Linda Lingle
GOVERNOR

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IN REPLY REFER TO

Statement of
Orlando "Dan" Davidson
Hawaii Housing Finance and Development Corporation
Before the

HOUSE COMMITTEE ON FINANCE

February 26, 2008, 10:00 a.m.
Room 308, State Capitol

In consideration of
H.B. 3059
RELATING TO LOW-INCOME HOUSING TAX CREDITS.

The HHFDC strongly supports H.B. 3059, which reduces the period over which state low-income housing tax credits are taken from 10 years to 5 years. The low income housing tax credit (LIHTC) program promotes the development and rehabilitation of low-income rental housing by providing equity to developers of eligible affordable housing projects. The program is a powerful financing tool for affordable rental housing development, especially when leveraged with state rental housing trust funds.

The LIHTCs provide a dollar-for-dollar credit against annual income tax liability over a 10 year period. Developers typically sell the tax credits to tax payers/investors to raise equity for the development of a rental housing project. Unfortunately, the sale of State LIHTCs generates less than half of the "equity" than that of the federal LIHTC, or approximately \$0.35 to \$0.50 for every \$1.00 of state credit. By shortening the time period over which the State credits can be taken (i.e., from 10 years to 5 years), the value of the State LIHTC could be enhanced and more equity could be generated for the development of rental housing.

The HHFDC agreed to an amendment to the Senate companion measure, S.B. 2981, S.D. 2, that would modify the applicable percentage of the qualified basis of each qualified low-income building that is placed in service beginning on January 1, 2009. This amendment makes the state housing credit one hundred per cent of the applicable percentage of the qualified basis of each building located in Hawaii; provided that the applicable percentage shall be calculated as provided in section 42(b) of the Internal Revenue Code. The HHFDC respectfully requests that the Committee consider adopting this amendment, with a minor technical amendment thereto, because S.B. 2981, S.D. 2 has not yet been scheduled for hearing by the Senate Committee on Ways and Means. The proposed H.D. 1 is attached for your consideration.

Thank you for the opportunity to testify.

A BILL FOR AN ACT

RELATING TO LOW-INCOME HOUSING TAX CREDITS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. Section 235-110.8, Hawaii Revised Statutes, is amended to read as follows:

"**§235-110.8 Low-income housing tax credit.** (a) Section 42 (with respect to low-income housing tax credit) of the Internal Revenue Code shall be operative for the purposes of this chapter as provided in this section[~~.~~], except as provided in subsections (h) and (i).

(b) Each taxpayer subject to the tax imposed by this chapter, who has filed [~~[~~]a[~~]~~] net income tax return for a taxable year may claim a low-income housing tax credit against the taxpayer's net income tax liability. The amount of the credit shall be deductible from the taxpayer's net income tax liability, if any, imposed by this chapter for the taxable year in which the credit is properly claimed on a timely basis. A credit under this section may be claimed whether or not the taxpayer claims a federal low-income housing tax credit pursuant to section 42 of the Internal Revenue Code.

(c) The low-income housing tax credit shall be fifty per cent of the applicable percentage of the qualified basis of each building located in Hawaii. The applicable percentage shall be calculated as provided in section 42(b) of the Internal Revenue Code.

(d) For the purposes of this section, the determination of:

(1) Qualified basis and qualified low-income building shall be made under section 42(c);

(2) Eligible basis shall be made under section 42(d);

(3) Qualified low-income housing project shall be made under section 42(g);

(4) Recapture of credit shall be made under section 42(j), except that the tax for the taxable year shall be increased under section 42(j)(1) only with respect to credits that were used to reduce state income taxes;

(5) Application of at-risk rules shall be made under section 42(k);

of the Internal Revenue Code.

(e) As provided in section 42(e), rehabilitation expenditures shall be treated as separate new building and their treatment under this section shall be the same as in section 42(e). The definitions and special rules relating to credit period in section 42(f) and the definitions and special rules in section 42(i) shall be operative for the purposes of this section.

(f) The state housing credit ceiling under section 42(h) shall be zero for the calendar year immediately following the expiration of the federal low-income housing tax credit program and for any calendar year thereafter, except for the carryover of any credit ceiling amount for certain projects in progress which, at the time of the federal expiration, meet the requirements of section 42.

(g) The credit allowed under this section shall be claimed against net income tax liability for the taxable year. For the purpose of deducting this tax credit, net income tax liability means net income tax liability reduced by all other credits allowed the taxpayer under this chapter.

A tax credit under this section which exceeds the taxpayer's income tax liability may be used as a credit against the taxpayer's income tax liability in subsequent years until exhausted. All claims for a tax credit under this section must be filed on or before the end of the twelfth month following the close of the taxable year for which the credit may be claimed. Failure to properly and timely claim the credit shall constitute a waiver of the right to claim the credit. A taxpayer may claim a credit under this section only if the building or project is a qualified low-income housing building or a qualified low-income housing project under section 42 of the Internal Revenue Code.

Section 469 (with respect to passive activity losses and credits limited) of the Internal Revenue Code shall be applied in claiming the credit under this section.

(h) In the case of any qualified low-income housing project placed in service beginning on January 1, 2009, section 42(b)(2)(B) of the Internal Revenue Code shall be modified as follows: the percentages prescribed by the Secretary for any month shall be percentages which will yield over a ten-year period amounts of credit under subsection (a) which have present value equal to:

(1) Seventy per cent of the qualified basis of a building described in section 42(c)(1)(A) (with respect to low-income housing credit) of the Internal Revenue Code; and

(2) Thirty per cent of the qualified basis of a building described in section 42(c)(1)(B) (with respect to low-income housing credit) of the Internal Revenue Code.

For the purposes of this subsection the state housing credit shall be one hundred per cent of the applicable percentage of the qualified basis of each building located in Hawaii; provided that the applicable percentage shall be calculated as provided in section 42(b) of the Internal Revenue Code.

(i) In the case of any qualified low-income housing project placed in service beginning on January 1, 2009, section 42(f)(1) of the Internal Revenue Code shall be modified as follows: the term "credit period" means, with respect to any building, the period of five taxable years beginning with:

(1) The taxable year in which the building is placed in service; or

(2) At the election of the taxpayer, the succeeding taxable year;

provided that the building is a qualified low-income building as of the close of the first year of such period. The election under paragraph (2), once made, shall be irrevocable.

[~~(h)~~] (j) The director of taxation may adopt any rules under chapter 91 and forms necessary to carry out this section."

SECTION 2. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 3. This Act shall take effect on January 1, 2009.

LINDA LINGLE
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HOUSE COMMITTEE ON FINANCE

TESTIMONY REGARDING HB 3059 RELATING TO LOW-INCOME HOUSING CREDITS

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: FEBRUARY 26, 2008
TIME: 10:00AM
ROOM: 308

This legislation modifies Hawaii's conformity to the federal Low-Income Housing Tax Credit provided by Section 42 of the Internal Revenue Code, by reducing the number of years over which the credit may be claimed.

The House Committee on Human Services & Housing passed this measure unamended.

The Department **strongly supports** this Lingle-Aiona Administration bill and encourages the Committee to pass this measure.

I. THE DEPARTMENT DEFERS TO THE HOUSING AGENCIES ON THE MERITS.

The Department defers to the various executive housing agencies on the merits of this bill in general. Hawaii is currently facing an affordable housing crisis. It will take meaningful initiatives in order to eliminate the shortage of affordable housing suitable for Hawaii residents.

II. THE ISSUE OF AFFORDABLE HOUSING IS IMPORTANT AND MAKING HAWAII'S CREDIT MORE ATTRACTIVE IS CRITICAL.

The Department recognizes that affordable housing is an important issue. To properly eliminate the affordable housing crisis, sufficient incentives must also be available in order to leverage public-private partnerships to construct additional housing Hawaii. Through the use of the Low-Income Housing Tax Credit, partnerships between the state and private developers are leveraged through attractive tax incentives that subsidize investments in projects.

This legislation is a positive solution. This legislation effectively reduces the horizon of years over which the Low-Income Housing Tax Credit must be claimed. Currently, the Hawaii credit must be claimed over a 10-year period. This bill reduces that period to 5 years. The reduction in the claim period makes the credit far more attractive to investors. The reduction also makes the credit more useful to project partnerships because cash from the government is released in a much shorter time.

III. REVENUE ESTIMATE

This legislation will result in the following revenue loss:

- FY2009 (loss): none
- FY2010 (loss): $1.25M
- FY2011 (loss): $2.50M
- FY2012 (loss): $3.13M
- FY2013 (loss): $3.25M

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L E G I S L A T I V E

TAXBILLSERVICE

126 Queen Street, Suite 304 TAX FOUNDATION OF HAWAII Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Low-income housing credit

BILL NUMBER: SB 2981; HB 3059 (Identical)
2/12 HSH 2/12 HSH 2/26 FIN

INTRODUCED BY: SB by Hanabusa by request; HB by Say by request

BRIEF SUMMARY: Amends HRS section 235-110.8 to provide that a low-income housing project placed in service beginning on January 1, 2009, pursuant IRC section 42(b)(2)(B) shall be eligible for the low-income housing credit taken over a five-year period instead of the current 10-year period.

EFFECTIVE DATE: January 1, 2009

STAFF COMMENTS: This is an administration measure submitted by the department of business economic development and tourism BED-06(08). The legislature by Act 216, SLH 1988, adopted the federal low-income rental housing credit which was part of the Tax Reform Act of 1986. The credit was enacted to offset the repeal of tax shelters and other incentives to build rental housing under prior law, such as accelerated depreciation, capital gains preference, certain tax-exempt bonds, etc., and to specifically target low-income rentals.

The federal credit is a 70% present value credit for qualified new construction and rehabilitation expenditures which are not federally subsidized, and 30% for those which are federally subsidized. While the existing state credit allows for a credit of 50% of the "applicable percentage of the qualified basis" allowed under federal law taken over a period of 10 years, the proposed measure would shorten it to five years. The justification sheet submitted with this measure states that by shortening the time period over which the low-income housing tax credits are taken would increase the present value of the credits when sold to investors. This would, the justification argues, provide a more attractive alternative financing incentive to potential developers of affordable rental housing.

While this is just one incentive to encourage developers to build affordable housing, consideration should be given to a number of strategies including the debt financing, partnerships with financial institutions who could then turn around and sell the credits, and the use of federal debt financing.

Digested 2/01/08

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February 26, 2008

The Honorable Marcus R. Oshiro, Chair
House Committee on Finance
State Capitol, Room 308
Honolulu, Hawaii 96813

RE: H.B. 3059, Relating to Low-Income Housing Tax Credits
Hearing Date: February 26, 2008 @ 10:00 a.m., Room 308

On behalf of our 10,000 members in Hawaii, the Hawaii Association of REALTORS® (HAR) **supports H.B. 3059,** which reduces the period over which state low-income housing tax credits are taken from 10 years to 5 years.

We believe Smart Growth is our road map to sustaining and enhancing the quality of life in our communities and we believe that this bill aligns with our core principle of ***providing housing opportunities.***

HAR has historically supported mechanisms to help increase the supply of low and moderate income affordable housing such as the Rental Housing Trust Fund Program which can help integrate the use of mixed-income and mixed-use projects, special purpose revenue bonds, low-interest loans, block grants, low-income housing tax credit programs and deferred loan programs to provide rental housing opportunities.

Amending the period over which state low-income housing tax credits are taken from ten years to five years would increase the present value of the credits when sold to investors, and provide a more attractive financing incentive to potential developers of affordable rental housing.

HAR looks forward to working with our state lawmakers in building better communities by supporting quality growth, seeking sustainable economies and housing opportunities, embracing the cultural and environmental qualities we cherish, and protecting the rights of property owners.

Mahalo for the opportunity to testify.

Sincerely,

Craig Hirai, Member
Subcommittee on Taxation and Finance
HAR Government Affairs Committee