

**THE BUZZ****The Residue of Design**

By Buzz Roberts, Local Initiatives Support Corporation

**W**ill Congress fix the low-income housing tax credit (LIHTC) to attract more investment and keep the pipeline of projects flowing? At this point, the congressional tax committees are preoccupied with health care and energy/climate change, but it's possible there will be an appropriate bill for LIHTC fixes toward the end of the year. (See related story on page 8.)

During the hectic effort a few months ago to assemble what became the American Recovery and Reinvestment Act (Recovery Act), sometimes called the stimulus bill, various LIHTC interests scrambled to propose solutions. Two ideas did become part of the bill: \$2.25 billion in HUD spending through the Tax Credit Assistance Program (TCAP) and the option for states to exchange a portion of the LIHTC allocation cap for cash. These provisions are beginning to jump-start stalled projects. But the Recovery Act did nothing to stimulate investments. Congressional sources say that the lack of consensus among the LIHTC community was a big part of the problem.

So if a legislative vehicle does appear later this year, the LIHTC community must already have agreed on a short list of fixes or it will miss the opportunity. To quote Branch Rickey, the legendary baseball pioneer who invented the farm system and recruited Jackie Robinson to break the color barrier, "Luck is the residue of design." We have to get ready to be lucky.

Suitably chastened, various LIHTC constituencies are working hard to hammer out a limited number of proposals for Congress to consider. Although a lot more work needs to be done, here is the current state of play.

Two ideas that were hot during the Recovery Act debate seem to have cooled off.

On the investment side, the Senate version of the Recovery Act included a plan to accelerate the schedule on which investors could claim the credits. But many investors say that this acceleration presents technical problems that make the idea unattractive. Others worry that if the investment market has limited appetite for tax credits in the near term, accelerating the credits would worsen the supply-demand mismatch by adding more credits over the next few years. Finally, acceleration would be expensive at a time when Congress is seeking to restore budgetary discipline.

A second idea that appears unlikely at this point would be to add money to TCAP. The context of the Recovery Act was unique because it provided one-time spending outside the regular appropriations process. But unless Congress decides to consider another stimulus bill—which at this point seems unlikely—any more TCAP money would come at the expense of other important HUD programs as part of FY 2010 appropriations. This would be highly controversial.

Instead, two other approaches appear to be gathering broad support.

The statutory change that promises to stimulate LIHTC investments the most would be to let investors carry back credits for up to five years if they cannot use them as scheduled. Investors that commit to make new LIHTC investments would get to carry back unusable credits on their current portfolio from their 2009-2011 tax returns for up to five years, instead of the one year now permitted. This would be a good incentive for stimulating new

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investments quickly from experienced LIHTC investors. In addition, future investors would carry back unusable LIHTCs at any point during the course of their investments, also for up to five years. This would reassure any prospective investor that a year or two ago assumed it would always be profitable but may not be so certain of that today.

In addition, the exchange program probably needs to be extended for one additional year. The case here is that the investment market will take time to fully revive, even if the carryback becomes law. It appears that Fannie Mae and Freddie Mac—which together made 40 percent of all LIHTC investments – will not be investing any time soon. Syndicators are beating the bushes to find new investors, but this would take time even if the economy were not in the midst of a deep, housing-driven recession. There are some encouraging signals, but so far few closings with new investors.

Chances for an extension of the exchange appear to be good, especially since Congress has to address other tax

incentives set to expire at the end of year. As a tweak to the exchange program, there is also a growing desire to find a way to apply the exchange concept to help stalled 4 percent LIHTC projects with tax-exempt bond financing, though more work is needed on how it might work.

One other idea is more controversial: to expand greatly the ability of individual investors to use LIHTCs. Under current law, individuals (as well as S corporations and certain closely held C corporations) can only use about \$8,750 in LIHTCs annually, essentially the same as when the LIHTC became law as part of the 1986 Tax Reform Act. At that time, a major driver of tax reform was to eliminate tax shelters that allowed high income taxpayers to avoid paying their fair share of taxes. So one big issue is whether Congress wants to walk back down that road.

Even if this broad tax policy issue can be resolved, a more important question for the LIHTC is whether bringing in individuals would be in the long-term interest of the program. Before the LIHTC, individuals invested in

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ISSN 1940-4980

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low-income housing with very mixed results, even with heavy HUD regulation. Many of these investors did not really understand what they were investing in and had no capacity to evaluate investment proposals or monitor performance. Especially in the early years of the LIHTC, some syndicators tapped individual investors and reported substantial difficulties working with them.

As the LIHTC evolved, corporate investors with substantial real estate finance expertise grew to provide crucial checks and balances in partnership with developers and syndicators. This structure has worked extremely well. Bringing more individual investors into the LIHTC market could be helpful if it could be done without sacrificing the essential discipline of the program. Otherwise, it will be short-sighted and risky. ❖



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*This article first appeared in the July 2009 issue of the Novogradac Journal of Tax Credit Housing.*

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