

**LETTER OPINION
2012-L-04**

May 1, 2012

Mr. Birch P. Burdick
Cass County State's Attorney
PO Box 2806
Fargo, ND 58108-2806

Dear Mr. Burdick:

Thank you for your letter requesting my opinion whether taxing authorities should consider tax credits or rent restrictions when assessing a property built using federal low income housing tax credits. Based on the following analysis, it is my opinion that taxing authorities may consider the effect, if any, of the tax credits and rent restrictions on a property's value when assessing a property built using federal low income housing tax credits, along with other evidence relevant to determine the true and full value of the property.

ANALYSIS

The federal Low Income Housing Tax Credits Program (LIHTC) is found in section 42 of the Internal Revenue Code,¹ and

was enacted by Congress in 1986 to provide the private market with an incentive to invest in affordable rental housing. Federal housing tax credits are awarded to developers of qualified projects. Developers then sell these credits to investors to raise capital (or equity) for their projects, which reduces the debt that the developer would otherwise have to borrow. Because the debt is lower, a tax credit property can in turn offer lower, more affordable rents.

Provided the property maintains compliance with the program requirements, investors receive a dollar-for-dollar credit against their Federal tax liability

¹ 26 U.S.C. § 42.

each year over a period of 10 years. The amount of the annual credit is based on the amount invested in the affordable housing.²

In exchange for the tax credits, the LIHTC program requires an affordability period of 30 years.³ During this time frame, a certain percentage of rental units must be restricted to an affordable level of rent and occupied by households with incomes at or below certain percentages of area median income that is adjusted for household size.⁴

The LIHTC program includes provisions addressing a change in the property's ownership or operations:

If the original owner or its successor ceases to operate the development as low-income housing under the terms of the regulatory agreement, the value of the tax credits is reduced or entirely recaptured. IRC [Internal Revenue Code] § 42(j). On the other hand, as long as the subsequent owner continues to operate under the regulatory agreement, it is entitled to receive the remaining tax credits. IRC § 42(d)(7)(A).⁵

The issue facing taxing authorities when determining the true and full value of a property in the LIHTC program is whether, and if so, how, to consider both the tax credits and the rent restrictions under the program. Some states have adopted specific legislation addressing how to value property subject to the LIHTC program.⁶ North Dakota, however, does not have such a law, and must rely on the statutory definition of true and full value.

In North Dakota, all real property that is subject to taxation is assessed a tax based on the property's "true and full value."⁷ The phrase "true and full value" means:

² U.S. Department of Housing and Urban Development, <http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/work.cfm> (last visited Apr. 30, 2012).

³ See <http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/eligibility.cfm> (last visited Apr. 30, 2012). This consists of a 15 year compliance period under 26 U.S.C. § 42(i)(1), and a 15 year extended use period under 26 U.S.C. § 42(h)(6)(D)(ii). The extended use period could be longer if there is a longer commitment in the agreement with the owner. See 26 U.S.C. § 42(h)(6)(D)(ii)(I).

⁴ See www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/eligibility.cfm (last visited Apr. 30, 2012).

⁵ *Huron Ridge LP v. Ypsilanti Twp.*, 737 N.W.2d 187, 188, n.1 (Mich. Ct. App. 2007).

⁶ For example, See Neb. Rev. Stat. § 77-1333.

⁷ N.D.C.C. ch. 57-02. See *Trollwood Vill. Ltd. P'ship v. Cass Cnty. Bd. of Cnty. Comm'rs*, 557 N.W.2d 732, 734-5 (N.D. 1996), for a concise description of the process of valuing a property and arriving at the final tax levy.

the value determined by considering the earning or productive capacity, if any, the market value, if any, and all other matters that affect the actual value of the property to be assessed.⁸

The North Dakota Supreme Court has indicated that there are three basic approaches to the valuation of property:

- (1) comparable sales, sometimes referred to as the market or market value or market data approach;
- (2) the cost (or original-cost or reproduction cost-less-depreciation) approach; and
- (3) the income (or economic) approach.⁹

Interpreting this definition, the North Dakota Supreme Court has indicated that all relevant matters that affect the value of a property should be considered.¹⁰ For instance, the Court has determined that multiple elements from each valuation approach may be used to determine true and full value of property.¹¹ Further, the Supreme Court has held that “[W]eighing factual material for tax purposes is the responsibility of county commissioners, not the courts.”¹² Accordingly, a reviewing court would intervene only “when there is such an absence of evidence or reason as to amount to arbitrary, capricious or unreasonable action [by the local governing body].”¹³ In other words, local governing bodies may

⁸ N.D.C.C. § 57-02-01(15) (emphasis added). An additional part of the definition of “true and full value,” which is not relevant here, relates to agricultural property. See N.D.C.C. § 57-02-01(15).

⁹ Ulvedal v. Bd. of Cnty. Comm’rs of Grand Forks Cnty., 434 N.W.2d 707, 710, n.3 (N.D. 1989) (citing 7 Nichols on Eminent Domain § 4.04[3] “The Appraisal Report” (1987)) (emphasis added).

¹⁰ See Ulvedal, 434 N.W.2d at 710-11 (board considered income, square footage compared with other buildings, and cost-depreciation), Trollwood Village, 557 N.W.2d at 737 (assessors considered income history and earning capacity, and market value), and American Crystal Sugar Co. v. Traill Cnty. Bd. of Comm’rs, 714 N.W.2d at 857-58 (board considered “trended cost” method, market sales method, and income method).

¹¹ See n.10.

¹² Ulvedal, 434 N.W.2d at 710.

¹³ Ulvedal, 434 N.W.2d at 709.

consider the strengths and weaknesses of all available evidence in order to select an amount within the boundaries of the evidence.¹⁴

North Dakota does not have any reported court cases directly addressing how low income housing tax credits affect the valuation of property, but other states' courts have considered the issue. As pointed out in your letter, some states appear to consider rent restrictions when valuing the property, but other states do not consider the tax credit for a variety of reasons, such as that the credits are personal property rather than real property, or that they may be recaptured if a future owner does not maintain the restricted rents during the period of affordability.¹⁵

For example, the Illinois Supreme Court noted that “[a] valuation approach which considers the subsidy income, but does not consider the negative aspects of a subsidy agreement upon the earning capacity of subsidized property, would be inappropriate. The taxing authority must weigh both the positive and the negative aspects of the subsidy agreement and adjust the actual income figure to accurately reflect the true earning capacity of the property in question.”¹⁶ Similarly, the Georgia Court of Appeals held that “the tax credits go hand in hand with restrictive covenants that require the property to charge below-market rent. . . . If viewed in isolation, the rental restrictions would artificially depress the value of the property for tax valuation purposes.”¹⁷ In an Indiana case, the taxing authority was upheld when it deemed that the federal tax credits would make up for any loss of rental income, and thus the rental restrictions did not cause an apartment complex to lose value.¹⁸ And, as pointed out in your letter, South Dakota likewise requires consideration of both the restricted rental rates and the tax credits for valuing properties

¹⁴ Dakota Nw. Assocs. Ltd. P’ship v. Burleigh Cnty. Bd. of Cnty. Comm’rs, 616 N.W.2d 349, 352 (N.D. 2000). Further, “[t]here is an element of subjectivity in every opinion about value.” Ulvedal, 434 N.W.2d at 710. “It is apparent that appraisal of property for tax purposes is far from an exact science but the method of appraisal should bear some relationship to the realities of the situation.” Midwest Processing Co. v. McHenry Cnty., 467 N.W.2d 895, 901-902 (N.D. 1991) (VandeWalle, J., concurring specially).

¹⁵ See Bayridge Assocs. Ltd. P’ship v. Dep’t of Revenue, 892 P.2d 1002 (Or. 1995), Cascade Court Ltd. P’ship v. Noble, 20 P.3d 997 (Wash. Ct. App. 2001), Maryville Props., L.P. v. Nelson, 83 S.W.3d 608 (Mo. Ct. App. 2002), Cottonwood Affordable Housing v. Yavapai Cnty., 72 P.3d 357 (Ariz. Tax Ct. 2003).

¹⁶ Kankakee Cnty. Bd. of Review v. Prop. Tax Appeal Bd., 544 N.E.2d 762, 769 (Ill. 1989) (the court was considering a subsidized rent program that operates similarly to the LIHTC program).

¹⁷ Pine Pointe Housing, L.P. v. Lowndes Cnty. Bd. of Tax Assessors, 561 S.E.2d 860, 863 (Ga. Ct. App. 2002).

¹⁸ Pedcor Investments - 1990-XIII, L.P. v. State Bd. of Tax Comm’rs, 715 N.E.2d 432, 439 (Ind. T. C. 1999).

subject to the LIHTC Program.¹⁹ These cases illustrate a consistency with North Dakota law, namely, that all factors are to be considered when determining the value of a property.

Therefore, it is my opinion that taxing authorities may consider the effect, if any, of both tax credits and rent restrictions on a property's value when assessing a property built using federal low income housing tax credits.²⁰ The amount of weight a taxing authority gives to the tax credits and rent restrictions will depend on the particular circumstances and facts relevant to the particular property being considered.²¹

Sincerely,

Wayne Stenehjem
Attorney General

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This opinion is issued pursuant to N.D.C.C. § 54-12-01. It governs the actions of public officials until such time as the question presented is decided by the courts.²²

¹⁹ Town Square Ltd. P'ship v. Clay Cnty. Bd. of Equalization, 704 N.W.2d 896, 902-03 (S.D. 2005).

²⁰ Both the benefit of tax credits and the burden of rent restrictions may be relevant when examining the property's value under the market value approach and the income approach, but would not be relevant when examining the property's value under the cost-less-depreciation approach.

²¹ This opinion addresses whether the effects of the LIHTC program should be considered when appraising property for tax purposes. There are standards of appraisal practices which are applicable to all licensed appraisers. Trollwood Village, 557 N.W.2d at 737. These standards supply the means by which this opinion should be applied when performing an appraisal.

²² See State ex rel. Johnson v. Baker, 21 N.W.2d 355 (N.D. 1946).