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Historic rehabilitation tax credit

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Developers whose projects utilize historic rehabilitation tax credits have high hopes that the Internal Revenue Service will soon introduce guidance that will provide comfort to their investors. At a recent tax practitioners' conference, an IRS representative indicated that the IRS is drafting a revenue procedure that will provide a safe harbor for investors in historic rehabilitation tax credit projects. This could be very good news for developers and investors who have been troubled by a 2012 Third Circuit court opinion that threw some uncertainty into the world of historic rehabilitation tax credits.

In August 2012, the United States Court of Appeals for the Third Circuit ruled in *Historic Boardwalk Hall v. Commissioner* that an investor in a syndicated partnership sharing in federal historic tax credits was not a bona fide partner. To be a bona fide partner, the investor was required to share in both the upside benefits and the downside risks of loss.

The Court determined that the investor in question lacked any meaningful downside risk for several reasons. First, the investor joined the partnership after the partnership had already committed sufficient funding to pay the costs of the project. Second, the investor did not make its capital contribution to the partnership until after the historic credits had been certified and were available to the investor. Third, the Court focused on the fact that the partnership and the New Jersey Sports and Exhibition Authority had given guarantees which protected the investor from loss arising from failure to complete the construction, environmental liabilities and any loss or reduction of the tax credits. Finally, a letter of credit secured the payment of the investor's preferred return and a loan made to the partnership by the investor.

In May of this year, the United States Supreme Court declined to review the Third Circuit's opinion. This created even more uncertainty in the historic tax credit industry and dampened investor interest in historic tax credit projects. Recognizing the damage that could be caused if the Third Circuit opinion was the last word on this issue, the IRS is now working to draft a revenue procedure which should provide comfort to developers and investors. This column will provide you with an update on that IRS guidance when it becomes available.

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