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Low Income Housing Tax Credit Fact Sheet

PHADA has established a working group related to the Low Income Housing Tax Credit (LIHTC) program, which continues to be the major production program for affordable rental housing. Two bills, Senate 548 and House of Representatives 1661, propose expanding and strengthening the LIHTC program. Below you will find some basic background information about the LIHTC program as well as a synopsis of the bills.

Background

The LIHTC program was established by revision to the US Tax Code in 1986 to provide private owners with an incentive to create and maintain affordable housing for low income households.

How the Tax Credit Works for Investors

Tax credits provide a dollar-for-dollar reduction of your income tax liability. This means that a \$1,000 tax credit saves you \$1,000 in taxes. Credits are more valuable than tax deductions, which lower your taxable income. Most investors are institutional and buy into funds that are operated by syndicators. The tax credit investment is usually underwritten at 35% corporate tax rate.

Allocation of Housing Tax Credits to States

Although housing tax credits are federal, each state has an independent agency, generally a housing finance agency (HFA), which decides how to allocate the state's share of federal housing tax credits. Tax credits are allocated to states based on population. In 2017, each state received \$2.35 per capita, with small states receiving a minimum of \$2.71 million. Each HFA must have a qualified allocation plan (QAP), which sets out the state's priorities and eligibility criteria for awarding federal tax credits, as well as tax-exempt bonds. The law requires that a minimum of 10% of an HFA's total tax credits be set aside for nonprofits.

Investors buy income tax credits in properties that have received state allocation, generating equity for owners and reducing project development debt burden. In exchange, the owner agrees to rent a specific number of units to qualified tenants at specified rents, usually below-market. Two levels of tax credits are available: one at a true 9% of depreciable basis, competitively allocated; the other, at a nominal 4% (based on the present value calculations using a Federal cost of funds rate) this is usually less than 4%) of depreciable basis, comes with state bond financing, which is capped and allocated by the state agency and which may or may not be competitive. Both SB 548 and HR 1161 propose to make this a "true" 4% rate.

Occupancy and Rent Restrictions

An owner may choose one of two occupancy restrictions:

- At least 20% of units occupied by households with incomes at or below 50% of area median income (AMI).
- At least 40% of units occupied by households with incomes at or below 60% of AMI.

Furthermore, an owner may elect to commit to a deeper restriction of 15% of the units at 40% of AMI. The occupancy restricted units must have "affordable" flat rents set at

30% of income of tenants at the top of the selected AMI category, with an assumed family size of 1.5 persons per bedroom. LIHTC owners may not refuse to rent to Voucher holders because of their status.

Low Income Housing Tax Credit Program by the Numbers

- Nearly 3 million homes built using the LIHTC from inception in 1986
- \$100 billion leveraged in private capital to finance the cost of building quality affordable housing
- 46% of units built house extremely low-income resident (those at 30% of area median income or less)
- 96,000 jobs created annually, 3 million jobs since inception of program
- Generates \$3.5 billion in federal, state and local taxes and \$9.1 billion in wages and business income

S. 548 and H.R. 1661

These bills being considered by the Senate (S. 548) and the House of Representatives (H.R. 1661) expand and strengthen the LIHTC program as noted below. These bills are virtually identical except that the House bill lacks a significant provision of the Senate bill, namely a 50 percent phased-in increase in the amount of available tax credits, and also treats certain energy tax credits differently.

Both bills change the official name from the *Low Income Housing Tax Credit* to the *Affordable Housing Tax Credit*.

The Senate bill would increase the amount of available tax credits by 50 percent, phased in over five years (it is estimated that this would create or preserve approximately 1.3 million rental units over 10 years, an increase of 400,000 units over the current program.) The per capita allocation was last increased and indexed to inflation in 2004, and is currently \$2.35. The current small state minimum is \$2.71 million. The proposal increases these amounts, subject to inflation, to \$3.53 and \$4.065 million, respectively, by 2022. **The House bill includes no such provision.**

Allow income averaging in housing credit properties to allow the 60 percent of AMI occupancy ceiling to apply to the average of all apartments in a property rather than to each individual apartment. The maximum income to qualify for a tax credit apartment would be limited to 80 percent of AMI. The higher rents that households with incomes above 60 percent of AMI could afford have the potential to offset the lower rents that households below 40 or 30 percent of AMI could afford, allowing developments to maintain financial feasibility while providing a deeper level of affordability.

Standardize income eligibility for rural properties - Base income limits in rural projects on the greater of area median income or the national nonmetropolitan median income. This would standardize tenant income limit rules for tax credit projects in rural areas regardless of whether or not they are financed with housing bonds, making bond-financed developments more feasible in rural areas while streamlining program rules.

Provide flexibility for existing tenant income eligibility – Allow existing tenants to be considered low income for the purposes of determining eligible basis if they meet the housing credit income requirement upon initial occupancy, provided their income has not risen above 120 percent of AMI.

Modification of the student-occupancy rules – The new rule makes households composed entirely of adult students under the age of 24 who are enrolled full-time at an institution of higher education ineligible to reside in a tax credit unit. Exceptions are: married students, veterans, the disabled, those with one or more dependent children, and those who are income eligible under tax credit income limits and are financially independent of their parents and guardians, for example, those aging out of foster care and formerly homeless youth.

Limit the rent charged to the maximum Tax Credit rent instead of the HUD-calculated fair market rent for apartments leased by voucher holders and benefiting from either income averaging or the basis boost for extremely low-income tenants since both of these options already reduce rents for the lowest-income tenants. By limiting the rental income to the maximum tax credit rent, the excess rental assistance can be used by the PHA to serve other families.

Establish a minimum 4 percent rate to stabilize 4% LIHTC projects, which have been imperiled by uncertainty in the tax credit syndication market. While historically-low interest rates have improved the viability of many projects, diminished equity proceeds and the elimination of the critical HOME and CDBG funding have nevertheless threatened these projects. The current legislation would permit state housing agencies to provide the same discretionary eligible basis boost to 4% projects as is presently available to 9% projects.

Reconstruction or replacement period after casualty loss – Clarifies that there is no recapture and no loss of the ability to claim tax credits during a restoration period that results from any casualty, provided that the building is restored within a reasonable period as determined by the state allocating agency, not to exceed 25 months from the date of the casualty.

Modification of rights relating to building purchase – Replaces the existing right of first refusal, which was intended to allow nonprofit sponsors of tax credit properties to gain full control of the property at the end of the initial 15-year compliance period, with a purchase option at the minimum purchase price allowed by current law. The current provision has been problematic in practice and this change is intended to help nonprofit sponsors keep properties affordable over the long term.

Modify the 10-year rule – Modify the prohibition on claiming acquisition housing credits for properties placed in service in the previous 10 years by creating an option to instead limit the acquisition basis of the building to the lowest price paid for the building during the past 10 years with an adjustment for cost of living and capital improvements. This provision is meant to support the preservation of properties in need of rehabilitation regardless of when they were placed in service.

Relocation Costs in rehabilitation expenditures - Allow for relocation costs incurred in connection with a rehabilitation of a building to be capitalized as part of the cost of the rehabilitation where they were not before.

Repeal the qualified census tract (QCT) population cap – Remove the aggregate QCT population cap, enabling properties in more areas to receive a 30 percent basis boost, if necessary to make the project financially feasible.

Prohibit local approval and contribution requirements – This provision would remove a requirement that state agencies notify the executive officer, or equivalent, of the local jurisdiction in which a proposed building would be located. Selection criteria in the state Qualified Allocation Plan cannot include consideration of any support for

or opposition to a project from local or elected officials or local government contributions to a project. Current requirements can have the unintended consequence of giving local governments veto power over projects, which is especially problematic in high-opportunity areas where the development of affordable housing may not be supported.

Increase the amount of housing tax credits that developments serving extremely low-income tenants can receive – Provide up to a 50 percent basis boost, if needed for financial feasibility, for developments serving extremely low-income and homeless families and individuals in at least 20 percent of the apartments. This provision would only apply to the portion of the development reserved for households with incomes under 30 percent of AMI.

Allow states to award a basis boost to housing bond-financed developments – Allow states to provide up to a 30 percent basis boost for properties financed with housing bonds if necessary for financial feasibility. This provides parity between development financed with housing bonds and development financed with tax credits.

Elimination of basis reduction for low-income housing properties receiving certain energy benefits – The Senate bill eliminates the basis reduction for tax credit projects that also claim the Section 45L New Energy Efficient Home Credits, the Section 179D Energy Efficient Commercial Building Deduction, and the Section 48 Energy Credit.

The House bill eliminates the basis reduction for projects that also claim the Section 48 Investment Credit, allowing developers to build housing that is affordable and also benefits from the renewable energy measures made possible by this tax incentive.

Restriction of planned foreclosures - Allows state housing finance agencies to prohibit the termination of long-term use agreements to restrict rents when the purpose of a transaction is specifically to terminate those agreements. Requires owner to provide states with at least 60 days written notice of intent to terminate the affordability period so that the state has time to assess the legitimacy of the foreclosure.

Increase of population cap for difficult development areas (DDAs) – Increase the DDA population cap from 20 to 30 percent, enabling properties in more areas to receive additional housing tax credit equity if necessary for project feasibility. DDAs are located in areas with high construction, land, and utility costs. This provision would make the production and preservation of tax credit properties in higher-cost areas more feasible.

Facilitate the development of housing for Native Americans

- (1) Require states to consider the affordable housing needs of Native Americans in their states through a QAP selection criteria.
- (2) Modify the definition of DDAs to automatically include projects located in a Native American area, making these projects eligible for increased tax credit equity if needed to make projects financially feasible.