



Newsletter

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Georgia Affordable Housing Tax Credit Program Available to Surplus Lines Brokers

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Many Georgia surplus lines brokers may not be aware of the option to offset Georgia's surplus lines tax through Georgia low-income housing tax credits ("Georgia Credits"). The Georgia Credits were originally proposed to offset state income tax but were expanded in 2001 to also allow credit against surplus lines tax, premium tax and premium taxes paid by risk retention groups.

Overview

Federal low-income housing tax credits are government incentives authorized under Code Section 42 of the Internal Revenue Code ("Federal Credits"). There is a parallel state incentive in Georgia under Code Section 33-1-18 of the Official Code of Georgia Annotated ("Georgia Code") which creates the Georgia Credits. Federal Credits and Georgia Credits are utilized to encourage private business to provide a public benefit by allowing investors, in certain circumstances, the ability to offset their respective tax liabilities by investing in low-income housing projects. Banks make equity investments in low-income housing developments to help meet their obligations under the Community Reinvestment Act.

Section 42 of the Internal Revenue Code provides for Federal Credits to be awarded to real estate developers (and equity investors in real estate) who develop and maintain affordable residential properties that satisfy prescribed criteria. Pursuant to the Georgia Code, one dollar of Georgia Credits is available for each dollar of Federal Credits generated by a low-income housing property. In exchange for equity capital for property development developers agree to allocate these credits to investors. Generally, in order to retain these credits, the property must be operated and maintained as a low-income housing project in accordance with prescribed rules for a minimum 15-year compliance period.

Under Section 42 of the Internal Revenue Code, Federal Credits are available with respect to "qualified low-income residential properties," that is, residential rental properties in which (a) 20% or more of the aggregate residential rental units are occupied by tenants with incomes of 50% or less of area median income, as adjusted for family size (the "20-50 Set-Aside Test") or (b) 40% or more of the aggregate residential rental units are occupied by tenants with incomes of 60% or less of area median income, as adjusted for family size (the "40-60 Set-Aside Test") (each test being the "Minimum Set-Aside Test"). Additionally, the gross rent charged to tenants of units comprising the Minimum Set-Aside cannot exceed 30% of the applicable Set-Aside income (50% or 60% of area median income) for a family of a specified size (the "Rent Restriction Test"). Georgia Credits are allowed with respect to residential properties in Georgia placed in service after January 1, 2001 which qualify for Federal Credits. Federal Credits are delivered during the first ten years a property meets the minimum requirements, although a property needs to remain in compliance with specific low-income housing rules for a full 15-year period. The Georgia Department of Community Affairs administers the Georgia Credit program subject to rulings from the Georgia Department of Revenue and Department of Insurance.

How Georgia Credits Work in Practice

Georgia Credits may be allocated among some or all of the partners, members, or shareholders of the entity owning the low-income housing project in any manner agreed to by such persons, whether or not such persons are allocated or

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allowed any portion of the Federal Credit with respect to the project. Thus, for example, to receive an allocation of Georgia Credits, an investor must be admitted (directly or indirectly) into the project-owning entity (such as a partnership or limited liability company) as an owner. The governing documents of the project-owning entity (such as a partnership agreement or limited liability agreement) dictate how the Georgia Credits are to be allocated among the owners.

When a surplus lines broker buys into a low income housing fund, Georgia Credits are normally sold and delivered over ten years. However, due to extraordinary circumstances, some banks have been selling one-year Georgia Credits. Georgia Credits are sold on a standalone basis and at a discount which creates a positive rate of return on funds which would otherwise be paid as taxes. A surplus lines broker who purchased Georgia Credits files Form IT-HC (typically provided by the bank) with his Georgia quarterly surplus lines tax affidavit. Georgia Credits are normally delivered in the first quarter for the previous tax year. As mentioned, the Georgia Credits offset surplus lines taxes dollar for dollar. So, for example, a \$100 of Georgia Credits will offset \$100 of Georgia surplus lines taxes. Any un-used Georgia Credits may be carried forward for up to three years, but cannot be applied to previous years' returns.

The Georgia low-income housing tax credit program benefits Georgians by subsidizing the cost of low-income housing and it can also be used by surplus lines brokers to turn what is normally an expense into an income producing asset.

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