10,623)	~~9,932~~	10,623
7	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(9,349)~~	(9,853)	~~9,349~~	9,853
8	(10,000)	(20,000)	10,000	(7,273)	(18,909)	11,636		~~(8,710)~~	(8,974)	~~8,710~~	8,974
9	(10,000)	(20,000)	10,000	(25,816)	(26,327)	511		~~(8,009)~~	(7,969)	~~8,009~~	7,969
10	(10,000)	(20,000)	10,000	(16,000)	(22,401)	6,401		~~(7,236)~~	(899)	~~7,236~~	899
11											
12											
13											
14											
15											
Total	$(100,000)	$(200,000)	######	$ (100,000)	$ (200,000)	######	$ -	~~$ (100,000)~~	$ (100,000)	~~$100,000~~	$ 100,000

~~**323-740-55-10** A detailed analysis of the effective yield method follows.~~ ~~**[For ease of readability, the table is not underlined as new text.]**~~

Year	Net Investment (1)	Tax Credits (2)	Amortization of Investment (3)	Tax Depreciation (4)	Current Tax Benefit (5)	Deferred Tax Benefit (Expense) (6)	Impact on Net Income (7)
1	$ 93,607	$ 16,000	$ 6,393	$ 7,273	$ 12,516	$ (352)	$ 12,164
2	86,599	16,000	7,008	7,273	11,901	(106)	11,795
3	78,918	16,000	7,681	7,273	11,228	163	11,391
4	70,499	16,000	8,419	7,273	10,490	458	10,948
5	61,272	16,000	9,227	7,273	9,682	782	10,464
6	51,158	16,000	10,114	7,273	8,795	1,136	9,931
7	40,073	16,000	11,085	7,273	7,824	1,525	9,349
8	27,923	16,000	12,150	7,273	6,759	1,951	8,710
9	14,605	16,000	13,318	7,273	5,591	2,418	8,009
10		16,000	14,605	7,273	4,304	2,935	7,239
11				7,273	2,909	(2,909)	
12				7,273	2,909	(2,909)	
13				7,273	2,909	(2,909)	
14				7,273	2,909	(2,909)	
15				7,273	2,909	(2,909)	
Total		$ 160,000	$ 100,000	$ 109,095	$ 103,635	$ (3,635)	$ 100,000

Internal rate of return based on tax credits only	9.61%

~~(1) End-of-year investment for a 5 percent limited partnership interest in the project net of amortization in Column (3).~~

~~(2) 8 percent tax credit on $200,000 tax basis of the underlying assets~~

~~(3) Column (2) - (beginning investment x 9.61%).~~

~~(4) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.~~

~~(5) Column (2) - Column (3) + (Column [4] x 40% tax rate).~~

~~(6) The change in deferred taxes resulting from the difference between the book and tax bases of the investment and tax losses in excess of the at-risk investment. In this Example, that amount can be determined as follows: (Column [3] - Column [4]) x 40% tax rate.~~

Year		Net Investment (1)	Tax Credits (2)		Amortization of Investment (3)		Tax Depreciation (4)		Current Tax Benefit (5)		Deferred Tax Benefit (Expense) (6)		Impact on Net Income (7)
1	$	95,411	16,000	$	4,589	$	7,273	$	14,320	$	(1,074)	$	13,246
2		90,165	16,000		5,246		7,273		13,663		(811)		12,852
3		84,167	16,000		5,998		7,273		12,911		(510)		12,401
4		77,311	16,000		6,856		7,273		12,053		(167)		11,886
5		69,473	16,000		7,838		7,273		11,071		226		11,297
6		60,512	16,000		8,961		7,273		9,948		675		10,623
7		50,268	16,000		10,244		7,273		8,665		1,188		9,853
8		38,557	16,000		11,711		7,273		7,198		1,776		8,974
9		25,169	16,000		13,388		7,273		5,522		2,447		7,969
10 [(a)]			16,000		25,169		7,273		(6,260)		7,159		899
11							7,273		2,909		(2,909)		-
12							7,273		2,909		(2,909)		-
13							7,273		2,909		(2,909)		-
14							7,273		2,909		(2,909)		-
15							7,273		2,909		(2,909)		-
Total			$ 160,000	$	100,000	$	109,095	$	103,636	$	(3,636)	$	100,000

Internal rate of return based on tax credits and other tax benefits 14.32%

(1) End-of-year investment for a 5 percent limited partnership interest in the project net of amortization in Column (3).
(2) 8 percent tax credit on $200,000 tax basis of underlying assets.
(3) Column (2) + (Column (4) x 40% tax rate) – (beginning investment x 14.32%).
(4) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.5 years.
(5) Column (2) – Column (3) + (Column (4) x 40% tax rate).
(6) The change in deferred taxes resulting from the difference between the book and tax bases of the investment and tax losses in excess of the at-risk investment. In this Example, that amount can be determined as follows: (Column (3) – Column (4)) x 40% tax rate.
(7) Column (5) + Column (6).

(a) Projections at the end of Year 10 indicate that the investment will generate a negative yield over the remaining term of the investment indicating a need to assess the investment for impairment. For purposes of the Example, the impairment loss is determined to equal the remaining net investment balance.

5. Add paragraph 323-740-65-1 and its related heading as follows:

> Transition Related to Accounting Standards Update No. 2013-XX, *Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects*

323-740-65-1 The following represents the transition information related to Accounting Standards Update No. 2013-XX, *Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects:*

a. The pending content that links to this paragraph shall be effective for fiscal years and interim periods within those years, beginning after ~~[date to be inserted after exposure]~~December 15, 2014.
b. The entity shall apply the pending content that links to this paragraph retrospectively for all periods presented.
c. Early application of the pending content that links to this paragraph is permitted as of the beginning of the fiscal year of adoption for financial statements not yet issued.

d. An entity shall provide the disclosures in paragraphs 250-10-50-1 through 50-3 in the period the entity adopts the pending content that links to this paragraph.

The amendments in this ~~proposed~~ Update were adopted~~pproved for publication~~ by the unanimous vote ~~affirmative vote~~ of the ~~six~~ seven members of the Financial Accounting Standards Board. ~~*Mr. Buck voted against publication of the amendments. His alternative view is set out at the end of the basis for conclusions.*~~

Members of the Financial Accounting Standards Board:

Russell G. Golden, *Chairm~~e~~an* ~~Leslie F. Seidman, *Chairman*~~
Daryl E. Buck
~~Russell G. Golden~~
James L. Kroeker
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information, Basis for Conclusions, and Alternative View – TO BE UPDATED FURTHER

Introduction

BC1. The following summarizes the Task Force's considerations in reaching the conclusions in this ~~proposed~~ Update. It includes the Board's basis for ratifying the Task Force conclusions when needed to supplement the Task Force's considerations. It also includes reasons for accepting certain approaches and rejecting others. Individual Task Force and Board members gave greater weight to some factors than to others.

Background Information

BC2. The low income housing tax credit program is designed to encourage investment of private capital for use in the construction and rehabilitation of low income housing. This program is an indirect tax subsidy that allows investors in a flow-through limited liability entity, such as a limited partnership or limited liability company that manages or invests in a qualified affordable housing project, to receive the benefits of the tax credits allocated to the entity that owns the qualified affordable housing project. The Revenue Reconciliation Act of 1993, enacted in August 1993, retroactively extended and made permanent the low income housing tax credit. Investors in entities operating qualified affordable housing projects receive tax benefits in the form of tax credits and tax deductions from operating losses. The tax credits are allowable on the tax return each year over a 10-year period as a result of renting a sufficient number of units to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. These credits are subject to recapture by the Internal Revenue Service over a 15-year period starting with the first year the tax credits are earned.

BC3. Investments in qualified affordable housing projects through flow-through limited liability entities have different risks and rewards than traditional equity investments. Generally, investors in qualified affordable housing project investments seek a majority of their return through the receipt of tax credits and other tax benefits (such as operating losses). Accordingly, the principal risk associated with qualified affordable housing investments is potential noncompliance with the tax code requirements resulting in unavailability or recapture of the tax credits (for example, failure to rent property to qualified tenants may result in loss of low income housing tax credits) and other tax benefits.

BC4. Under current U.S. GAAP, an entity that invests in a qualified affordable housing project through a limited partnership investment may elect to account for the investment using the effective yield method (described in paragraphs 323-740-35-2 and 323-740-45-2) provided all of the following conditions are met:

a. The availability (but not necessarily the realization) of the tax credits allocable to the investor is guaranteed by a creditworthy entity through a letter of credit, a tax indemnity agreement, or another similar arrangement.
b. The investor's projected yield based solely on the cash flows from the guaranteed tax credits is positive.
c. The investor is a limited partner in the affordable housing project for both legal and tax purposes, and the investor's liability is limited to its capital investment.

BC5. For those qualified affordable housing project investments that are not accounted for using the effective yield method, paragraph 323-740-25-2 requires that those investments be accounted for in accordance with Subtopic 970-323, which results in qualified affordable housing project investments being accounted for under either the equity method or the cost method.

Scope and Other Considerations

BC6. The Task Force reached a consensus~~ for exposure~~ that an entity may elect to account for a limited liability investment in a qualified affordable housing project using the ~~effective yield~~proportional amortization method if all of the following conditions are met:

a. It is probable that the tax credits allocable to the investor will be available.
b. The investor retains no operational influence over the investment other than protective rights, and substantially all of the projected benefits are from tax credits and other tax benefits (for example, tax benefits generated from the operating losses of the investment).
c. The investor's projected yield based solely on the cash flows from the tax credits and other tax benefits is positive.
d. The investor is a limited liability investor in the affordable housing project for both legal and tax purposes, and the investor's liability is limited to its capital investment.

BC7. The Task Force agreed that for those limited liability investments in qualified affordable housing projects not accounted for using the ~~effective yield~~proportional amortization method, the investment should~~would~~ be accounted for in accordance with Subtopic 970-323.

BC8. In reaching its consensus~~ for exposure~~, the Task Force discussed whether the scope of the amendments in this~~ proposed~~ Update should apply only to limited partnership investments in affordable housing projects. The Task Force noted that as investments in affordable housing projects have increased, entities have invested in affordable housing projects through both limited partnerships and limited liability companies. One Task Force member noted that the limited liability entity is required to elect to be taxed as a flow-through entity for the investor to be eligible to receive the tax credits. The Task Force clarified that the amendments in this ~~proposed~~ Update should apply to both limited partnership and limited liability investments in qualified affordable housing projects.

BC9. In reaching the decision to add this Issue to the Task Force's agenda, the Board noted that limiting the scope of this Issue to only investments in qualified affordable housing projects will result in a quicker response by the Task Force to the various concerns in practice with respect to the income statement presentation of those investments. Because there is existing guidance in Issue 94-1, the Task Force ~~would~~ ha~~ve~~s the ability to revisit the conclusions of that consensus to determine whether modifications are necessary to the criteria for applying the ~~effective yield~~proportional amortization method. Additionally, due to the potential interaction with the Board's research project on the accounting for government assistance and the complexities involved in defining a "tax credit investment," the Board concluded~~believes~~ that the scope of this Issue should be narrow. Some Task Force members expressed concern about limiting the scope of the ~~proposed~~ Update because it may result in treating investments made under other tax credit programs that meet the specified conditions in the ~~proposed~~ Update differently. As a result of those concerns, the Task Force agreed to include a question for stakeholders about the applicability of the guidance in this ~~proposed~~ Update to investments made under other tax credit programs.

BC10. The Task Force observed that the threshold for applying the ~~effective yield~~proportional amortization method should remain high absent the requirement for a guarantee by a creditworthy entity and therefore decided that it should be probable that the tax credits allocable to the investor will be available. The Task Force acknowledged that such a threshold should be higher than the more-likely-than-not threshold described in Topic 740, Income Taxes.

BC11. In reaching its consensus ~~for exposure~~, the Task Force also clarified that operational influence should~~would~~ be limited only to protective rights that do not allow the limited liability investors to participate in financial and operating decisions of the limited liability entity that are made in the ordinary course of business. The Task Force noted that most limited liability investments in affordable housing projects have some protective rights, and paragraphs 810-20-55-1 through 55-9 discuss factors that distinguish between a limited partner's protective and substantive participating rights.

BC12. The Task Force expects that more investments in qualified affordable housing projects will~~would~~ qualify for the ~~effective yield~~proportional amortization method than under current U.S. GAAP as a result of (a) removing the requirement for a guarantee by a creditworthy entity and (b) modifying the requirement for a positive yield based not only on the cash flows from the tax credits but rather on cash flows from both the tax credits *and* other tax benefits. One Task Force member disagreed with the application of the "effective yield" measurement approach if the requirement for a guarantee by a creditworthy entity was removed and the requirement for a positive yield included other tax benefits. That Task Force member noted that the effective yield method of accounting should~~would~~ be appropriate for investments with characteristics similar to those of debt instruments. That is, the effective yield method of measurement is appropriate for investments with fixed cash inflows or cash inflows that vary on the basis of financial terms (for example, interest rates). The Task Force member concluded~~believes~~ that current or future investments in qualified affordable housing projects that qualify for the effective yield measurement approach could have significant cash flow variability that is not based on financial terms. The Task Force member concluded~~believes~~ that a more appropriate measurement method for investments meeting the conditions specified ~~would~~[n1] ~~be~~is to amortize the investment ~~on a~~ systematically ~~basis~~ on the basis of the realization of the tax benefits. The Task Force agreed to include a question for stakeholders about the method of accounting that should be used to account for investments in qualified affordable housing projects.

Disclosures

BC13. The Task Force reached a consensus ~~for exposure~~ that the amendments in the ~~proposed~~ Update should include required disclosure objectives. In reaching its consensus ~~for exposure~~, the Task Force noted that disclosures should help users of the financial statements understand the nature of the qualified affordable housing project investments and the effect of those investments on the reporting entity's financial statements. The amendments should include disclosure objectives for reporting entities and provide potential items that the reporting entity should consider disclosing to meet those objectives. Disclosures should also be incremental to limit the increased burden on reporting entities. Therefore, the Task Force suggested that to meet the disclosure objectives, a reporting entity may consider disclosures such as the following:

a. The amount of affordable housing tax credits recognized during the year
b. For qualified affordable housing project investments accounted for using the equity method, the amount of investment income or loss included in pretax income
c. Whether the qualified affordable housing project is currently subject to any regulatory reviews and the status of such reviews (for example, investigations by the housing authority)
d. Any commitments or contingent commitments (for example, guarantees or commitments to provide additional capital contributions), including the

amount of equity contributions that are contingent commitments related to qualified affordable housing project investments and the year(s) that contingent commitments are expected to be paid

e. The amount and nature of the write-downs during the year resulting from the forfeiture or ineligibility of tax credits or other circumstances. Those write-downs may be based on actual property-level foreclosures, loss of qualification due to occupancy levels, compliance issues with tax code provisions, or other issues.

Transition and Transition Disclosures

BC14. The Task Force discussed whether the ~~proposed~~ guidance should be applied retrospectively, prospectively to new investments, or under a modified retrospective approach with a cumulative-effect adjustment to opening retained earnings at the beginning of the fiscal year of adoption. The Task Force reached a consensus ~~for exposure~~ that an entity should apply the ~~proposed~~ guidance on a retrospective basis by applying the requirements for accounting changes in paragraphs 250-10-45-5 through 45-10 because it believes that investments in qualified affordable housing projects have long terms and a retrospective application should~~would~~ provide comparable information. The Task Force also concluded~~believes~~ that information to retrospectively apply the ~~proposed~~ amendments should~~would~~ be readily available. Early adoption is~~would be~~ permitted as of the beginning of the fiscal year of adoption for financial statements not yet issued.

BC15. The guidance on other presentation matters in Subtopic 250-10, Accounting Changes and Error Corrections—Overall, is applicable for any voluntary change in accounting principle, including a change in the method of applying an accounting principle. The Task Force reached a consensus ~~for exposure~~ to apply the disclosure requirements in Section 250-10-50 for an accounting change required by the ~~proposed~~ guidance. No additional transition disclosures other than the requirements in paragraphs 250-10-50-1 through 50-3 are required.

Benefits and Costs

BC16. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Task Force's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC17. The Task Force does not anticipate that entities will incur significant costs as a result of the amendments in this ~~proposed~~ Update. The Task Force also concludeds~~believes~~ that presenting the returns from such investments using a~~n~~ ~~effective yield~~proportional amortization method should~~would~~ be reflective of the investment's performance and should~~would~~ provide users with better understanding of the entity's investment returns.

Alternative View

BC18. Mr. Buck disagrees with the publication of this proposed Update because he believes that it does not result in an improvement to financial reporting. Mr. Buck believes that investments in qualified affordable housing projects through limited liability entities have similar characteristics to other investments in limited liability entities. Therefore, Mr. Buck believes that the effective yield method, wherein no pretax losses are presented in the financial statements, represents an exception to the accounting requirements for economically similar transactions, and he would support its elimination as an elective, specialized accounting treatment.

BC19. Mr. Buck notes that the Board recently affirmed its tentative decision to eliminate the separate lease accounting model for leveraged leases, which is also a model that factors tax benefits into a calculated after-tax yield. Thus, removing the exception that permits the effective yield method of accounting for certain investments in qualified affordable housing projects would be consistent with the Board's decision in the leases project.

BC20. While Mr. Buck would prefer to remove the effective yield method from U.S. GAAP, he would not object to its retention with the existing qualification criteria (that is, retain the status quo) until such time as the Board could more broadly consider the accounting for tax-advantaged investments. However, because the proposed guidance would instead ease the qualification criteria and, thus, likely result in an expansion of the ability to elect the effective yield method and an increase in the related diversity in practice, Mr. Buck does not believe that it would benefit financial statement users.

Amendments to the XBRL Taxonomy

The amendments to the *FASB Accounting Standards Codification®* in this Accounting Standards Update require changes to the U.S. GAAP Financial Reporting Taxonomy (UGT). Those changes, which will be incorporated into the proposed 2014 UGT, are available for public comment at www.fasb.org, and finalized as part of the annual release process starting in September 2013.

~~The provisions of this Exposure Draft, if finalized as proposed, would require changes to the U.S. GAAP Financial Reporting Taxonomy (UGT). We welcome comments on these proposed changes to the UGT at ASU Taxonomy Changes provided at www.fasb.org. After the FASB has completed its deliberations and issued a final Accounting Standards Update, proposed amendments to the UGT will be made available for public comment at www.fasb.org and finalized as part of the annual release process.~~