

January 30, 2015

Mr. David Bean
Director of Research and Technical Activities
Project No. 19-20E
Government Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Exposure Draft, *Tax Abatement Disclosures*

Dear: Mr. Bean:

As a leading national certified public accounting and consulting firm since 1989, Novogradac & Company LLP has assumed a leadership position in the affordable housing and community development industry. As part of its leadership role, the firm established the low-income housing tax credit (LIHTC) and new markets tax credit (NMTC) Working Groups, coalitions established to provide a platform for LIHTC and NMTC industry participants to work together to resolve technical and administrative LIHTC and NMTC program issues, and create recommendations to make the LIHTC and NMTC Programs even more efficient in delivering the maximum benefit to end users. Our groups include nonprofit and for-profit developers, LIHTC syndicators, NMTC allocatees, nonprofit and for-profit community development entities (CDEs), investors, accountants, lawyers, and other related professionals.

Under the leadership provided by Stacey Stewart and Brad Elphick, the LIHTC and NMTC Working Groups are highly regarded by the U.S. Department of the Treasury, Internal Revenue Service (IRS), Treasury's Community Development Financial Institution (CDFI) Fund, the National Council of State Housing Agencies, and LIHTC allocating agencies, as well as the industry as a whole, for the work they have done to improve the efficiency of the LIHTC and NMTC Programs.

Summary

As the lead coordinator of the LIHTC and NMTC Working Groups, we are providing comments on your Exposure Draft, *Tax Abatement Disclosures* (the "Exposure Draft"). As detailed in our recommendations below, the LIHTC and NMTC Working Groups urge GASB to clarify further that tax credits like LIHTC and NMTC should not be considered tax abatements. The Exposure Draft description and definition of a tax abatement is ambiguous. We don't believe it is appropriate to apply the proposed disclosure requirements to tax credits like LIHTC and NMTC, because it would provide an inaccurate assessment of the total impact on state and local government finances of the activities the LIHTC and NMTC are subsidizing.

Background on the LIHTC

Since its creation in the Tax Reform Act of 1986, the LIHTC has been used to raise equity capital to finance a wide variety of affordable rental housing developments, from low-income family housing to housing for the elderly, people with disabilities, the homeless, veterans, farmworkers, rural populations, and many others.

Each state is provided with \$2.30 per capita in annual LIHTC authority, which is competitively awarded to affordable housing developments. Developers in turn use LIHTC allocation awards to raise equity capital from investors and syndicators to finance the development of affordable rental housing, which is subject to land-use restrictions designed to maintain the property as low-income housing for a minimum of 30 years. The LIHTC serves low-income households earning at or below 60 percent of the area gross median income (AMGI) at rents no more than 30 percent of 60 percent of AMGI.

The LIHTC has been found to have a substantial positive economic impact in the communities in which the properties are located. The National Association of Home Builders found in a 2014 study that in a typical year, the LIHTC supports 95,700 jobs; \$3.5 billion in federal, state, and local tax revenue; and \$9.1 billion in economic income (wages and business income).

The LIHTC is not solely a federal tax credit; many states also have a similar tax credit. Fifteen states (Arkansas, California, Colorado, Connecticut, Georgia, Hawaii, Illinois, Massachusetts, Missouri, New Mexico, New York, North Carolina, North Dakota, Utah, and Vermont) and the District of Columbia have created state LIHTC programs largely based upon the federal LIHTC.

Background on the NMTC

Authorized in the Community Renewal Tax Relief Act of 2000, the NMTC was created to address a persistent problem in economically distressed areas: despite the presence of attractive business opportunities and untapped demand, the cost and scarcity of patient, flexible capital is a substantial impediment to local economic growth. Underserved communities face challenges in securing conventional commercial loans, including: lack of investor familiarity; perceived risk; lingering effects of past discrimination; and difficulty in obtaining formal market data. Whatever the reason, many of the cities, neighborhoods, and rural communities targeted by the NMTC have experienced decades of stagnation and disinvestment that stubbornly persisted even during the 1990s, a period of extraordinary economic growth.

The NMTC attracts capital to low-income communities by providing private investors with a 39 percent federal tax credit for investments made in businesses or economic development projects located in some of the most distressed communities in the nation – census tracts where the individual poverty rate is at least 20 percent or where median family income does not exceed 80 percent of the area median.

Since its creation in 2000, the NMTC has been considered one of the most effective economic and community development programs in the nation, and its effectiveness results in large part to its structure as a tax incentive, instead of an appropriated, government spending program.

A recent NMTC economic impact report using the most robust and comprehensive data collection system of all federal economic development programs found that its investments led to 744,267 jobs in low-income urban and rural communities, including 457,487 construction jobs and 286,781 full-time equivalent jobs in nearly every industry sector of the economy. This impact also was found to produce more federal tax revenue than it costs; for example, in 2012, the NMTC generated \$15.2 billion in economic activity, resulting in \$984 million in federal tax revenue, more than enough to over the estimated \$800 million annual federal cost of the program in 2012. Similarly, the NMTC was found to produce about \$542 million in state and local tax revenue.

Like the LIHTC, the NMTC is not solely a federal tax credit; many states also have a similar tax credit. Fourteen states (Alabama, Arkansas, Florida, Illinois, Indiana, Kentucky, Louisiana, Maine, Mississippi, Nebraska, Nevada, Ohio, Oregon, and Texas) have created state NMTC programs largely based upon the federal NMTC.

Exposure Draft Comments - Tax Abatements vs. Tax Credits

The Exposure Draft would apply new accounting and disclosure standards for government agencies using tax abatements, and it defines tax abatements as a subset of tax expenditures. As such, the Exposure Draft would not apply to all tax expenditures, specifically noting that tax exemptions and tax deductions are not tax abatements.

However, the Exposure Draft does not specifically mention another common form of tax expenditures: tax credits. The LIHTC and NMTC Working Groups urge GASB to clarify whether tax credits like LIHTC and NMTC should be considered as tax abatements for the purposes of the Exposure Draft.

It is unclear whether tax credits like LIHTC and NMTC are captured in the Exposure Draft's proposed definition of the tax abatements. In B4, the Exposure Draft describes the purpose of tax abatements to be:

Tax abatements typically are utilized as part of economic development programs to achieve goals such as (a) increasing the property or other tax base; (b) addressing cost disadvantages; (c) revitalizing distressed local economies; (d) retaining or attracting jobs, companies in particular industries, or a specific company; and (e) increasing the number of persons employed by existing employers.

The NMTC is designed to achieve these purposes, and the LIHTC has a similar economic impact. As such, they would appear to be covered by the Exposure Draft. However, in B8, the Exposure Draft would appear to contradict the earlier conclusion and exclude the LIHTC and NMTC when it excludes from the scope of the statement performance-based incentives:

Certain tax expenditure programs that exhibit the features of a tax abatement—they reduce taxes, encourage beneficial actions by taxpayers, and may be based on an agreement—are, nevertheless, excluded from the scope of this Statement because the government does not commit to abate taxes until *after* the taxpayer has already performed the activity for which the government is providing the tax abatement.

Investors may claim NMTCs over seven years after making their investment and only if their investments remain in compliance. Indeed, any noncompliance could result in as much as 100 percent NMTC recapture. Similarly, after putting their capital at risk during development and lease-up based on a reservation of LIHTCs from the allocating agency, investors may generally claim LIHTCs over 10 years only if the allocating agency awards the LIHTCs to the owner of the project based on the reservation, which happens after construction completion and if property remains in program compliance over the first 15 years of operation. Noncompliance can also result in LIHTC recapture. These performance-based features are key to the success of the LIHTC and NMTC programs.

After making these seemingly conflicting introductory descriptions, the Exposure Draft resolves to define tax abatements in B12 as follows:

Based on the aforementioned considerations, the Board defines a tax abatement (for financial reporting purposes) as resulting from an agreement between one or more governmental entities and a taxpayer in which (a) one or more governmental entities promise to forgo revenues from taxes for which the taxpayer otherwise would have been obligated and (b) the taxpayer promises to take a specific action after the agreement has been entered into that contributes to economic development or otherwise benefits the governments or the citizens of those governments. The scope of this Statement is limited to transactions that meet this definition.

Once again, the proposed definition of tax abatement would appear to apply to tax credits like LIHTC and NMTC. Often, these tax credit programs result from an agreement between state tax allocating agencies and a taxpayer or an entity controlled by the taxpayer. These agreements require the taxpayer to meet certain requirements in order to receive the tax credits.

Because the above guidance and definition are unclear in their applicability to LIHTC and NMTC programs, we believe further clarification should be provided to exclude tax credits like LIHTC and NMTC from the Exposure Draft.

Recommendations

The LIHTC and NMTC Working Groups believe the main motivation behind the Exposure Draft and its disclosure principles is to provide transparency on the impact of tax abatements on the amount of government revenue. The LIHTC and NMTC do not lack transparency as both credits are unambiguous commitments of a specific amount of government resources, competitively allocated and governed by a detailed allocation agreement, and with a clear set of outcomes for low-income households and economically disadvantaged communities. The current definition lacks the specificity required about whether tax credits like LIHTC and NMTC should be considered tax abatements for purposes of these disclosure requirements, which could lead to inconsistencies in financial reporting. The LIHTC and NMTC Working Groups urge GASB to clarify further that tax credits should not be considered tax abatements.

However, if GASB chooses to define tax abatements to include tax credits like LIHTC and NMTC, we would recommend that the disclosure requirements include the expected outcomes resulting from the tax credit investments, including future revenues stimulated, the future expenses reduced, and other community benefits obtained through the foregone revenue. As we noted previously, the LIHTC and NMTC have had a powerful economic impact on low-income communities and excluding these impacts from the disclosure would provide a distorted picture of the overall impact of the tax abatements, as defined by the Exposure Draft. Omitting these impacts from disclosure requirements would negatively impact these tax credit investments, making them appear to be a liability on state and local governments in their financial statements.

We acknowledge that disclosing the full economic impact of tax credit investments will be administratively burdensome and extremely difficult to determine the exact impact amount for financial reporting purposes, which could also be costly to the financial statement preparers. The lack of available information and lack of consistency in presentation may further undermine the intended benefits to users of the financial statements. This provides a further rationale for not including tax credits like LIHTC and NMTC in the tax abatement disclosure requirements in the first place.

Furthermore, the disclosure requirements outlined in the Exposure Draft may be overly specific for some state and local governments and such information may not be readily available to make these disclosures. There also may be abatement agreements executed by others for which they may not be aware. Lastly, it is not entirely clear as to what constitutes an abatement agreement for the purposes of the financial disclosure.

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We appreciate the opportunity to comment on this matter and the consideration taken in making your decision. We commend the GASB in their efforts and conclusions with regard to this very important issue. We would be glad to discuss our comments and address any questions or comments you may have.

Yours very truly,

Novogradac & Company LLP

by 

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by 

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