Bloomberg BNA

Daily Tax Report®

New Rules for New York Historic Credits Create Opportunities for Investors

BY DAVID BURTON

New York Gov. Andrew Cuomo (D) March 29 signed bill S2609D-2013 to implement New York's fiscal plan for the 2013-2014 fiscal year; the fiscal plan amends the New York historic tax credit rules.

First, the New York historic tax credit is made refundable for properties placed in service in 2015 or later.[1]

Second, the New York property, in addition to being listed in a specified historic register,[2] must be in a census tract with a median family income at or below the median family income for the state.[3]

The refundability feature starting in 2015 reduces challenges currently encountered in finding tax equity investors for New York transactions.

The new law clarifies that the census tract median family income is determined by the most recent estimate from the American Community Survey published by the U.S. Census Bureau. Further, under prior law the census tract did not matter if the building was in a ''targeted residence area'' within the meaning of Internal Revenue Code Section 143(j), but S2609D-2013 eliminated that flexibility.

The refundability amendment was supported by political leaders from Buffalo, N.Y. Buffalo has a lower cost of living than many downstate communities, so much of the Buffalo area will satisfy the census average family income requirement (nonetheless, the property must be certified as historic).

Overview of New York's Historic Tax Credit Rules

The New York historic tax credit mimics the federal rehabilitation tax credit of Section 47 of the Internal Revenue Code. Both are 20 percent of ''qualified rehabilitation expenditures''; however, the New York tax credit is capped at $5 million per property. Starting in 2020, the New York tax credit declines to 30 percent of the federal tax credit.[4]

Currently, the New York historic tax credit may be carried forward 15 years,[5] but the carryforward will be unlikely to be used for credits arising for buildings placed in service in 2015 or later due to the refundability option. The federal credit may be carried back one year and forward 20 years.[6]

The New York tax credit rules require the same taxpayer that claims the federal credit to claim the New York credit.[7] This requirement makes finding tax equity investors for New York transactions challenging as such an investor, typically a financial institution, has to have both federal and New York tax appetite. That challenge is eliminated by the refundability feature starting in 2015; however, even then developers of historic buildings will still need to find tax equity investors with appetite for the federal credit, and the New York credit (even though refundable) must follow the allocation of the federal credit. Thus, a developer cannot claim the refundable New York credit for itself while allocating the federal credit to a tax equity investor.

The federal credit (but not the New York credit) results in a dollar for dollar reduction in tax basis for federal income tax purposes.[8] (This is in contrast to federal

[1] Specifically, taxpayers without sufficient tax liability in New York to apply the tax credit to can obtain a cash payment from the state equal to the amount of the credit.

[2] The relevant historic registers are specified in Internal Revenue Code 47(c)(3).

[3] N.Y. Tax Law Sections 210(40)(5) (corporate franchise tax), 1456(u)(5) (bank franchise tax), 1511(y)(5) (insurance franchise tax).

[4] N.Y. Tax Law Sections 210(40)(1)(A) (corporate franchise tax), 1456(u)(1)(A) (bank franchise tax), 1511(y)(1)(A) (insurance franchise tax).

[5] N.Y. Tax Law Sections 210(12)(e) (corporate franchise tax), 1456(i)(5) (bank franchise tax), 1511(q)(4) (insurance franchise tax).

[6] Although the federal tax credit is not refundable, it may be carried back one year and carried forward 20 years. I.R.C. Section 39(a).

[7] TSB-M-10(2)(C), (3)I at 2 (N.Y. Dep't of Tax & Fin. Feb. 3, 2010).

[8] I.R.C. Section 50(c)(1).

David Burton is a partner in the tax practice at Akin Gump Strauss Hauer & Feld LLP. He serves as editor of the firm's blog, Tax Equity Telegraph (http://www.taxequitytelegraph.com/).

energy tax credits that reduce tax basis by only half of the amount of the energy tax credit.[9]) Similarly, the New York tax credit (but not the federal credit) reduces tax basis for New York tax purposes.

In the first five years after the rehabilitated building is placed in service, a transfer of the building[10] or of more than a one-third interest in a partnership[11] that owns the building results in ''recapture'' of the credit. Recapture means that the taxpayer must include the amount of the credit in taxable income. The amount that must be included declines by 20 percent each year after the placed in service date.[12] The New York rule parallels the federal rule.[13] Claiming a refund, rather than a New York tax credit, does not alter the application of the recapture rule.

Flexibility, Premium Returns

In the long term, the New York historic tax credit rules will provide developers with greater flexibility in selecting investors and may result in lower after-tax returns for investors.

In the short term, the New York tax credit rules will enable corporations with tax appetite in New York to demand premium returns for historic tax credit investments.

Tax executives who project New York and federal tax appetite in 2013 or 2014 should consider investing in properties eligible for the New York tax credit to capture the premium returns that are available in the present market that dwarf that available in other tax-advantaged investments.

[9] I.R.C. Section 50(c)(3).

[10] I.R.C. Section 50(a)(1). There are different rules for lease transactions. See Treasury Regulations Section 1.47-2(b).

[11] Treas. Reg. Section 1.47-6.

[12] I.R.C. Section 50(a)(1).

[13] N.Y. Tax Law Sections 210(40)(3) (corporate franchise tax), 1456 (u)(3) (bank franchise tax), 1512(y)(3) (insurance franchise tax).

  DTR ISSN 0092-6884