June 7, 2022

Ms. Hillary H. Salo
Chair, Emerging Issues Task Force
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Comments on EITF 21-A, Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method – Issue Summary No. 1C

Dear Ms. Halo:

On behalf of the members of the GAAP Accounting for Tax Credits Working Group ("GAAP Working Group"), we submit the following comments, considerations, and recommendations in connection with the pending Emerging Issues Task Force ("EITF") project–EITF 21-A, Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method. We believe that improving the accounting treatment for investments in tax credits is of vital importance to ensure the relevant and faithfully representative financial reporting for investments such as those made in the Low-Income Housing Tax Credit ("LIHTC"), New Markets Tax Credit ("NMTC"), Historic Rehabilitation Tax Credit ("HTC"), Renewable Energy Tax Credit ("RETC") and others.

We are encouraged by the efforts of the EITF to consider making proportional amortization available to other tax credits as was recommended originally by FASB staff in ASU 2014-01. As was voted on in the March 24th meeting, the recommendation by the EITF to remove the LIHTC limitation so that ALL tax credit investments have an opportunity to elect into the proportional amortization method is a positive step forward to simplifying the accounting treatment for various tax credits. However, in order for the guidance to be applied broadly, we recommend the EITF and FASB also consider reviewing and making changes to the current criteria.

In an effort to organize the GAAP Working Group's comments for the EITF to consider, we have organized our comments by addressing the eleven questions in the Issue Summary No. 1C document included in the March 24th meeting materials.

Issue Summary No. 1C

Question 1: At which level does the Task Force want the proportional amortization method accounting policy election to apply?

We recommend the Task Force reevaluate this question and reconsider Alternative A, the staff recommendation. Due to the existing criteria and how they are currently understood, it will be difficult for some investments in certain types of tax credits to be eligible for the proportional amortization method. Due to this diversity in types of tax credits as well as the possibility of future, unknown tax credits, we believe it is most practical to allow preparers to apply the election to use the proportional amortization method on a tax-credit-program-by-tax-credit-program basis for tax credit investments that meet the criteria in paragraph 323-740-25-1.

We support the staff comment that "Alternative A allows for an appropriate level of flexibility for entities to manage the costs associated with evaluating whether an investment is eligible to apply the proportional amortization method and the benefits of the resulting financial reporting in the income tax line item depending on the number and size of investments within that tax credit program." It is difficult to expand the existing criteria to all investments and assume that one size fits all. Having an election in place on a tax-credit-program-by-tax-credit-program basis allows investors the flexibility needed to address the diversity of investments in their portfolio and make the accounting policy election that will provide the most relevant information for each portfolio. It would be much more costly if an investor is required to determine eligibility for all of its tax credit investments and may impact its decision to make certain tax credit investments.

We also agree with the staff's understanding that there is not much diversity in practice in considering investments that qualify for more than one tax credit and how to apply the proportional amortization method by determining which tax credits are the principal benefits of the investment. We believe this practice would continue to be applied if the proportional amortization method is available to all tax credits.

Question 2: Does the Task Force want to make any changes to Criteria #1, #4, and #5 in paragraphs 323- 740-25-1(a), (b), and (c), respectively?

We recommend the Task Force reevaluate this question and consider making changes to Criterion #4 regarding the positive yield requirement. The positive yield criterion will likely preclude many investment structures currently utilized by the solar industry from qualifying for the proportional amortization method. This is a result of credits being recognized upfront in conjunction with tax equity investors contributing more than one dollar per dollar of tax credit received. Conversely, production tax credits, LIHTCs, HTCs and NMTCs are monetized over a period of five years or more and are typically invested on a discounted basis for less than one dollar per dollar of tax credit received. Tax credits invested on a discounted basis naturally have a higher proportion of tax credits/benefits relative to equity contributions that help in satisfying both the positive yield and substantially all criteria.

Solar and wind transactions generate cash flows, a portion of which tax equity investors receive for both tax and economic motivations. However, these investments are still made primarily for the purpose of receiving tax credits and other tax benefits. For both production tax credit and investment tax credit transactions, these additional cash flows prove problematic in meeting the positive yield and substantially all criteria as it results in investors contributing additional equity and receiving more cash when compared to other tax credit investments. LIHTC transactions often operate on a near-breakeven basis which generally results in less cash distributed to the LIHTC investor.

If the Task Force elects to keep the positive yield criteria without making a change due to scope limitations of this project, we recommend that the Task Force consider a separate project that revisits the positive yield criterion and update it in a manner that would allow more tax credit investments to qualify for the proportional amortization method.

Question 3: Does the Task Force want to clarify at which entity Criterion #2 in paragraph 323-740-25-1(aa)— The investor does not have the ability to exercise significant influence over the operating and financial policies of the limited liability entity—is evaluated in a multitiered structure?

We agree and support the staff recommendation to provide clarification that the significant influence criterion should be evaluated at the project's operating company level. We agree that this is consistent with the original intent of the criterion and that the tax credit investor's involvement in the operating company is what would ultimately call into question whether the investment is primarily for tax credits and other tax benefits.

Question 4: Does the Task Force agree that when applying Criterion #3 in paragraph 323-740-25-1(aaa)— Substantially all of the projected benefits are from tax credits and other tax benefits—the existence of refundable tax credits does not automatically preclude an investor from applying the proportional amortization method?

We believe that the existence of refundable tax credits should not preclude an investor from applying the proportional amortization method. We disagree with the staff's assessment that the refundable credits should only be included in the denominator of the substantially all test. Refundable tax credits are an economic incentive provided by the taxing authority, not cash flows from the operations of the project. Considering them tax benefits is consistent with the overall scope of the project.

Question 5: Does the Task Force want to clarify Criterion #3 in paragraph 323-740-25-1(aaa) to define "projected benefits"?

We agree and support the staff recommendation to clarify the criterion so that it is clear that "projected benefits" refers to total return, including tax credits, other tax benefits, and non-tax-related cash flows. We believe that this is the correct interpretation and the application that is understood and used by preparers and practitioners currently for LIHTC investments. Alternative B, if chosen, would likely lead to a diversity in practice and result in investments being accounted for differently.

Question 6: Does the Task Force want to clarify Criterion #3 in paragraph 323-740-25-1(aaa) to specify whether discounted or undiscounted amounts should be used?

We agree and support the staff recommendation that discounted amounts should be used in applying the substantially all criterion. However, we recommend that the clarification not specify which discount rate should be applied. Rather, we believe that it should be up to the preparer and practitioners to determine an appropriate and supportable discount rate. The use of an appropriate discount rate would more accurately weight cash flows received many years into the future that do not generally impact the tax credit investor's decision to invest.

If the Task Force does not support Alternative A to clarify that discounted amounts should be used, we recommend and support Alternative C to not provide any specific guidance. We believe that preparers and practitioners will develop a practice of applying Criterion #3 for other tax credits similar to the practice developed without any clarification in place for LIHTC investments.

Question 7: Does the Task Force want to require entities to reassess whether a tax credit investment meets the proportional amortization method criteria throughout the life of the investment? If yes, which alternative does the Task Force select?

We agree and support the staff recommendation to only reassess the use of the proportional amortization method upon a change in the nature of the investment or a change in the relationship with the project sponsor. We believe that requiring a reassessment at each reporting date would be overly burdensome and would create unnecessary volatility, impacting tax rates and pre-tax earnings. Requiring reassessment only when there is a fundamental change in the nature of the investment or a change in the relationship with the project sponsor would be the most appropriate approach.

Question 8: What tax credit investments does the Task Force want the disclosure requirements to apply to?

We agree and support the staff recommendation to require the disclosures apply to all investments in tax credit programs.

Question 9: What disclosures does the Task Force want to require for investments in tax credits?

We agree and support the staff recommendation to amend the disclosure requirements and to require certain specific disclosures with some suggested disclosures.

Question 10: Which transition method does the Task Force want to require?

We recommend that the Task Force consider a new alternative that allows the reporting entity the option to use either the prospective, modified prospective or retrospective methods. In Update 2014-01, the Task Force reached a consensus that an entity should apply the guidance on a retrospective basis because qualified affordable housing projects have long terms and would provide comparative information that other methods could not provide. In reaching a consensus, the Task Force observed that information should be readily available in most instances to apply the amendments retrospectively. In practice, preparers found that implementing Update 2014-01 on a retrospective basis was costly and complex to implement.

We believe that a single transition method would not be easily applied if the proportional amortization method is expanded to all credits as the terms of the credits vary widely from LIHTCs. The composition of tax credit investor portfolios of various credits will vary considerably. Therefore, instead of requiring all entities to conform to a single transition method regardless of the composition of their tax credit portfolios, we believe it would benefit the reporting entities and the financial statement users if the reporting entities are allowed to elect a transition method based upon their own portfolio and what would be the most accurate presentation.

We support the staff recommendation to require an entity to disclose the transition methodology selected if the Task Force allows an option for transition.

Question 11: Does the Task Force agree with the staff recommendation for transition disclosures?

> We agree and support the staff recommendation to require the disclosure of a change in accounting as required in paragraphs 250-10-50-1 through 50-2.

ADDITIONAL CONSIDERATIONS

In addition to our recommendations above, we believe that if the proportional amortization method were made available to all tax credits today without changing any of the current five criteria, that only a limited additional amount of tax credit investments would qualify. While this would be an improvement and one that would be welcomed by those that are able to meet the existing criteria, many investors, especially those that invest in multiple credits, would see it as falling short of what is needed to truly level the playing field for all tax credit investments.

Of the five criteria, we believe that the following three will need to be re-examined to determine ways that they can be changed to allow more tax credit investments to be eligible for the proportional amortization method:

- The investor does not have the ability to exercise significant influence over the operating and financial policies of the limited liability entity.

- 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).

- The investor’s projected yield based solely on the cash flows from the tax credits and other tax benefits is positive.

We recommend that the EITF or FASB include the re-examination of these criteria in its current project. If not, we recommend a follow-up project that performs a deeper dive into reviewing the existing criteria so that proportional amortization may be applied for all investments that are made primarily for the purpose of receiving tax credits and other tax benefits.

For example, if the substantially all threshold remains at 90 percent, many transactions, especially RETCs, will fail to meet this criterion and will not be able to use the proportional amortization method, regardless of whether the LIHTC limitation is removed. If changed to a lower percentage, such as 70%-75%, or different measurement, we believe a majority of existing RETC transactions will be able to meet the substantially all criterion. We have previously provided to the FASB staff an analysis of the changes to the substantially all and positive yield criteria that are needed to ensure that the proportional amortization method is available to the most types of tax credit investments.

We believe a principles-based approach is necessary so that the proportional amortization method can be applied to investments in existing tax credits as well as those that will be created in the future. We also recommend that FASB allow early adoption to allow investors to timely reflect the nature of their tax credit investments. We appreciate the opportunity to submit these comments and recommendations. We believe the time and effort the FASB and EITF are spending on this issue is vitally important to the overall impact that tax credit investments can have on communities across the country, many of which are low-income. Thank you for your time and consideration. Please do not hesitate to contact us if you have any questions regarding our comments or if we can be of further assistance.

Yours very truly,
Novogradac & Company LLP

by Brad Elphick

Brad Elphick