

## Publications

### Long Awaited 50(d) Income Regulations Released

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On July 22, 2016, the Internal Revenue Service (IRS) and Department of Treasury published long awaited temporary and proposed regulations (Regulations) regarding so-called “50(d) income” affecting historic tax credit (HTC) transactions and energy tax credit (ETC) transactions. The Regulations are applicable to projects placed in service on or after September 19, 2016.<sup>[1]</sup>

In a so-called “direct investment” structure, it is the owner of the property generating the credit that claims the HTC (or ETC). When this structure is used, the tax basis of the property must be reduced by the amount of the HTC claimed (or 50% of the ETC claimed), thereby reducing the aggregate depreciation deductions available to the property owner over the depreciable life of the property. 50(d) income has no application to “direct investment” structures.

In the popular “master lease” structure, the property owner makes an election to allow a lessee of the property to claim the HTC (or ETC). The tax basis of the property is not reduced in this structure. Rather, the lessee must include a deemed amount in income each year during the depreciable life of the property (i.e., 50(d) income). The amount of the annual income inclusion is equal, in effect, to the amount of the depreciation reduction that would have resulted from a tax basis decrease under the “direct investment” structure. For example, if in a master lease structure the underlying property is depreciable over 39 years, and the amount of the HTC is \$3,900,000, then the lessee’s annual 50(d) income inclusion amount would be \$100,000.

Historically there has existed significant uncertainty as to how to apply 50(d) income rules where the lessee is a partnership for tax purposes, most notably with respect to (i) the impact upon 50(d) income of the exit of a partner from the lessee partnership, and (ii) the impact of 50(d) income upon the tax basis of the partners of the lessee partnership.

The Regulations provide that 50(d) income is direct income of the partners of the lessee partnership, and that, therefore, the 50(d) income of a partner will have no impact on the tax basis of its partnership interest. In addition, under the Regulations, such a partner will continue to have 50(d) income inclusions even after the partner transfers all of its interest in the lessee partnership, though upon exit from the lessee partnership following the recapture period a partner may elect to accelerate its remaining 50(d) income. (Similar rules apply with respect to shareholders of lessee S corporations.)

Taxpayers have until October 20, 2016 to submit written comments on the Regulations. The tax credit industry is actively analyzing the Regulations and addressing concerns with IRS representatives. Vorys will continue to monitor developments relating to the Regulations.

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<sup>[1]</sup> In spite of the stated effective date, the Regulations contain examples that apply the new rules to transactions involving property placed in service prior to September 19, 2016. Preliminary discussions with the IRS on this point suggest that the use of earlier dates in the examples was inadvertent, but uncertainty on this point currently exists.