

# THE HFA INSTITUTE 2024

## Monitoring Compliance with the Average Income Test



National Council of State Housing Agencies



**MRBs and Other Federal Homeownership Programs**  
JANUARY 10 – 12



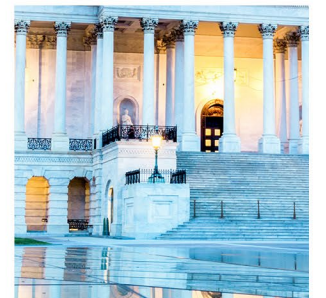
**Housing Credit**  
JANUARY 9 – 11



**Section 8 and Other Federal Multifamily Programs**  
JANUARY 10 – 12



**HOME and Housing Trust Fund**  
JANUARY 7 – 9



**DISCUSSION LEADER**

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Director of Compliance and Training | Ohio Capital Corporation for Housing

# Agency Perspective

- Average Income Test (AIT) 2018-2021
  - Partner Discussions
  - Agency Interpretation & Implementation
  - QAP Updates
  - Temporary Rule (Fixed Units) & Public Comment Period & Hearings
- AIT 2022 Final Rule
  - Removal of the “Cliff Test”
  - Units can Float
  - Additional Annual Owner Reporting Requirements

# Agency Perspective

- Agency Monitoring Concerns
  - Waiting on Software Enhancements
  - Identifying and Reporting Noncompliance
  - Multiple Building Project Elections (IRS 8609 Line 8b)
  - AIT with 4% Tax Exempt Bonds
  - Written Guidance & Monitoring Procedures
  
- Annual Reporting - Required for 2023
  - Unit Designation & Changes
  - Qualified Group of Units – Average Test and Applicable Fraction
  - Excluded Units

# Qualified Unit Group – Average Income Test

- Meet the Minimum Set-Aside
- Taxpayer identifies a “qualified group” of 40% of the project’s units having income levels averaging 60% or less
- Qualified Average Income Test (AIT) Group is identified timely each taxable year of the extended use period
  - Maintains records in accordance with retention requirements in Treas. Reg. § 1.42-5(b)(2)
- Units in Qualified AIT Group are rent-restricted
- Units in Qualified AIT Group are occupied by qualified households

# Qualified Unit Group – Applicable Fraction

- Defines low-income units used to calculate annual credits
- Taxpayer identifies a “group of qualified units” for purposes of determining the Applicable Fraction (AF)
  - Each taxable year throughout the extended use period, the taxpayer will need to identify the units to be included in the group
- Same definition for the Qualified AIT Group
- Can include, but not limited to, the same units in the Qualified AIT Group
  - IRS Form 8609, line 8b – If Yes, units in the Qualified AF Group are not limited to one BIN and **can span** across multiple BINs.

8a Original qualified basis of the building at close of first year of credit period . . . . .	8a
b Are you treating this building as part of a multiple building project for purposes of section 42 (see instructions)? . . . . .	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No

# Floating of Unit Designations

- **2020 Proposed Regulation** – stipulated once a unit was designated a specific income limit level designation it could not be changed
  - Created additional & unnecessary barriers when transfers needed under VAWA, Reasonable Accommodations, or correcting noncompliance
- **Final Regulation** – removed the blanket prohibition giving State Housing Finance Agencies (HFAs) broad discretion to develop policies & procedures regarding unit designation changes

# Floating of Unit Designations

- Unit designations **can** change:
  - Federally permitted changes
  - In accordance with Housing Finance Agency (HFA) policy
  - When the designation change is needed:
    - VAWA
    - Fair Housing Act
    - Section 504 of the Rehabilitation Act of 1973
    - Other federal, state or local law affording tenant protections
  - When an income-qualified household tenant transfers to a different unit in the project
    - Units swap income level designations
  - Restore compliance with AIT requirements (discussed later with Correcting Noncompliance)

# Floating of Unit Designations

- Timings for Unit Designation Changes:
  - **Vacant Units** – designation must be changed before being occupied
  - **Occupied Units** – must be changed prior to the last day of the taxable year

# Annual Recertifications

- **100% LIHTC Projects** – does not have to complete annual income recertifications
  - Be aware of State Housing Finance Agency (HFA) requirements
  - Understand your Investor requirements
  - Know Layered Program requirements
- **Mixed-Income Projects** – will continue to complete annual recertifications

## Next Available Unit Rule (NAUR)

- **2020 Proposed Regulation** – Prohibited changing unit designations and Mitigating Actions
- **Final Regulation** –
  - Next available **market rate unit** being used to satisfy the NAUR be rented & re-designated to an income limit designation that will maintain compliance with AIT instead of the income limit level that was designated to the over-income (OI) unit initially triggering the NAUR
  - NAUR **does not** have to be followed in any specific order when multiple low-income units are determined to be over-income
    - Could impact the “Qualified Unit Group” – Applicable Fraction

# Correcting Noncompliance

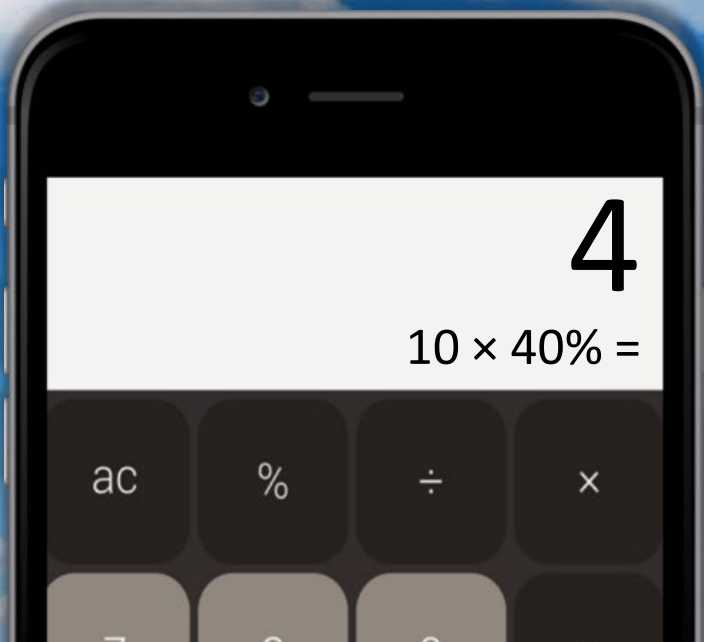
- Final Regulation removed Mitigating Actions that stipulated issues of noncompliance impacting AIT could only be remedied if the noncompliance was corrected & AIT restored within 60 days of the close of the taxable year
- Redesignating Units, *if applicable*
- **EXAMPLE – Piney Flats**
  - 10-unit building – all units are the same size
  - 5 units were designated at 40%
  - 5 units were designated at 80%
  - Eligible Basis was \$3,000,000 and Applicable Credit Percentage was 9%

Piney Flats

YEAR 1

Average  
Income Group ←

101 80%	106 40%
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 80%	110 40%



# Piney Flats

## YEAR 1

**Average** ←  
**Income Group**

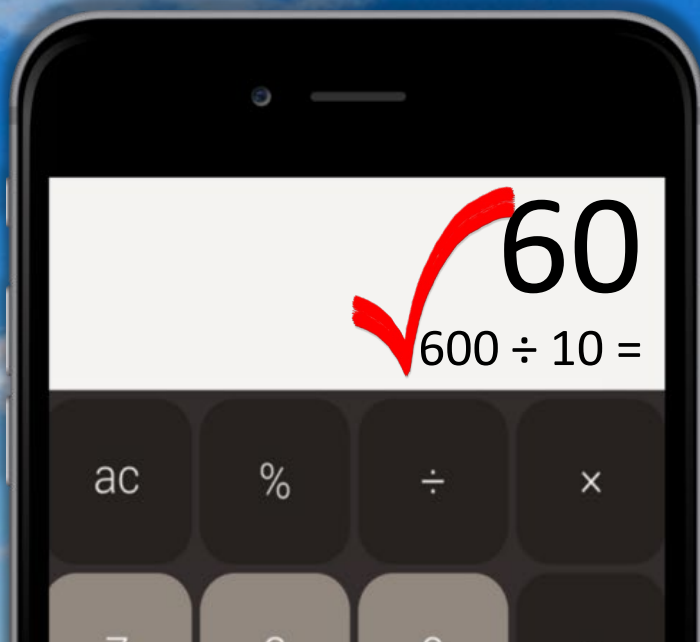
101 80%	106 40%
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 80%	110 40%



Piney Flats  
**YEAR 1**

Applicable  
Fraction  
Group

101 80%	106 40%
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 80%	110 40%



# Piney Flats

## YEAR 1

**Eligible Basis** X **Applicable Fraction**  
= **Qualified Basis**

**Qualified Basis** X **Applicable Credit %**  
= **Annual Tax Credit**

3,000,000

$3,000,000 \times 100\% =$

270,000

$3,000,000 \times 9\% =$

101  
80%

106  
40%

102  
80%

107  
40%

103  
80%

108  
40%

104  
80%

109  
40%

105  
80%

110  
40%




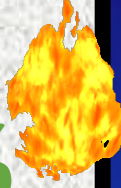
# Correcting Noncompliance

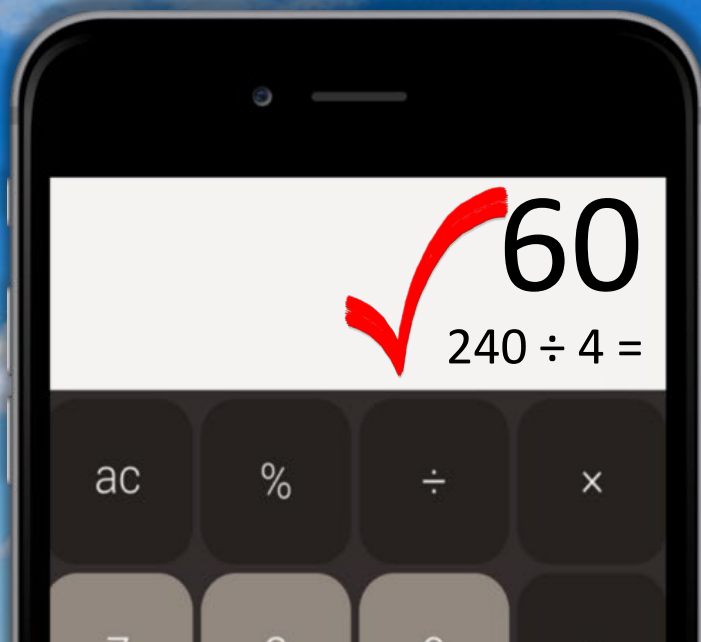
- **EXAMPLE – Piney Flats**
  - 10-unit building – all units are the same size
  - 5 units were designated at 40%
  - 5 units were designated at 80%
  - Eligible Basis was \$3,000,000 and Applicable Credit Percentage was 9%
- **YEAR 2**
  - Unit 106 was destroyed by fire and was not restored to habitable condition by the end of the year.

Piney Flats

YEAR 2

Average  
Income Group ←

101 80%	 106 40% 
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 80%	110 40%



# Piney Flats YEAR 2

Applicable  
Action  
up

<del>100 80%</del>	<del>106 40%</del>
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 80%	110 40%

560  
 $80 + 80 + 80 + 80 + 80 +$   
 $40 + 40 + 40 + 40 =$

62.22  
 $560 \div 9 =$



# Correcting Noncompliance

## ■ EXAMPLE – Piney Flats

- 10-unit building – all units are the same size
- 5 units were designated at 40%
- 5 units were designated at 80%
- Eligible Basis was \$3,000,000 and Applicable Credit Percentage was 9%

## ■ YEAR 2

- Unit 106 was destroyed by fire and was not restored to habitable condition by the end of the year.
- **Owner removed Unit 105 from the calculation to restore AIT compliance → affects the annual credit amount**

Piney Flats  
**YEAR 2**

Applicable  
Fraction  
Group

**101**  
80%

~~106~~  
~~40%~~

**102**  
80%

**107**  
40%

**103**  
80%

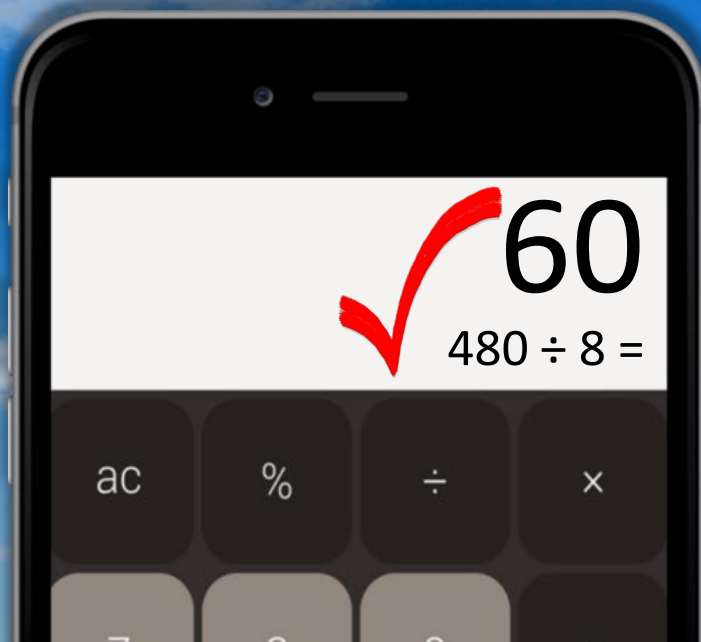
**108**  
40%

**104**  
80%

**109**  
40%

~~105~~  
~~80%~~

**110**  
40%



# Piney Flats

## YEAR 2

**Eligible Basis** X **Applicable Fraction**  
= **Qualified Basis**

**Qualified Basis** X **Applicable Credit %**  
= **Annual Tax Credit**



101 80%	<del>106 40%</del>
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
<del>105 80%</del>	110 40%



# Piney Flats

## YEAR 2

**Eligible Basis** × **Applicable Fraction**  
= **Qualified Basis**

**Qualified Basis** × **Applicable Credit %**  
= **Annual Tax Credit**

2,400,000

$3,000,000 \times 80\% =$

216,000

$2,400,000 \times 9\% =$

101  
80%

~~105  
40%~~

102  
80%

107  
40%

103  
80%

108  
40%

104  
80%

109  
40%

~~105  
80%~~

110  
40%



**But what if...**

# Correcting Noncompliance

- **EXAMPLE – Piney Flats**

- 10-unit building – all units are the same size
- 5 units were designated at 40%
- 5 units were designated at 80%
- Eligible Basis was \$3,000,000 and Applicable Credit Percentage was 9%

- **YEAR 2**

- Unit 106 was destroyed by fire and was not restored to habitable condition by the end of the year.
- **Owner redesignated Unit 105 from 80% to 60% (existing tenant qualifies under 60%) → affects the annual credit amount**

# Piney Flats YEAR 2

Applicable  
Fraction  
Group ←

101 80%	<del>106 40%</del>
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 60%	110 40%



# Piney Flats

## YEAR 2

**Eligible Basis** X **Applicable Fraction**  
= **Qualified Basis**

**Qualified Basis** X **Applicable Credit %**  
= **Annual Tax Credit**



101 80%	<del>106 40%</del>
102 80%	107 40%
103 80%	108 40%
104 80%	109 40%
105 60%	110 40%



# Piney Flats

## YEAR 2

**Eligible Basis** X **Applicable Fraction**  
= **Qualified Basis**

**Qualified Basis** X **Applicable Credit %**  
= **Annual Tax Credit**

2,700,000

$3,000,000 \times 90\% =$

243,000

$2,700,000 \times 9\% =$

101  
80%

~~106  
40%~~

102  
80%

107  
40%

103  
80%

108  
40%

104  
80%

109  
40%

105  
60%

110  
40%



# AIT & Multiple Subsidies

- AIT & HOME Funds
- AIT & HUD

# Syndicator Perspective

- It's still early days!
- Investors still cautious
- Developers have whiplash
- Monitoring concerns
  - Additional pre-approval reviews
  - Reports
    - Need more transparency on rents
    - Need to identify excluded units and qualified groupings

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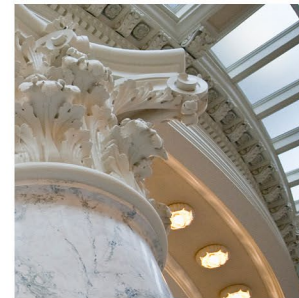
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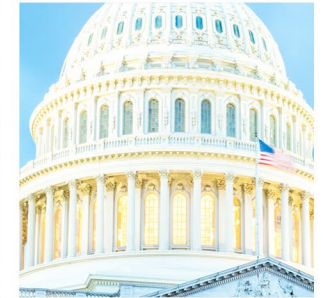
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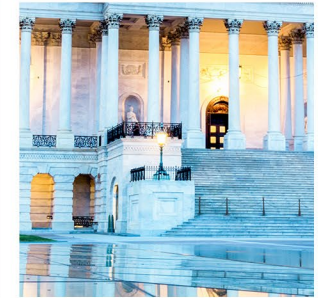
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## THANK YOU for joining us!



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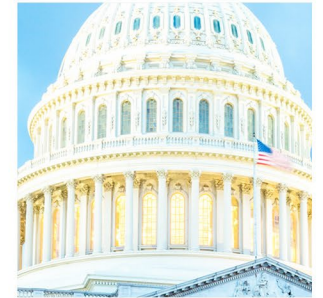
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