



A Guide to Accounting for Tax Credit Investments

Key Aspects of ASU 2023-02:

ASU 2023-02 Investments – Equity Method and Joint Ventures (Topic 323) expands the proportional amortization method to more tax credit investment structures. Previously, the proportional amortization method was only available for investments in qualified affordable housing projects, such as those involving Low-income Housing Tax Credits (LIHTC). ASU 2023-02 expands the scope, allowing entities to elect the proportional amortization method for other types of tax credit investments made primarily to receive income tax credits and other income tax benefits, such as New Market Tax Credits (NMTC), Historic Rehabilitation Tax Credits (HTC), and Renewable Energy Tax Credits (RETC), provided certain conditions are met.

The proportional amortization method must be elected on a tax credit program by tax credit program basis, not for individual investments. The investment must be a limited liability entity that is a flow-through for tax purposes, made primarily to receive income tax credits and other income tax benefits, and must meet the conditions in FASB 323-740-25-1 –

It must be probable that any income tax credits allocated to the investor will be available.

- The investor does not have significant influence over the operations or financial policies of the underlying project.
- Substantially all of the total projected benefits of the investment are derived from income tax credits and other income tax benefits.
- The investor expects a positive yield from the investment based solely on the anticipated income tax benefits.
- The investor is a limited liability investor in the limited liability entity for both legal and tax purposes, with liability limited to its capital investment.

Under ASU 2023-02, the investment cost is amortized in proportion to the receipt of tax credits and income tax benefits, with the amortization and related tax credits netted in the income statement as a component of income tax expense (benefit).

Situational Example #1 – Low-Income Housing Tax Credit (LIHTC) Investment:

A corporation invests \$100,000 in a partnership for affordable housing, expecting \$120,000 in tax credits/benefits over 10 years. If \$12,000 is allocated in Year 1, then 10% (\$10,000) of the investment is amortized as expense in Year 1. Both amortization and tax credits are presented net in income tax expense.



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Situational Example #2 –New Market Tax Credit (NMTC) Investment:

A bank invests in an LLC for New Markets Tax Credits. The bank elects the proportional amortization method, amortizing its investment in proportion to the NMTCs and other tax benefits received each year, with results presented net, in income tax expense.

Situational Example #3 –Renewable Energy Tax Credit (RETC) Investment:

A utility invests in a partnership for solar projects, qualifying for renewable energy tax credits. The investment is amortized in proportion to the tax credits and benefits received, with presentation net, in income tax expense.

Situational Example #4 – Investment with Non-Income Tax Related Benefits:

If an investment provides both income tax credits and non-income-tax-related benefits (e.g., state grants), only the portion related to income tax benefits is eligible for the proportional amortization method. The rest is accounted for separately.

Required Disclosures:

- The amount and reporting line of income tax credits and other benefits recognized during the period.
- The amount and reporting line of the investment in the statement of financial position.
- The amount of investment amortization recognized in income tax expense.
- The amount and reporting line of non-income tax related returns received.
- Any significant modifications or events affecting the investment or underlying project.
- The amount of any commitments or contingent commitments (including delayed equity contributions), by year.
- The amount and description of any impairment losses recognized due to forfeiture or ineligibility of tax credits or similar circumstances.

Summary:

ASU 2023-02 is effective for all entities, other than public business entities, for fiscal years/periods beginning after December 15, 2024. The proportional amortization method directly links the amortization of the investment to the receipt of tax benefits and presents the net effect in income tax expense which provides a clearer reflection of investments made primarily for tax benefits.