



June 1, 2017

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2017-28)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

Re: Notice 2017-28 Public Comment Invited on Recommendations for 2017-2018 Priority Guidance Plan

Dear Ladies and Gentlemen:

On behalf of the members of the New Markets Tax Credit (“NMTC”) Working Group, we submit the following comments, considerations and recommendations regarding existing NMTC rules and regulations, which we believe will increase the effectiveness and efficiency of the NMTC program. We have also included an executive summary, which should be read in conjunction with this letter, for your convenience.

The members of the NMTC Working Group are participants in the NMTC industry who work together to help resolve technical NMTC program issues and provide recommendations to make the NMTC program even more efficient in delivering benefits to qualified businesses located in low-income communities around the country. Our group includes over 65 organizations that are allocatees, nonprofit and for-profit community development entities (“CDEs”), consultants, investors, accountants and lawyers.

In previous responses to requests for public comment on the priority guidance plan, we have submitted extensive lists of recommendations that we wanted you to consider. This year, as was the case last year, we have limited our response to the five most important recommendations that members of the NMTC Working Group would like to see implemented. Our comments related to these five priority recommendations have not changed from our previous submission for the 2016-2017 Priority Guidance Plan in a letter dated May 16, 2016. For your convenience, the recommendations have been summarized in the attached Executive Summary and are listed in what we believe to be in the order of highest priority. However, we believe that each recommendation should be considered to generate and sustain the greatest possible community impact. Our comments reflect the work of more than 60 member organizations participating on numerous conference calls and countless drafting sessions over several years. We trust you will find our comments useful and instructive. All of the NMTC Working Group’s previous comments regarding these issues, as well as many others, can be

found on our website (www.nmtcworkinggroup.com) in the Comment Letters section. We would be happy to meet with you to discuss our comments in further detail.

We appreciate the opportunity to comment on ways to further enhance the good being done by the NMTC program, and we also appreciate the level of commitment, dedication and outreach that has been shown and continues to be shown by the CDFI Fund, the Internal Revenue Service (“IRS”) and the Treasury’s Office of Tax Policy and Office of Small Business, Community Development & Housing Policy in implementing and managing the NMTC program. The CDFI Fund, IRS and Treasury have proven to be capable managers of the NMTC program. This is evidenced by the tremendous success the NMTC program has enjoyed since its inception in 2000 by targeting billions of dollars of investments in low-income communities across the country. We applaud the various offices within Treasury that have worked with all those involved in these transactions to ensure that those dollars get into highly distressed communities as efficiently as possible.

Since the program’s inception, the knowledge, understanding and experience among participants in the NMTC program has been continuously rising, as has the demand and competition for the NMTC among participants in the NMTC program, including investors, lenders, CDEs and qualified businesses. The interaction of these and other factors has led to ever-greater efficiencies and effectiveness of the NMTC program in delivering much-needed subsidy to qualified businesses.¹ These factors have also helped direct a greater portion of the NMTC program to the nation’s most distressed low-income communities and to qualified businesses, generating even greater community impacts.

We commend the IRS for requesting items to be included on its annual Guidance Priority Plan. We believe that one of the most effective ways to further improve the efficiency of the NMTC program requires a statutory change – that is to make the credit permanent. Congress has exhibited a trend of granting short-term extensions, which creates uncertainty in the industry. In 2015, Congress passed the Protecting Americans from Tax Hikes (PATH) Act, which extended the NMTC Program at \$3.5 billion annually through 2019; however, uncertainty remains surrounding the NMTC Program regarding its long-term future. Uncertainty in any aspect, especially as it relates to the future of funding for the NMTC program, limits the number of investors and potential CDEs willing to participate, and also limits the level of long-term investment that existing investors and CDEs are willing to make. Willingness by investors to participate in the NMTC program would also be greatly enhanced if a permanent extension of the NMTC included provisions that eliminates the basis reduction and that would allow the NMTC to offset the alternative minimum tax (AMT).² Both provisions would put the NMTC program on par with Low-Income Housing Tax Credits, Historic Tax Credits and certain Renewable Energy Tax Credits, and would increase the demand by investors for the NMTC. An

¹ See “Reports Indicate that NMTC Program Improves with Age,” *Novogradac Journal of Tax Credits*, July 2011, Volume II, Issue VII.

² For further discussion of AMT implications, see §2.16 of *Novogradac & Company New Markets Tax Credit Handbook*, 2011.

increase in demand by investors would lead to an even greater amount of subsidy reaching qualified businesses. Additionally, if the NMTC program were made permanent, CDEs and other NMTC program participants would dedicate more resources to the NMTC program and generate even greater efficiencies. Since the economic downturn, the financing of qualified businesses has become increasingly complicated, requiring industry participants to become progressively more creative in transaction structuring while simultaneously ensuring that as much subsidy from the NMTCs as possible reaches qualified active low-income community businesses (“QALICBs”).

We believe that the following comments, considerations and recommendations concerning existing NMTC rules and regulations, if pursued and adopted, will increase the effectiveness and efficiency of the NMTC program. That said, we believe one regulatory change rises above all others in its potential to positively impact the NMTC program – the manner in which tax credit recapture is determined. By imposing the risk of full recapture, plus interest and penalties, for the full term of the investment for all potential causes of recapture, the NMTC program has created a level of compliance analysis and transaction structuring unrivaled by other tax credit programs. A reduction in tax-credit-recapture risk during the term of the investment would lower overall transaction costs and help facilitate the financing of specific types of businesses that tax credit investors are currently reluctant to make.

The following comments, considerations, and recommendations specifically relate to regulatory changes. Because many of the proposed revisions to the regulations clarify policies that many industry participants have thought were already implicit in the regulations, we believe it would be helpful if the proposed changes, at the option of the taxpayer, could be relied on for periods prior to their effective date. Otherwise, CDEs will receive no additional comfort that transactions structured before the effective date will be allowed to rely on any of the clarifications and guidance provided in the proposed regulations.

We appreciate the opportunity to submit our suggestions for issues that should be included on the 2017-2018 Priority Guidance Plan. We believe that further guidance on these issues is essential to sustain and increase the impact of the NMTC program on low-income communities. With further guidance, we believe that the NMTC can be an even more effective tool in restoring economic growth throughout the country. We commend the Department of Treasury and IRS for their continuing efforts to improve and clarify tax guidance for the NMTC program in order to ensure its continuing success. Thank you in advance for your time and consideration.

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2016-2017 Priority Guidance Plan
June 1, 2017

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 and Company LLP

by 
Brad Elphick

Enclosures

cc: Robert Ibanez

Recommendations for 2017-2018 Priority Guidance Plan

Executive Summary

This executive summary should be read in conjunction with our letter dated May 25, 2017 to the Internal Revenue Service regarding recommendations for the 2017-2018 Priority Guidance Plan. We believe these comments, considerations and recommendations concerning existing NMTC rules and regulations, if pursued and adopted by Treasury, will increase the effectiveness and efficiency of the NMTC program. The comments are organized by priority in which we believe they should be addressed.

1. Redemption Safe Harbor for Partnership CDEs:

- *Timing of distributions* – Treasury Regulation §1.45D-1(e)(3) should be modified to allow CDEs, solely for purposes of determining if a recapture event has occurred, to treat distributions made by the due date (including extensions) of a CDE’s federal income tax return as having been made in the prior taxable year;
- *Distributions made for prior year(s)* – Treasury Regulation §1.45D-1(e)(3) should be modified to allow CDEs taxed as partnerships the ability to make distributions for prior years’ accumulated profits, similar to current regulations allowing corporations to make distributions out of accumulated earnings and profits from all prior taxable years;
- *Catch-up period* – CDEs should be allowed to apply these rules retroactively to allow them to “catch-up” their distributions;
- *Definition of operating income - capital gains* – Treasury Regulation §1.45D-1(e)(3)(iii)(A) should be modified to include capital gains in the calculation of operating income;
- *Special exceptions* – Treasury Regulation §1.45D-1(e)(3) should be modified to define “operating income” to include QLICI loan interest payments without regard to whether the income should be accrued for federal income tax purposes up to the amount of the loan loss reserve held by the CDE. It should also be modified to add back the tax deductions incurred by the qualified active low-income community business or the CDE that do not reduce the CDE’s operating cash flow.
- *Allocation among multiple QEIs* – Guidance is needed under Treasury Regulation §1.45D-1(e)(2)(ii) to clarify the definition of “proceeds of the investment”. Guidance is also needed under Treasury Regulation §1.45D-1(e)(2)(iii) to clarify how distributions from the CDE which constitute a return of capital will be attributed among those QEIs. CDEs should be permitted to elect to use any reasonable method to treat proceeds from a repaid QLICI as applicable to the QEIs made into that CDE. Further, the Regulations should state that the use of a FIFO method, a LIFO method or a pro-rata allocation method should be allowed if consistently applied; and

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Executive Summary

- *C Corporation filing consolidated return* – A C Corporation CDE distributes all of its earnings and profits to its parent and makes a payment to its parent for its allocable share of income taxes. This payment should not be considered a distribution in excess of earnings and profits.
2. **Application of the Rehabilitation Tax Credit Safe Harbor, Rev. Proc. 2014-12, to Transactions which Involve the New Markets Tax Credit** – Clarification should be provided on the application of Sections 4.01 and 4.05(3) from Revenue Procedure 2014-12 to transactions combining HTCs and NMTCs. Without further guidance, these two provisions will continue to have a chilling effect on combining the two tax credits.
 3. **Definition of Control** – Treasury Regulation §1.45D-1(d)(6)(ii)(B) should modify the definition of “control” for purposes of the “reasonable expectation” safe harbor by removing the reference to a value-based test and clarifying voting and management rights that should be considered for control.
 4. **Partnership Allocations (IRC section 704(b))** – Internal Revenue Code §45D and §704(b) provide no specific reference on how the NMTC should be allocated among partners in a partnership. Guidance on this issue would be very helpful, particularly to CDEs seeking to make venture capital investments.
 5. **De Minimis Rule** - Treasury Regulation §1.45D-1(d)(5)(iii)(B) should be modified to state the following: “Certain other trades or businesses. The term ‘qualified business’ does not include any trade or business, (i) from which more than 10 percent of its total gross receipts are derived from, the operations of any private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack or other facility used for gambling, or (ii) consisting of any store the principal business of which is the sale of alcoholic beverages for consumption off premises. In determining whether this 10 percent test is satisfied, only gross receipts from the taxpayer’s trade or business activity that includes operations of any private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack or other facility used for gambling, are taken into account.”