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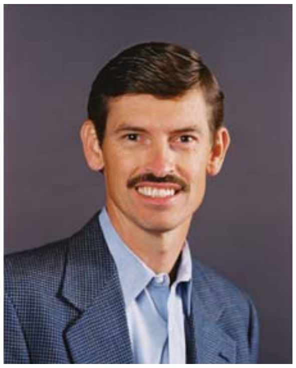
Remaking the Case for Tax Credits

By Michael J. Novogradac, CPA



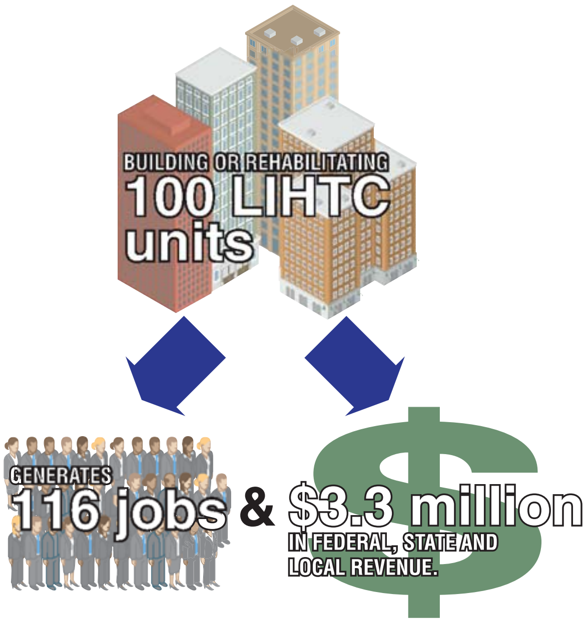
Regular readers of this column are likely aware of the attention being paid in recent months to tax expenditures, tax reform and related topics. The tax extenders legislation that nine months ago was considered by many to be guaranteed to pass, instead stalled for months until it barely squeaked by, finally passing on January 16 during the lame duck session of Congress. Meanwhile, a string of proposals were released by groups such as the President's Economic Recovery Advisory Board and the National Commission on Fiscal Responsibility and Reform that suggested scaling back or eliminating tax credits as part of a fundamental reform the tax code.

And even though there was objection from both sides of the aisle to the prospect of eliminating all tax expenditures, the proposals got people talking. Unfortunately, many of these conversations overlook an important aspect of tax expenditures: the far-reaching social and economic benefits that certain tax credits provide at the national, state and local level.

As Buzz Roberts succinctly put it in the December 2010 installment of The Buzz, "It's about people and neighborhoods and the local economy. And jobs, jobs, jobs." On that note, this month we will examine some of the benefits of low-income housing tax credits, historic tax credits, new markets tax credits and renewable energy tax credits.

Low-Income Housing Tax Credits

Widely regarded as the most successful affordable housing production and preservation program in the nation's history, the LIHTC shines on many levels. In terms of meeting its intended purpose, the LIHTC has financed more than 2 million housing units since 1987. Before the recession, the LIHTC program financed approximately 120,000 units each year.



Research by the National Association of Home Builders (NAHB) in "The Direct Impact of Home Building and Remodeling on the U.S. Economy," in October 2008 indicates that building or rehabilitating 100 LIHTC units generates 116 jobs and more than $3.3 million in federal, state and local revenue. NAHB also reports that until the recent finan-

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cial crisis and resulting slump in the equity market, the LIHTC program was generating about 140,000 jobs annually and $1.5 billion in state and local taxes and other revenues. In fact, according to NAHB's "Housing and Economic Outlook," dated September 16, 2010, even at reduced levels of investment and production, the LIHTC represented half of all multifamily housing starts in 2010.

An example of the substantial and durable benefits that the LIHTC brings to neighborhoods and their residents at a local level can be seen in research released last year by Local Initiatives Support Corporation (LISC) and Enterprise Community Partners (Enterprise). The study, "Affordable Housing for Families and Neighborhoods: the Value of Low Income Housing Tax Credits in New York City," examined both the immediate and long-term impact of 660 developments built throughout the city between 1987 and 2003, specifically on property values within a 1,000-foot impact ring – a common measure that reflects perceptions of neighborhood value – compared with values in similar neighborhoods without LIHTC properties. The research found that throughout New York City, sales prices of homes near LIHTC developments immediately rose relative to more distant properties by six percentage points. This is clear market evidence that LIHTC properties have a favorable neighborhood impact. Moreover, the gain improved to nearly 10 percentage points after five years, confirming that LIHTC projects trigger a chain reaction of revitalization. The positive impact was greater in lower-income neighborhoods—where nearby sales prices immediately rose by 8.5 percentage points relative to more distant properties—but was still significant in higher-income neighborhoods, where the gain was 3.8 percentage points.

Historic Tax Credits

The federal historic tax credit (HTC) provides numerous quantitative and qualitative benefits, including providing affordable housing, fostering downtown economic development and encouraging adaptive reuse. To quote a summary of the HTC provided by the National Park Service, the agency that administers the program, "[Tax credits] are instrumental in preserving the historic places that give cities, towns and rural areas their special character. ... They also generate jobs, enhance property values, and augment revenues for state and local governments through increased property, business and income taxes."

Last year, a first-of-its-kind report showed the extent of benefits that accrue from the investment in HTC rehabilitation projects. The "First Annual Report on the Economic Impact of the Federal Historic Tax Credit," published in March 2010 by Rutgers University, the Historic Tax Credit Coalition and the National Trust Community Investment Corporation, found that almost all sectors of the nation's economy see their payrolls and production increased as a result of HTC development activity.

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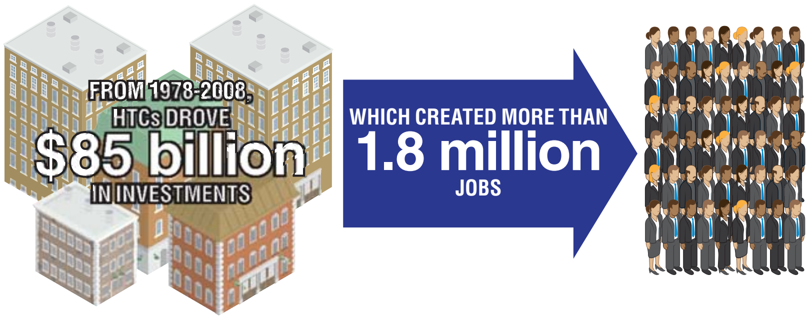

The report indicates that since 1978 the HTC has driven $85 billion in tax credit-aided rehabilitation investment and supported more than 1.8 million jobs. In addition to construction, the HTC creates jobs in the services, manufacturing and retail sectors. In 2008 alone, the report estimates that $3.6 billion for historic rehabilitation expenditures resulted in approximately 58,000 jobs.

The NPS in its "Statistical Report and Analysis for Fiscal Year 2009," says that in 2009, 1,044 applications were approved and each projected created an average of 69 local jobs created per project, equaling an estimated 70,992 total number of local jobs created by the HTC in 2009.

Moreover, these investments result in increased tax revenue for federal, state and local governments. The Rutgers report estimates that since 1978, the total increase in tax revenue is more than $28 billion; in 2008 total tax receipts were increased by approximately $1 billion because of the HTC.

New Markets Tax Credits

The new markets tax credit (NMTC) program in only 10 years has made a significant positive impact on thousands of businesses in hundreds of low-income communities. NMTC investments have supported a wide variety of projects, including, among others, charter schools, health-care facilities, condominiums, timberlands, child-care providers, supermarkets, restaurants, museums, hotels, performing arts centers, pharmacies, convenience stores, manufacturers, processors, distributors, trucking companies, printing companies, waste management companies, energy companies, sporting goods stores, business incubators, office buildings, shopping centers, substance abuse treatment facilities, car dealerships, florists, and recording studios.

In a keynote address at the New Markets Tax Credit Coalition's 9th Annual Conference on December 9, 2010, Community Development Financial Institutions (CDFI) Fund Director Donna Gambrell said that through the first seven allocation rounds, the CDFI Fund has made 495 awards, providing $26 billion in NMTC allocation authority. From fiscal year (FY) 2003 through FY 2010, the organizations receiving these awards have made 2,175 loans and

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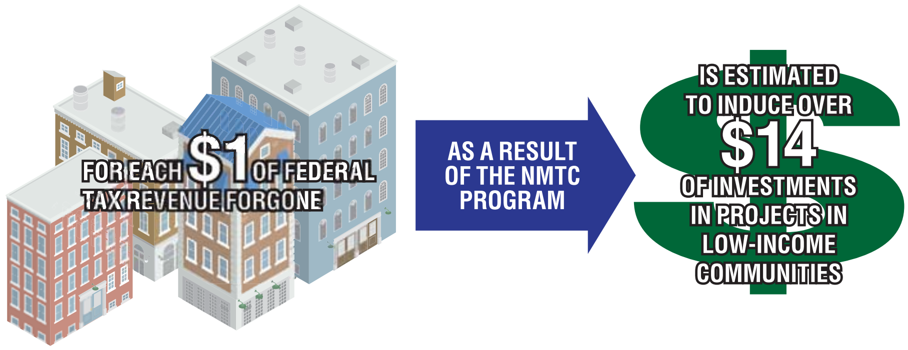


investments, totaling $9.9 billion, to support real estate development and rehabilitation in low-income communities; 2,079 loans investments totaling $5.5 billion to support businesses in low-income communities; and 182 loans and investments totaling $351.4 million to support other community development entities (CDEs).

According to the CDFI Fund's "2009 Performance and Accountability Report," allocatees reported that as of September 30, 2009, 98.9 percent of the loans and investments they provided in FY 2008 had better rates and terms than could be offered in the prevailing market.

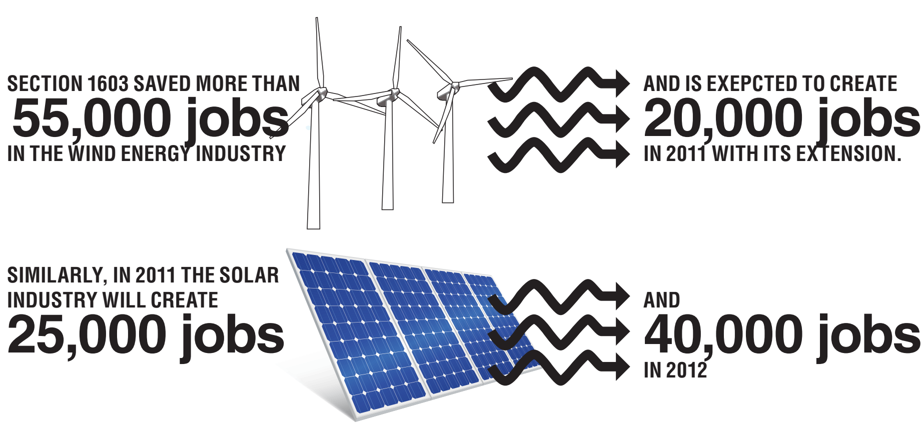
In addition to benefiting businesses and low-income communities, the NMTC benefits the federal, state and local economies. According to the CDFI Fund report, "New Markets Tax Credit Program: Promoting Investment in Distressed Communities," published October 20, 2008: "CDEs reported that 466 of the real estate projects funded with NMTC proceeds created construction jobs, with a median of 80 jobs created; 320 of said real estate projects created jobs at the tenant businesses, with a median of 80 jobs created or maintained; and 233 of the operating businesses created or maintained a median of 16 full-time employees."

Moreover, the report indicates that on average, each $1 of NMTC investment supported total project costs totaling $3.56 and every $1 of federal tax revenue forgone as a result of the NMTC program is estimated to induce more than $14 of investments in projects in low-income communities.

Renewable Energy Tax Credits

Beyond reducing the use of fossil fuels, tax incentives for renewable energy are also being credited with significant job creation. A study by Lawrence Berkeley National Laboratory, "Preliminary Evaluation of the Impact of the Section 1603 Treasury Grant Program on Renewable Energy Deployment in 2009," found that the Section 1603 renewable energy tax credit cash grant exchange program enabled hundreds of renewable energy projects to move forward and saved more than 55,000 jobs in the wind industry alone. In addition, a jobs census recently conducted by the Solar Foundation found that there are more than 93,000 solar workers in the United States, roughly double the number estimated for 2009. The Solar Foundation says that the Section 1603 cash grant was a key factor in this remarkable job growth.

Last month, renewable energy trade groups urged Congress to extend the construction deadline of the Section 1603 program. They contend that with an extension and when compared to what they project in the absence of an extension, the wind industry could create 20,000 new jobs in 2011. Similarly, the solar industry estimates that when compared to a business-as-usual scenario, an extension of the Section 1603 deadline will create 25,000 more jobs next year and 40,000 more new jobs in 2012. Continued federal policy support for geothermal energy, including a Section 1603 extension, would lead to the creation of 11,200 jobs. Likewise, the trade groups say an extension will also lead to the creation of thousands of jobs in the biomass and hydropower sectors.



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Similarly, the Recovery Act's Section 48C manufacturing investment tax credit (MTC) is generating thousands of jobs. The Department of Energy (DOE) announced the recipients of the $2.3 billion in credits in January 2010. Successful applicants for the projects announced under the MTC have said that they will create more than 17,000 jobs, according to "A Manufacturing Blueprint for the Wind Industry," a report released by the American Wind Energy Association, BlueGreen Alliance and United Steelworkers.

Conclusion

It's unclear at this time how tax reform and related efforts will fare in 2011. But in light of last year's increased scrutiny on tax expenditures, including the low-income housing tax credit, new markets tax credit, historic tax credit and renewable energy tax credits, it will be essential that the many benefits of the programs are conveyed to lawmakers at the local, state and federal level.

The economic and social benefits described here are just a summary; inviting policymakers and other stakeholders to the grand opening of a tax credit project—be it new affordable housing for seniors, a new grocery store in a low-income community, a revitalized historic property or a new wind farm or solar array—will go a long way to showing them the total impact that these tax credits have in the communities they represent.

This article first appeared in the January 2011 issue of the Novogradac Journal of Tax Credits.