

The 2017 Tax Cut and Jobs Act LIHTC's and Opportunity Zones

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Overview

- Changes impacting LIHTC projects – the program remains in place but changes impact the economics of tax credit deals.
- Opportunity zones – a new investment vehicle could provide capital to reinvigorate blighted areas.
- State law revision – provides new tax break for year 15 LIHTC properties.

LIHTC

- Reduced corporate tax rates = lower tax credit pricing
 - Top corporate rate reduced from 35% to 21%
 - The credit prices prevailing in 2016 were over \$1.00 and the credit underwriters previously assumed a 25% tax rate moving forward
 - Credit prices have been less than \$.90
- March 2018 budget legislation - Income averaging rules revised to allow more flexibility in tenant mix – allow tenants up to 80% of AMI so long as overall income of tenants does not exceed 60% of AMI

DEPRECIATION

- Depreciation – cost recovery period for residential rental property is reduced from 40 years to 30 years.
- NPO's no longer need to create for profit subsidiaries to qualify for 27.5 year ACR depreciation or forego incentive management fees and non-fixed cashflow waterfall payments, which was the choice. Distributions from the subsidiary to the NPO constituted UBI, so neither option was optimal. * Subject to a caveat (of course).
- Qualified personal property (generally useful life less than 20 years) – can be fully expensed.

BUSINESS INTEREST EXPENSE DEDUCTION

- Limitation on deductions for business interest expense - The limitation is calculated as an amount of business interest equal to the sum of (i) the business interest income of the taxpayer for the taxable year, (ii) 30 percent of the “adjusted taxable income” of the taxpayer for such taxable year (which may not be a negative amount) and (iii) the “floor plan financing interest” of the taxpayer for such taxable year. This is determined at the partnership level.
- Opt out can be possible, but * requires use of 27.5 year alternative cost recovery for depreciation

BEAT

- Base Erosion Anti-Abuse Tax - The BEAT functions as a type of alternative minimum tax that takes account of tax benefits derived from payments to non-United States businesses or entities that are related to the taxpayer.
- A taxpayer making material amounts of payments to foreign affiliates is currently at risk of losing up to 20 percent of the value of its LIHTC and, for taxable years beginning after December 31, 2025, the entire benefit of the LIHTC to such a taxpayer could be lost, as any LIHTC that is lost due to the BEAT cannot be carried forward. Accordingly, the BEAT could significantly and negatively impact the appetite of certain investors in the LIHTC equity market.

OPPORTUNITY ZONES

- The 2017 Tax Cut and Jobs Act included a new Section 1400Z which allows individual and corporate investors to defer recognizing capital gains on the sale of property if the sale proceeds are reinvested in a qualified opportunity fund, which is a partnership or corporation that invests in qualified opportunity zones.
- The governor of each state was granted the authority to designate up to 25% of the state's low-income census tracts as qualified opportunity zones.

Florida Qualified Opportunity Zones

- The Florida Department of Economic Opportunity developed the list of Opportunity Zones for the Governor's approval.
- DEO's economists created a statistical model using census tract data and other economic indicators, such as poverty level, unemployment rates and population density.
- DEO used a proportional method of nominating tracts so that every county would receive at least one census tract nomination.
- Finally, DEO incorporated into the model requests from city and county governments, regional planning councils, nonprofits, investors, developers and others.

Florida Opportunity Zones: only distressed areas

- The tax bill allowed 5% of tract nominations to be tracts that did not meet the low income designation but were contiguous, or next to, other tracts that did meet the criteria.
- Florida chose not to nominate contiguous tracts so that the areas with the most need could be designated.

Investor Benefit: deferral or elimination of gain

- An opportunity zone investment allows an investor to defer or eliminate gain, similar to a 1031 transaction, except this vehicle allows for elimination of gain if an investment is held for at least 10 years.
- Holding periods:
 - Less than five years - zero gain eliminated
 - At least five years - 10% of gain eliminated
 - At least seven years - 15% of gain eliminated
 - At least ten years - 100% of gain eliminated

Opportunity Funds

- Opportunity Funds and their investments are private-sector driven.
- Once an opportunity zone is certified by the U.S. Department of the Treasury, local communities will have the ability to promote their Opportunity Zones to qualified Opportunity Funds in order to secure investments.
- Opportunity Funds will be designated through the U.S. Department of the Treasury and the Internal Revenue Service as eligible based on rulemaking that has not yet taken place.
- The Opportunity Funds must invest 90 percent of their fund in Opportunity Zones to receive the tax benefits.

Opportunity Zone Investment Property

- Opportunity Funds invest in Opportunity Zone Property, which are defined as:
 - Qualified opportunity zone stock – any stock in a domestic corporation
 - Qualified opportunity zone partnership interest – any capital or profits interest in a domestic partnership
 - Qualified opportunity zone business property – tangible property used in a trade or business of the qualified opportunity fund that substantially improves the property

Implementation

- In addition to providing guidance on the processes for submitting Opportunity Zone designations and certifying Opportunity Funds, the Treasury must adopt regulations to implement the law.
- The process generally goes as follows:
 - Treasury will propose a structure for implementing the new rule, after which it will issue a notice of proposed rulemaking and will request public comments on the proposal.
 - The comment period typically lasts from 30 to 60 days. Upon reviewing the comments and making any necessary changes to the rule, Treasury will issue a final rule that formalizes the program.

FLORIDA LAW – REAL ESTATE TAX BREAK FOR YEAR 15 LIHTC PROJECTS

- Amendment to F.S. Section 196.1978 allows for 50% reduction in property taxes for LIHTC projects at year 15
- Helps preserve affordable housing stock