

Housing Credit 101

Housing Credit Program Basics

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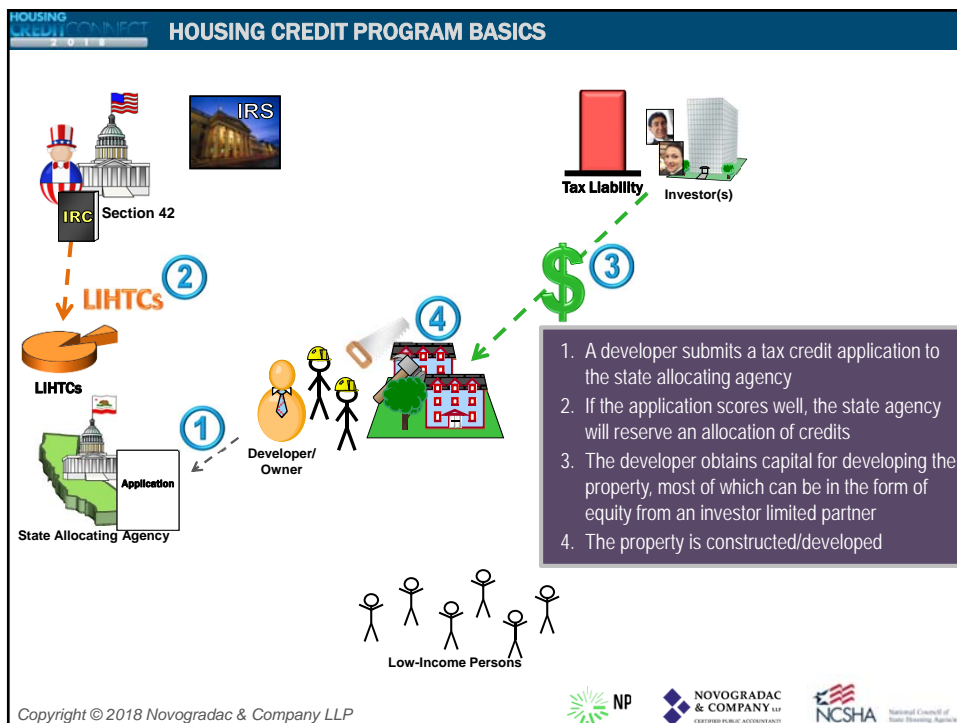
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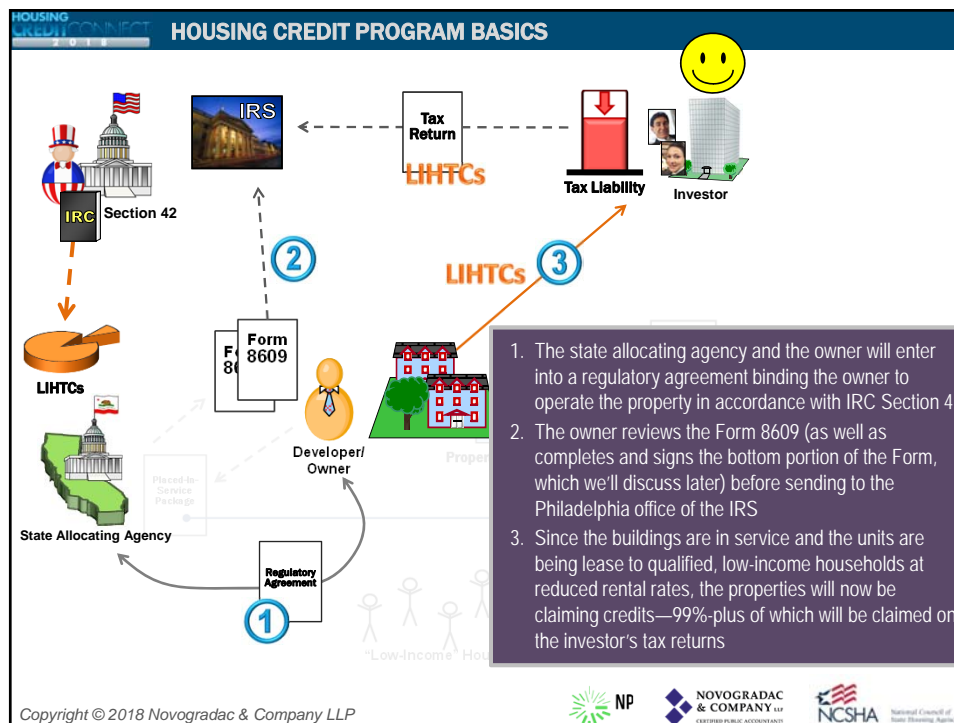
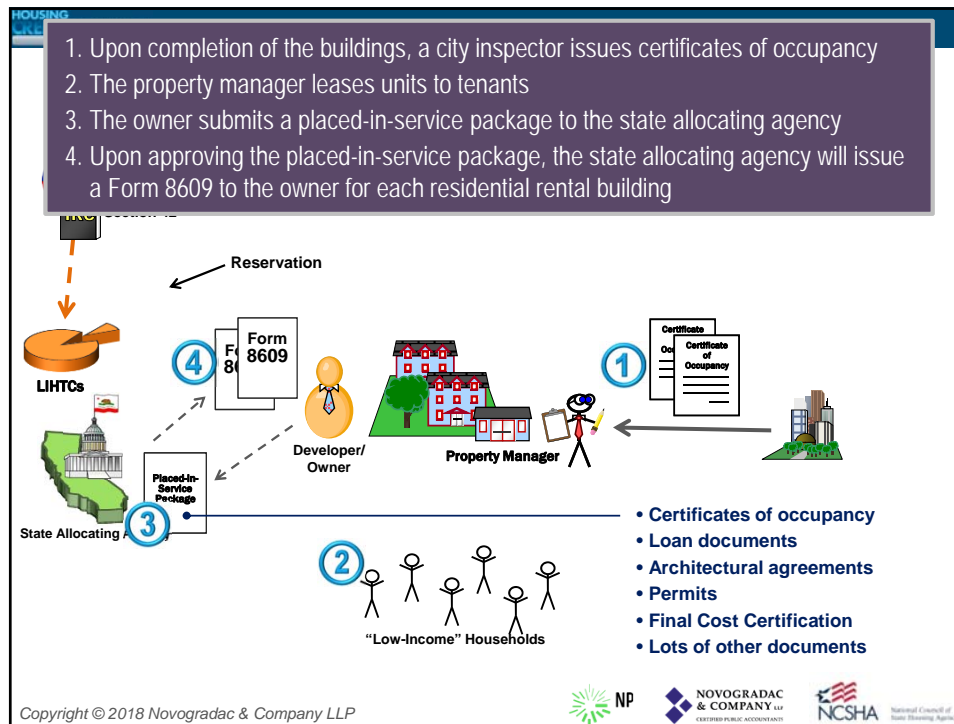
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HOUSING CREDIT CONNECT
2018

NCSHA









HOUSING CREDIT PROGRAM BASICS

Background




- Part of 1986 Tax Reform to Encourage the Construction and Rehabilitation of Affordable Rental Housing
- Administered by the Treasury Department and Allocated by State Agencies
- Contained in Section 42 of the Tax Code
- Emphasis on Private Sector Involvement (i.e. Developing and Managing Properties)
- Objective:
 - To Provide Investor Equity to Lower Debt Service, Thereby Lowering Rents
- Credit is a Dollar-for-Dollar Tax Reduction
- Credit Amount Based on the Cost of Constructing or Rehabilitating Housing Developments

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Program Requirements

- Minimum Percentage of LIHTC Units (20/50, 40/60, or Income Averaging)
- Minimum 30-Year Affordability Commitment
- Maximum Income Limited for Households Renting LIHTC Units
- Maximum Rents Limited for LIHTC Units
- Projects Subject to IRS and State Regulation/Compliance

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HOUSING CREDIT PROGRAM BASICS

Industry Participants




- Congress
- IRS/Department of Treasury
- State Tax Credit Agencies
- Developers/Owners
- Property Managers
- Syndicators/Investors
- GSEs
- Nonprofits
- State/Local Governments
- HUD
- Tenants
- Tax Professionals


  

HOUSING CREDIT PROGRAM BASICS

State Allocation Volume Limit




- Credits Are Limited
- In 2000, Congress Raised Cap from \$1.25 to \$1.50 in 2001, \$1.75 in 2002, and Thereafter Adjusted for Inflation
- In 2008, Congress Raised Cap from \$2.00 to \$2.20 (2008/2009 only)
- 12.5% increase for 2018-2021
- \$2.70 Per Person for 2018
- \$3,110,000 State Minimum in 2018


  

**HOUSING CREDIT PROGRAM BASICS**

Volume Limit Rules




- **Example:**
 - State With Three Million Population Has \$8,1000,000 in Credits in 2018
- **Allocated Amount Is for One Year of Credit**
- **10% Nonprofit Set-Aside**
- **50% Test: Private Activity Tax-Exempt Bonds Subject to Bond Volume Cap; No Credit Allocation Needed**


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**HOUSING CREDIT PROGRAM BASICS**

Qualified Allocation Plans




- **State Must Adopt QAP to Allocate Credits**
- **Must Set Forth Allocation Priorities**
- **Must Give Preference to:**
 - Lowest Income Tenants
 - Longest Period of Low-Income Use
 - QCT Projects Contributing to a Concerted Revitalization Plan
- **Must Take into Account Energy Efficiency and Historic Nature of Projects**
- **Must Provide Procedure for Notifying IRS of Non-Compliance**
- **Bond-Financed Projects Must “Satisfy” QAP**


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HOUSING CREDIT PROGRAM BASICS

Project Evaluation




- Credit May Not Exceed Amount State Agency Determines Is Necessary for Feasibility and Viability
- Agency Must Consider:
 - Sources and Uses
 - Amounts Expected to Be Generated by Tax Benefits
 - Reasonableness of Development and Operating Costs
- Evaluation Occurs at the Time of Application, Allocation and Placement in Service


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Project Evaluation




- Owner Must Certify as to Amount of Subsidies
- For Tax-Exempt Bond Financed Projects, Issuer Must Make Similar Evaluation
- Agency Must Require Market Study Paid by Developer


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Compliance Monitoring




- State Credit Agencies Monitor Projects
- Check QAP for Specific Requirements
- Owners' Recordkeeping Requirements:
 - Number of Low-Income and Total Units
 - Income Certifications and Annual Re-Certifications (in some Cases, Other Than for 100% low-income) and Backup Verifications
 - Qualified Basis and Eligible Basis Amounts
 - Rent Amounts
- Owner Annual Compliance Certifications

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Who Can Use Credits?



- C Corporations Can Use Credits and Losses Against Ordinary Income and Taxes
- Limitations on “Closely-Held” Corporations
- Individuals Limited Under Passive Loss Rules
- *Credit May Be Used to Offset Alternative Minimum Tax (Effective for Buildings Placed in Service After 2007 and Rehabilitation Expenditures Incurred After 2007)*

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Eligible Basis: General Rules




- New Construction = Adjusted Basis (Generally, Development Cost Less Land)
- Acquisition = Acquisition Cost of Building
- Substantial Rehabilitation = Capitalized Rehabilitation Expenditures (24-Month Rule)
- Must Subtract Federal Grants
- Excludes Commercial Space But Includes Common Areas
- 130% Increase in Qualified Census Tracts (“QCTs”) and Difficult Development Areas (“DDAs”), and Areas Specially Designated by Credit Agencies

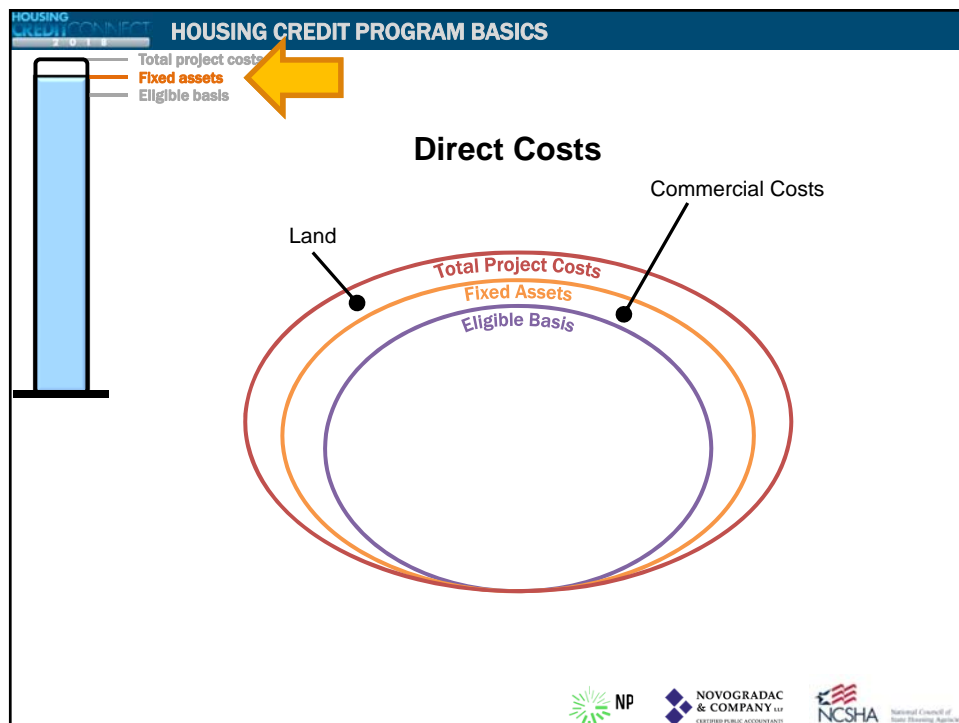
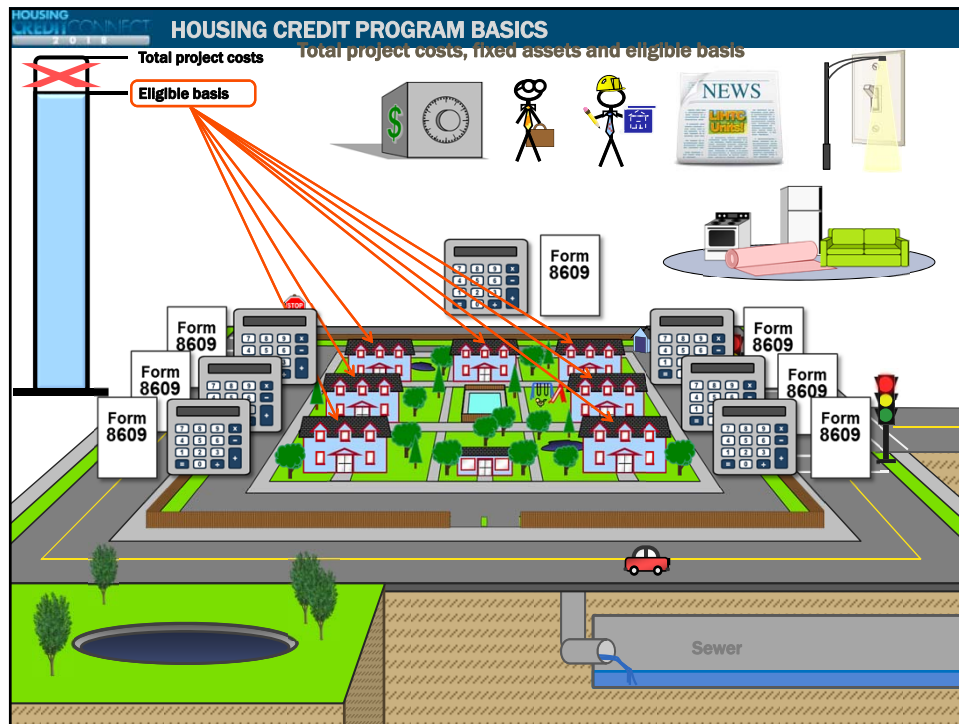



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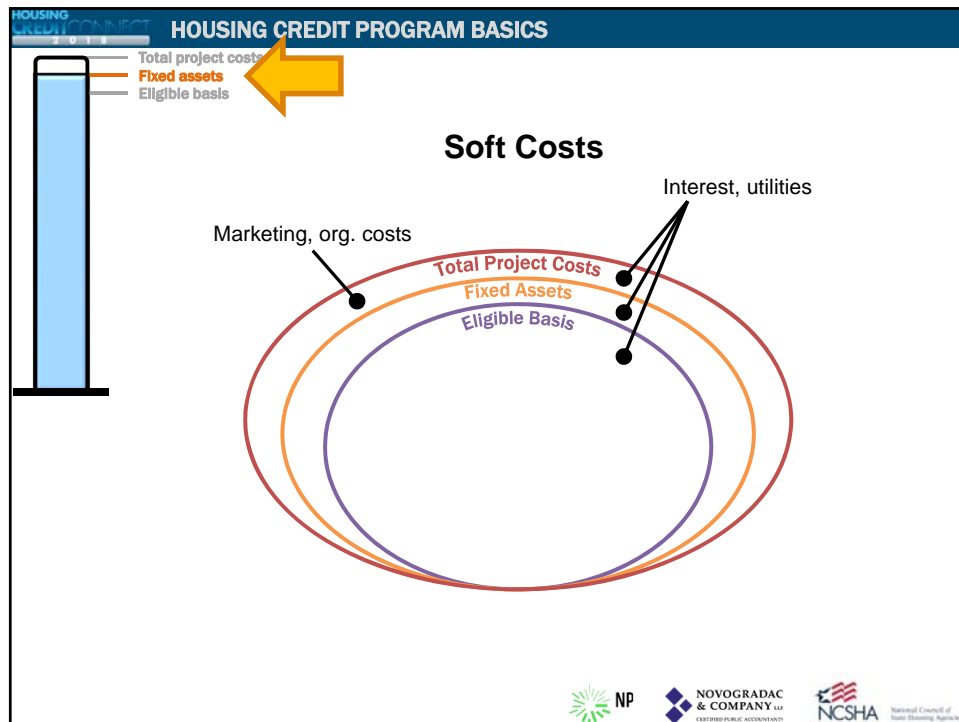
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Calculating Credits

Eligible Basis	\$ 2,000,000
<u>x Applicable Fraction</u>	<u>x 100%</u>
Qualified Basis	\$ 2,000,000
<u>x Tax Credit Percentage</u>	<u>x 9%</u>
Annual LIHTCs	\$ 180,000
<u>x Ten Years</u>	<u>x 10</u>
Total LIHTCs	\$ 1,800,000




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HOUSING CREDIT PROGRAM BASICS

Eligible Basis: What Is Included?

Depreciable Basis of Residential Rental Housing Eligible for Tax Credits

INCLUDES	EXCLUDES
<ul style="list-style-type: none"> • Impact Fees • Onsite Roads, Sidewalks and Parking Lots • Cost of Utility Hookup • Landscaping if Adjacent to Building • Final Grading of Building Site • Common Area • Full-Time Manager's Unit • Community Space (with Some Limitations) 	<ul style="list-style-type: none"> • Land and Land-Related Costs • Historic Tax Credits Taken on Residential Part of Project • Fees and Costs Related to Permanent Loan Financing • Syndication-Related Costs • Tax Credit Fees • Reserves • Post-Construction Working Capital • Federal Grants • Non-Residential Costs

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Understanding the 4% and 9% Credits

Qualifying for the 4% Credit

Qualifying for the 9% Credit


- Acquisition of Building
- Tax-Exempt Bond Financing

- New Construction/Rehabilitation if Building Is Not "Federally Subsidized" (Which Now Means Financed by Tax-Exempt Bonds)
- "Below Market Federal Loans" No Longer Disqualify Building from 9% Credit

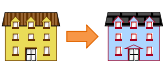




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Construction Method




New Constr.




Acq/Rehab

Financing Method







Non-volume-cap-bond debt



"Federally Subsidized"




9%	3.29% / 9%
3.29%	3.29% / 3.29%






**HOUSING CREDIT PROGRAM BASICS**

Applicable Percentage




- With Qualified Basis Defined, Now Define Applicable Percentage
- Two Credit Rates:
 - 4% Credit = 3.29% for June 2018 (Floating)
 - 9% Credit = “Not Less Than 9.00%” PATH Act of 2015
- Owner Elects to Set Applicable Percentage Either
(i) When Receiving a Binding Commitment From the State
(or When Tax-Exempt Bonds Are Issued), or (ii) When
Building Is Placed in Service



**HOUSING CREDIT PROGRAM BASICS**

Understanding the Affordability Commitment




- 30-Year Affordability Commitment
 - 15-Year Tax Credit Compliance Period
 - 15-Year Extended Use Period
- Extended Use Agreements
- Early Termination of 30-year Affordability Commitment
 - Foreclosure (or Instrument in Lieu of Foreclosure)
 - Qualified Contract Process



HOUSING CREDIT PROGRAM BASICS

Understanding Income and Rent Restrictions




- Income Restrictions
- Rent Restrictions

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Income Restrictions

- Minimum Set-Aside Election of:
 - 20% of Units at 50% of Area Median Income ("AMI"), or
 - 40% of Units at 60% of AMI, or
 - Income Averaging
- Election Upon Placement in Service
- Must Meet Minimum Set-Aside by End of First Credit Year
- HUD Publishes Area Income Figures Annually




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Income Averaging

- Consolidated Appropriations Act of 2018 makes it possible for units to qualify as “low income units” with incomes as high as 80% of Area Median Income (“AMI”)
- Under the new rules, at least 40% of the low income units must average 60% of AMI, provided that no low income unit’s occupants may exceed 80% of AMI
- An owner will literally designate units at any of the following percentages: 20, 30, 40, 50, 60, 70 or 80, provided that all of the units taken together will average out to not more than 60%
- Floor size does not affect this computation







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Open Questions/Issues With Income Averaging




- Are the states obligated to adopt income averaging?
- Will income averaging apply to pre-2018 deals that have not received IRS Forms 8609?
- Will state QAPs need to be modified to permit income averaging?
- Is IRS guidance necessary to implement this new rule?
- Are 80% units allowed to “float” during the compliance period?
- Does income averaging apply to rent limits as well as income limits?
- Additional questions and open issues?




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Rent Restrictions




- Rent (Including Utilities) Cannot Exceed 30% of Qualifying Income for Assumed Family Size; Based on Bedrooms Per Unit
- Rent Limits Change Annually With Publication of New Area Median Incomes
- Rent Will Not Decrease Below Original Floor
- Gross Rent Does Not Include Section 8 (or Similar Rental Subsidies)
- Gross Rent Must Include Utility Allowance for Tenant-Paid Utilities (i.e., Deduct From Rent to Owner)

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Nonprofit Set-Aside

- Each State Tax Credit Agency Must Set Aside at Least 10% of Its Annual Credit Ceiling Each Year for Projects Involving Qualified Nonprofit Organizations
- Many States Provide Preferences for Nonprofit Sponsored Projects by Assigning “Points” to Projects with Nonprofit Involvement
- Whenever There Is Nonprofit Involvement, Need to Determine Whether the Tax Credit Agency Actually Awarded Credits from the Nonprofit Set-Aside

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