



TAX CREDIT COMPLIANCE MANUAL

2017 Edition

[Low-Income Housing Tax Credit Program \(LIHTCP\)](#) - Generates low-income residential rental units by encouraging private investment through federal tax credits.

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Introduction:

About the LIHTC

The low-income housing tax credit (LIHTC) program, created in 1986 and made permanent in 1993, is an indirect federal subsidy used to finance the construction and rehabilitation of low-income affordable rental housing. Washington lawmakers created this as an incentive for private developers and investors to provide more low-income housing. Without the incentive, affordable rental housing projects do not generate sufficient profit to warrant the investment.

The LIHTC gives investors a dollar-for-dollar reduction in their federal tax liability in exchange for providing financing to develop affordable rental housing. Investors' equity contribution subsidizes low-income housing development, thus allowing some units to rent at below-market rates. In return, investors receive tax credits paid in annual allotments, generally over 10 years.

Financed projects must meet eligibility requirements for at least 30 years after project completion. In other words, owners must keep the units rent restricted and available to low-income tenants. At the end of the period, the properties remain under the control of the owner.

Responsibilities:

The entities/persons involved in the compliance of the LIHTC Program include WVHDF, the development owner, and the management company/agent including onsite management personnel. The various responsibilities for these entities/persons are set forth below.

Responsibilities of the West Virginia Housing Development Fund

Review Annual Owner Certifications

Annual Owner Certifications are due February 15 every year for the previous year. These will be collected and reviewed along with the Annual Tenant Data upload. All dates and signatures should be complete.

Conduct File Monitoring and Physical Unit Inspections

WVHDF will perform a file review for each development within two (2) years of the last building being placed-in-service and at least every three (3) years thereafter. Owners of the selected developments will be required to provide detailed information on tenant income and rent for at least 20% or more of the low-income units in the development. Information to be reviewed will include, but is not limited to, the annual Tenant Income Certifications, the documentation received to support those certifications (i.e. income and asset verifications), and rent and utility allowance records. Owners must provide organized tenant files to WVHDF with documentation in chronological order. For more information on the monitoring process, see Part 7.6

WVHDF (either by a third-party inspector contractor or by WVHDF staff) will also perform a physical inspection for each development based on the same schedule as defined above.

WVHDF retains the right to perform a file review and/or physical inspection of any low-income building and/or unit at any time during the Compliance and Extended Use Periods, with or without notice to the owner.

Notify IRS of Noncompliance

The Fund is required to notify the Internal Revenue Service using Form 8823, Low-Income Housing Credit Agencies Report of Non-compliance or Building Disposition, no later than forty-five (45) days after the end of the correction period, including extensions.

Whether the project owner remedies the non-compliance or remains out of compliance, the Fund must file a Form 8823.

Retain Records

The Fund will retain all certifications and records for not less than three years from the end of the calendar year in which they are received. The Fund will retain records of non-compliance or the failure to certify for compliance for six years after filing IRS Form 8823, Low-Income Housing Credit Agencies Report of Noncompliance or Building Disposition.

Conduct Training

To be determined

Compliance Monitoring: IRS Form 8609

Owners of residential low-income rental housing are allowed a low-income credit for each qualified **building** over a ten (10) year period. Form 8609 is used to obtain a housing credit allocation from the Fund. A separate Form 8609 must be issued for each building in a multiple building project.

The Fund requires all project owners to provide a completed signed copy of each IRS Form 8609 for each building in a project. This will provide the Fund with the Minimum Set-Aside selected by the project owner, the amount of tax credit claimed, the first year for claiming credit, and whether the building is part of a multiple building project.

Schedule A (Form 8609), Form 8609, and Form 8586 are to be completed annually by the project owner and filed with annual tax return.

Minimum Set-Aside

The applicable household income limits for LIHTC units are based on the Project Owners **Minimum Set-Aside** election; which are located on the signed 8609 for each building in the project. The election once made, is **irrevocable**.

The election will be either 20/50 or 40/60:

- 20/50 is 20 percent or more of the residential units in the building are both rent restricted and occupied by individuals whose income is 50 percent or less of area median gross income,
- 40/60 is 40 percent or more of the residential units in the building are both rent restricted and occupied by individuals whose income is 60 percent or less of area median income.

There is a deadline meeting the Minimum Set-Aide and if not meet, the project is not a low-income building and can never qualify to claim credits. Initial compliance with Minimum Set-Aside must be met no later than December 31st of the second year.

If the minimum set-aside is not met by the initial compliance date, no tax credits can be allowed for the project.

If a building is identified as part of a **multiple building project** on Line 8b of the Form 8609, the minimum set-aside may be met across all noted buildings in the project. If the building is not identified as part of a multiple building project, the minimum set-aside must be met **within that building**.

Placed-in-Service Date

The Placed-in-Service date is the **trigger** for compliance monitoring. This is a building by building date. There will be only one Placed-in-Service date for each building in a project. A building may be placed in service even if the rental units in the building are not currently occupied by low-income tenants. It is possible to have the same or different dates for different buildings in a project. For the purposes of Section 42, the placed-in-service date has two definitions – one for buildings and one for rehabilitation expenditures that are treated as a separate new building. The Placed-in-Service date is:

- For a new construction or existing building used as residential rental property is the date on which the building is ready and available for its specifically assigned function; which is the date on which the first unit in the building is certified as being suitable for occupancy in accordance with state or local law (certificate of occupancy). In general, a transfer of the building results in a new placed-in-service date if, on the date of the transfer, the building is occupied or ready for occupancy,

- For rehabilitation expenditures that are treated as a separate new building are placed-in-service at the close of any twenty-four (24) month period, over which such expenditures are aggregated. The placed-in-service date applies even if the building is occupied during the rehabilitation period²

Regulatory and Restrictive Covenants

The Fund will prepare a Regulatory and Restrictive Covenants for Land Use Agreement prior to the issuance of the IRS Form 8609. Per IRC §42(h)(6), this document must be recorded before the end of the calendar year in which credit is first claimed.

Only Part 1 of the IRS Form 8609 is prepared by the Fund; this is completed by the Fund's Tax Credit Department. An **IRS Form 8609** is prepared for **each building** in the development.

- If rehabilitation and acquisition credits are claimed on the same building, the rehabilitation is treated by Section 42 as a separate building. Therefore, **the acquisition and rehabilitation will receive separate 8609 forms.**

General Public – Fair Housing

All residential rental units in the project **must** be available for use by the general public. LIHTC projects are subject to Title VIII of the Civil Rights Act of 1968, also known as the Fair Housing Act, prohibiting discrimination in the sale, rental and financing of dwellings based on race, color, religion, sex, national origin, familial status, and disability.

The Fair Housing Act also mandates specific design and construction requirements for multi-family housing built after March 13, 1991, to provide accessible housing for individuals with disabilities.

Available to the general public applies to **all** residential units, market or low-income.

Vacant Unit Rule

If a low-income unit becomes vacant during the year, the unit remains LIHTC compliant and eligible for the tax credit for purposes of the minimum set-aside requirement provided reasonable attempts are made to rent the unit or the next available comparable or smaller size unit is rented to an eligible household and no other comparable or smaller size units in the project are rented to non-qualified individuals.

Empty Units

Units that have never been occupied are termed “empty” rather than vacant and cannot be counted as low-income units. However, they must be included in the building’s total unit count.

Next Available Unit Rule – 140% Rule

If the household income for a tenant in a qualified unit increases to more than one-hundred forty (140) percent of the current applicable income limit, the unit is considered as an over-income unit but may continue to be counted as a low-income unit as long the unit continues to be rent restricted and the next comparable size unit in the building **must be rented** to a qualified low-income tenant; even if it is a market rate unit.

Market Unit

A market unit is any non-LIHTC unit whether occupied or not.

Non-transient Occupancy

Residential rental units must be for the use by the general public and all of the units in a project must be used on a non-transient basis.

Staff Unit

Staff units are allowed for full-time staff members. Staff units can be handled one of two ways:

- If the staff unit is a rental unit and is to be counted as part of the qualified basis, then the staff must be income eligible, be certified and sign a lease the same as any low-income eligible tenant. In this case if the staff member receives free rent or a rental discount, the imputed value of the rent must be included as income,
- If the unit is not a residential unit but used as common area by full-time staff, then the staff does not have to be income eligible, certified, sign a lease, or be considered a tenant. The unit would be considered as part of the project’s common care and not classified as a residential unit.

Unit Transfers

As of September 26, 1997, a household can now move to another unit within the same building regardless of income being above the income limit, and still be eligible and counted towards the qualified bases and the minimum set-aside. This is considered a swap in status.

When the Audit Guide was issued it stated that households can move from one building to another as long as the income does not exceed the 140% limit. However, there is nothing in Section 42 or any Revenue Ruling to backup this position. Therefore, the Fund's policy is:

- A household may move from one building to another building within the project as long as, at the time of relocating to another building, the tenant meets the **current** income limit per household size. The household is treated as a new move-in and the unit moved from is treated as a move-out.

The Fund does not require interim recertification's for residents of unit transfers. However, the date of the transfer must be clearly identified in the tenant file.

During the Initial Credit Period, existing tenants **cannot** be transferred for the purposes of qualifying more than one LIHTC unit to count towards the Minimum Set-Aside or Applicable Fraction. Under **no** circumstances can one household be used to initially qualify more than one tax credit unit in the **project**.

Student Rule

Many students are considered to be transient and are not LIHTC eligible. IRS states that no dormitory may be a qualified low-income project.

The student issue is only a concern when everyone in the household is a full-time student; which is defined by the IRS as someone taking twelve (12) credit hours a semester or attending school full-time five (5) months per year at an educational institution with regular facilities, other than a correspondence or night school.

There is no grandfathering of eligibility because a tenant was not a student when they moved-in and later became one. The student rule is to be monitored annually for this purpose. Failure to verify student status annually is an issue of non-compliance.

There are exceptions to this rule:

- A student receiving assistance (Welfare) under Title IV of the Social Security Act,
- Enrolled in a job training program receiving assistance under the Job Training Partnership Act or under other similar Federal, State, or laws,
- Single parents and their children and such parents are dependents and the children are not dependents of another individual other than the parents,
- Married filing a joint return, or
- Student was previously under the care, placement, and responsibility of the local or

county children services agency (foster care)

Tax Credit Compliance Period

The program requires fifteen (15) years of continuous compliance, but allows the credit to be taken over a ten (10) year period.

Once the credits have been allocated, a property built or rehabilitated, the focus shifts for the next fifteen (15) years to compliance.

While there are several critical areas of compliance, the two major keys are income eligibility and rent restrictions for the fifteen-year continuous compliance period.

Extended Use Period

Project Owners are required to extend the low-income commitment period by an additional fifteen (15) years beyond the initial fifteen (15) year compliance period (the extended use period). The extended use period can be up to thirty (30) years for some of the Fund's projects.

The extended use period for a project and other commitments made by the Project Owner and the Fund is part of the Regulatory and Restrictive Covenants for Land Use Agreement.

Compliance by Building

All compliance monitoring is a building issue. Records must be kept by building and by unit number; not by project or in alphabetical order.

Identifying a Building

Each LIHTC building in a project receives a separate IRS Form 8609 and is assigned a Building Identification Number (BIN). The first two letters represent the state of allocation, the next two numbers represent the year the owner applied for the credits, the next three numbers represent the order in which the application was received, and the last two are the building number (WV-00-000-00).

Project Composition

A LIHTC project may have both tax credit units (low-income units) and market rate units (unrestricted rent units). The number of LIHTC units in a project can be found in the Regulatory and Restrictive Covenants for Land Use Agreement.

The income eligibility and rent restrictions only apply to the low-income units.

Qualified Low-Income Housing Tax Credit Unit

A low-income unit qualifies for the tax credit when the following conditions are met:

- Tenant eligibility verified and certified,
- Restricted rent,
- Non-transient residency,
- Unit suitable for occupancy,
- Tenant eligibility
- Available to the general public on a non-discriminatory basis

Income Limits

The IRS requires project owners to use income limits published by the Department of Housing and Urban Development (HUD), adjusted for family size, to be used when determining eligibility of LIHTC tenants at move-in. The minimum set-aside election establishes whether the fifty (50) or sixty (60) percent area median gross income limit applies to the project's credit units. When new income limits are published they are to be implemented within forty-five (45) days.

Determining Eligibility – The Application

Potential tenants for low-income rent-restricted units should be advised early in the application process that there are maximum income limits that apply to tax credit units. Potential tenants should understand that the anticipated gross income for all persons eighteen (18) years of age or older and unearned income of minor children expecting to occupy the unit must be included and verified on a **Tenant Income Certification** form (TIC) prior to occupancy and annually thereafter.

Before a tenant takes occupancy, owners/property managers must determine that the household will cause the unit to be a qualified housing tax credit unit. This is known as the initial Certification. Each year, thereafter, a recertification must be performed to ensure continued compliance. This is known as the Annual Recertification.

The certification consists of:

- A written application, signed and dated by all household members

- Third party verification of all sources of income and assets,
- A calculation of annual income by the owner/property manager,
- Any forms and documents necessary to qualify the family under the full-time student rule, if applicable,

Determining Annual Income

According to 26 CFR Part 1, Section 1.42-5 for the LIHTC Program, Resident income is calculated in a matter consistent with the determination of annual income under Section 8 of the United States Housing Act of 1937 (Section 8), not in accordance with the determination of gross income for federal income tax liability.

Annual income is the amount of gross income anticipated to be received by all adult members of the household (18 years of age and older, including full-time students), and unearned income of minor children during the twelve (12) month period following the date of certification.

Annual income includes amounts derived (during the 12-month period) from assets to which any member of the family has access.

Annual income is the amount of income that is used to determine a family's eligibility for assistance. Annual income is defined as:

- All amounts, monetary or not, that go to or are received on behalf of the family head, spouse, or co-head (even if the family member is temporarily absent) or any other family member; or
- All amounts anticipated to be received from a source outside the family during the twelve (12) month period following admission or annual recertification.

Refer to HUD Handbook 4350.3 REV-1, Change 4 for complete list of income inclusions and exclusions.

Verifying Annual Income and Assets

All anticipated sources of income and assets must be verified directly from a third party. The project owner/management company/site manager must receive verification prior to the execution of the TIC and lease. Verification required, at a minimum, must:

- Verify the anticipated earned income of every prospective household member eighteen (18) years of age or older including foster adults,

- Verify unearned income, assets, and asset income from all household members, including minors and foster children/foster adults,

Third-party verifications are valid for one-hundred and twenty (120) days following receipt. Owners may not rely on verifications that are more than 120 days old. After that time, a new written verification must be obtained.

An authorization to release information must be signed by the applicant/tenant and must accompany the request.

Recertification

Section 42 requires that the household income of residents in qualifying units be recertified annually. Therefore, during the initial 15 year compliance period, at least once every three-hundred and sixty five (365) days from a household's last income certification date, management must complete an income recertification for the household.

During the Extended Use Period in years 16-30 management must do an initial income certification at move-in. Upon the household reaching the second year of occupancy only a self-certification is required using the approved form located on the Fund's website.

The Fund **does not and will not** issue a Recertification Waiver.

Live-in-Aide

A live-in-aide is a person who resides with one or more elderly persons, near-elderly persons, or persons with disabilities, and who:

- Is determined to be essential to the care and well being of the person(s),
- Is not obligated for the support of the person(s), and
- Would not be living in the unit except to provide the necessary supportive services.

A relative of the household may be considered to be a live-in-aide if they meet the above requirements.

Rent Requirements

The IRS requires Project Owners to restrict rents for qualified Tax Credit units. Project owners are required to implement the new rent limits within forty-five days. However, owners may not increase the rent payable by a tenant unless it serves the tenant with a written notice advising them of the increase thirty (30) days before the first rental increase.

Maximum Gross Rent

Under IRC 42(g)(2)(A) a unit qualifies as an LIHTC unit when the gross rent does not exceed thirty (30) percent of the imputed income limitation applicable to such unit.

Gross rent does not include any housing assistance payments made to an owner to subsidize a tenant's rent; such as Section 8. Only the actual rent paid by the tenant, including tenant-paid utilities, is counted toward the maximum gross rent allowable.

Utility Allowances

In order to qualify as a "rent-restricted unit" within the meaning of section 42(g) of the Code, the gross rent for such unit must not exceed 30 percent of the applicable income limitation. Failure to qualify as a rent restricted unit may result in ineligibility for the section 42 credit, reduction in the amount of the credit, and/or recapture of previously allowed credits. For this purpose, gross rent includes the cost of any utilities, other than telephone. If any utilities are paid directly by the tenant, section 42(g)(2)(B)(ii) requires the inclusion in gross rent of a utility allowance determined by the Secretary, after taking into account the procedures under section 8 of the United States Housing Act of 1937.

Regulations will provide that the owner of a HUD-regulated building--a building whose rents and utility allowances are reviewed by HUD on an annual basis -- must use HUD utility allowances. For other buildings occupied by one or more tenants receiving HUD rental assistance payments ("HUD tenant assistance"), an owner must use the applicable Public Housing Authority (PHA) utility allowances established for the Section 8 Existing Housing Program. A building owner must apply USDA utility allowances to any rent-restricted unit in a building where either the building or any tenant receives USDA housing assistance. If a building is both HUD-regulated and USDA assisted, then USDA utility allowances must be used. Similarly, all low-income tenants receiving HUD rental assistance are subject to USDA utility allowances where the building or any other tenant in the building receives USDA assistance. For example, a low-income building receiving assistance under USDA section 515 shall use Exhibit A-5 of USDA Instruction 1944-E (or a successor method of determining utility allowances), regardless of whether the building is HUD regulated or any low-income tenant in the building receives HUD rental assistance. These rules

will apply only for the purposes of section 42(g), and will not apply to the use of utility allowances by HUD or USDA for their own internal purposes.

Regulations will also provide that a building owner must use the applicable Public Housing Authority (PHA) utility allowance for a building where there is neither (1) HUD tenant assistance, nor (2) an applicable HUD or USDA utility allowance. In these cases, any interested party (e.g., a low-income tenant, building owner, or state housing authority) may obtain a letter from a local utility company providing the estimated cost of that utility for each unit of similar size and construction for the geographic area in which the low-income building is located. An interested party may obtain a letter from the local utility company at any time during the building's 15-year compliance period. Costs incurred in this process must be borne by the initiating party. The interested party must furnish a copy of the letter to the owner of the building and should retain the original. If the utility estimates provided by the local utility companies differ from the utility allowances provided by the PHA, the utility company estimates shall be used in calculating the gross rent limitation. If the utility estimates provided by the local utility companies are higher for one or more rent-restricted units, the building owner must adjust the rents of any rent-restricted unit where failure to do so would result in a violation of the gross rent limitation of section 42(g)(2). Finally, if at any time during the building's 15-year compliance period the building or a low-income tenant (1) becomes subject to HUD or USDA utility allowances, or (2) receives HUD tenant assistance, all rent-restricted units in the building become subject to the appropriate HUD, USDA, or PHA utility allowance.

These allowances shall apply throughout the building's 15-year compliance period and shall be updated at the time rents are revised. A building owner who must apply a new utility allowance during the 15-year compliance period because a building or tenant receives HUD or USDA assistance, or because local utility company estimates become applicable, must use such new utility allowances to compute gross rents of rent-restricted units paid 90 days after the date of occupancy of the federally-assisted tenant or 90 days from the post date of the last utility company estimate. These utility allowances shall also be updated when rents are revised.

In all cases, rent paid for occupancy after the deadline for applying the correct utility allowance must reflect the correct utility allowance. If application of the correct utility allowance results in a violation of the gross rent limitation of section 42(g)(2) for any low-income tenant, then the building owner must adjust that tenant's rent to claim a credit for the unit occupied by that tenant.

Compliance Monitoring Procedures

The Fund is responsible for establishing compliance monitoring procedures for the entire period of affordability and for reporting any incidences of non-compliance to the IRS during the initial 15-year compliance period. Compliance with tax credit regulations is ultimately the responsibility of the Owner. The Owner will be liable for consequences of non-compliance regardless of the Owner's reporting or the Fund's compliance procedures.

Monitoring each project is an ongoing activity that extends throughout the Credit compliance period; which could be forty-five (45) or more years.

The Fund's monitoring responsibilities include:

- Review the Annual Owners Certification of Continued Compliance,
- Review the annual Resident and Income Report,
- Conduct on-site monitoring for all properties, at least once every three years
- Notify the IRS of non-compliance

The Fund must verify at least annually, for the preceding twelve (12) month period the following areas:

Annual Owners Certification

Annually the project owner is required to submit an Annual Owners Certification and a unit history report for all tax credit units. The unit history report is for the previous year and is to be submitted to the Fund by February 15 each year. This information is required by law, so it is very important the information submitted is timely and accurate. Failure to submit on time, incomplete submissions, or inaccurate submission may be determined non-compliant.

Minimum Set-Aside

The project met the requirement of the 20-50 test or the 40-60 test whichever was applicable to the project by December 31 of the first year credits are claimed.

Applicable Fraction

Confirmation that there was no change in the applicable fraction of any building in the project, or that there was a change, there is a description for the change.

Eligible Basis

There was no change in the eligible basis of any building in the project, or if there was a change, the nature of the change (a common area has become commercial space, or a fee is now charged for a tenant facility formerly provided without a charge).

Vacant Units

If a low-income unit in a building becomes vacant during the year, that reasonable attempts were or are being made to rent that unit or the next available unit of comparable or smaller size is rented to tenants having a qualifying income before any units in the project were or will be rented to tenants not having a qualified income. Unless the project is a one-hundred (100) percent low-income project; then all units must be rented to income qualified tenants.

Next Available Unit Rule

If the income of tenants of a low-income unit in the project increased above the limit allowed in section 42, the next available unit of comparable or smaller size in the building if the election was made on the 8609 to not include all buildings as a project and project if the 8609 elected to treat the building as a multiple building project was or will be rented to tenants having a qualified income.

Non-Transient Units

All low-income units in the project were used on a non-transient basis.

Extended Use Agreement

The Extended Use Period (IRC 42(h)(6)(D)) restricts the eligibility of developments to receive an allocation of Tax Credits to only those developments that agree to keep the property income and rent restricted for an extended period. The term for this period is a minimum of 15 years in addition to the normal 15-year compliance period. This results in a total term of compliance period of 30 YEARS.

Units

Confirm that all units in the project were for use by the general public, including the requirement that no finding of discrimination under the Fair Housing Act occurred for the project. See the On-Site Inspections section for details regarding unit inspections.

Suitability

The buildings and all low-income units in the project were suitable for occupancy, taking in to account local health, safety, and building codes (or other habitability standards). That the State

or local government unit responsible for making local health, safety and building codes did not issue a violation.

On-Site Inspections (Every three years)

By December 31 of the second year after the last building places in service and at least once every three years thereafter. The Fund will audit twenty (20) percent of the files, inspect twenty (20) percent of the units, and inspect all of the common area in all buildings. The Fund will randomly select which low-income units and tenant records are to be inspected by the Fund. The units to be inspected must be selected in a manner that will not give owners of low-income housing projects advance notice that a unit will or will not be inspected.

The Fund will give an owner reasonable notice; at least thirty days (30) that an inspection of buildings and low-income units will occur. It is the responsibility of the project owner to notify tenants of the site inspection.

The Fund must verify that all units in the project were for use by the general public, including that there were no findings of discrimination under the Fair Housing Act for the project.

The Fund must inspect LIHTC projects to ensure the buildings and low-income units were suitable for occupancy, taking into account local health, safety, and building codes (or other habitability standards). If a violation report or notice was issued by the government unit, the owner must attach a statement summarizing the violation report or notice or a copy of the violation report or notice to the annual owner's certification submitted to the Fund. In addition, the owner must state whether the violation has been corrected.

The Fund must also determine whether the buildings and units satisfy the uniform physical condition standards (**UPCS**) for public housing. The UPCS does not supersede or preempt local health, safety, and building codes.

The UPCS requires housing to be decent, safe, sanitary and in good repair. The major areas of consideration include:

- The site (fencing, walls, grounds, mailboxes, etc.),
- Building exterior (structurally sound, secure, etc.),
- Building systems (domestic water*, electrical systems, elevators, etc.),
- Residential units (bathroom, ceiling, doors, etc.),
- Common areas (basement, garage, restrooms, etc.),

- Health and safety concerns (air quality, electrical hazards, fire exits, etc.)

*The unit **must** have hot and cold running water, including an adequate source of drinkable water.

Health and safety violations can be divided into non-life-threatening and exigent, life safety conditions. Exigent health and safety and fire hazards require immediate attention because of their life-threatening potential. Evidence must be provided to the Fund within seventy-two (72) hours of the review, to ascertain that the life-threatening issues have been corrected.

The Fund will perform on-site inspections of any low-income housing project through the end of the extended use period once every three years. No waiver will be issued by the Fund to opt out of the requirement.

Notification and Correction of Compliance Exceptions

The Fund will notify, within thirty (30) days, via written notice to the owner of a low-income housing project if the Fund discovers by inspection, review, or some other manner that the project is not in compliance with the provisions of section 42. The notification letter establishes and documents the beginning of the correction period for any “out of compliance” issues.

The Fund will allow the project owner ninety (90) days to provide clarification or document that issues of non-compliance have been addressed. If additional time is needed to correct issues, the project owner may request an extension of time, up to a total of six (6) months. The request must be sent to the Compliance Monitoring Administrator. Upon receipt of the response the Fund will determine whether the project was always in compliance, has corrected non-compliance, or remains out of compliance.

Regardless, of whether the owner remedies the non-compliance or remains out of compliance, an IRS Form 8823 must be filed with the IRS. A copy of the IRS Form 8823 will be provided to the project owner.

Record Keeping – The Project

The owner is responsible for proper administration of the project, including the Code requirements that resident income and rent records be kept and maintained for each building in the project for the compliance period.

The Code requires owners to maintain the records necessary for the Fund to conduct a compliance monitoring review and for the IRS to conduct an audit. Owners must maintain records for the first year of the credit period for a minimum of twenty-one (21) years, and records

for all other years in the fifteen (15) year compliance period for a minimum of six (6) years following each year's end. The records must include:

- The total number of residential rental units in the building (including the number of bedrooms and the size in square feet of each residential unit),
- The percentage of residential rental units in the building that are low-income units,
- The rent charged on each residential rental unit in the building and the applicable utility allowance,
- The number of occupants in each low-income unit,
- The number of low-income vacancies in the building,
- The annual income certification of each eligible resident with documentation
- Documentation to support each low-income tenant's income certification (a copy of the tenant's federal income tax return, Forms W-2, or verification of income from third parties)
- The eligible basis and qualified basis of the building at the end of the first year of the credit period,
- The use of the non-residential portion of the building included in the project's eligible basis

The property should also have a copy of:

- The Regulatory and Restrictive Covenants for Land Use Agreement,
- A copy of all fully executed 8609's for each building in the project,
- Any utility allowance updates and revisions,
- Documentation to support that the building complies with any statutory set-asides or Qualified Action Plan requirements.

Compliance Monitoring Fees

The Fund is authorized to charge a fee to cover the cost of the monitoring. The fee, per unit, will be determined by the Asset Management and Technical Services Department of the Fund. The current fee is \$35 per low income unit. Monitoring fees are to be paid annually each year of the compliance period and the extended use period. Annually, the Fund will issue each project owner an invoice with the amount due.

Resources:

Regulatory Organizations

- **Internal Revenue Service**

www.irs.gov

George R. Lydford

Senior Program Analyst, LIHC & ACA

Examination Quality & Technical Support

- **Phone: (480)503-7287**

- **Quick Links**

- Audit Technique Guides

www.irs.gov/businesses/small/article/0,,id=108149,00.html

- Private Letter Rulings

www.irs.gov/app/picklist/list/writtenDeterminations.html

- Internal Revenue Bulletins

www.irs.gov/irb/

- Tax Code, Regulations and Official Guidance

www.irs.gov/taxpros/article/0,,id=98137,00.html

- **Department of Housing and Urban Development (HUD)**

(202) 708-1112

451 7th Street S.W., Washington, DC 20410

www.hud.gov

- **Quick Links**

- Fair Housing Laws & Executive Orders

www.hud.gov/offices/ftheo/FHLaws/index.cfm

- Handbooks, Notices and Special Directories

www.hud.gov/offices/adm/hudclips/index.cfm

- Home Program

www.hud.gov/offices/cpd/affordablehousing/programs/home/

- Housing Research and Data Sets

www.huduser.org/portal/

- Income Limits:

- HOME Program
www.hud.gov/offices/cpd/affordablehousing/programs/home/limits/income/
 - HUD Programs
www.huduser.org/portal/datasets/il.html
 - MTSP Programs
www.huduser.org/portal/datasets/mtsp.html
 - LIHC Database
www.huduser.org/portal/datasets/lihlc.html
 - Qualified Census Tracts & Difficult Development Areas
www.huduser.org/portal/datasets/qct.html
- **Rural Housing Service (RHS)**
(202) 720-9619
U.S. Department of Agriculture, Room 5014, South Building, 14th Street and Independence Avenue, S.W., Washington, D.C. 20250
www.rurdev.usda.gov/rhs/
 - **Quick Links**
 - Income and Housing Eligibility
eligibility.sc.egov.usda.gov/eligibility/welcomeAction.do
 - Income Limits
www.rurdev.usda.gov/HSF-Guar_Income_Limits.html
 - Local RD Office Locator
offices.sc.egov.usda.gov/locator/app?state=us&agency=rd

Important Code References

- **IRC Section 42**
- **Handbooks**
 - 8823 Guide
 - HUD Handbook 4350.3 REV-1, Changes 1, 2 & 3
- **Treasury Regulations 1.42**
 - 1.42-1 Reserved
 - 1.42-1T Limitation on Credits Allowed
 - 1.42-2 10 Year Rule
 - 1.42-3 Treatment of Buildings Financed with Loan Proceeds Under FIRREA
 - 1.42-4 Not-for Profit Material Participation
 - 1.42-5 Monitoring Compliance

- 1.42-6 – 1.42-12 Carryover Allocations
- 1.42-13 Agencies Correction of Administrative Errors
- 1.42-14 Allocation Rules for Post-1989 State Housing Credit Ceiling Amounts
- 1.42-15 Available Unit Rule
- 1.42-16 Eligible Basis Reduced by Federal Grants
- 1.42-17 Qualified Allocation Plan

Glossary:

4 Percent Credit

The 4 percent credit is the credit percentage available for existing housing or for federally subsidized new construction or rehabilitation (30 percent credit).

9 Percent Credit

The 9 percent credit is the credit percentage available for new construction or rehabilitation (70 percent credit).

15-40 Test

See Deep Rent Skewing Set-Aside.

20-50 Test

The 20-50 test is a minimum set-aside test used to determine if a building is a qualified low-income housing project. Under the test, a building is generally a qualified low-income building if at least 20 percent of the units are both rent restricted and are occupied by tenants whose income is less than or equal to 50 percent of area median gross income.

40-60 Test

The 40-60 test is a minimum set-aside test used to determine if a building is a qualified low-income housing project. Under the test, a building is generally a qualified low-income building if at least 40 percent of the units are both rent restricted and are occupied by tenants whose income is less than or equal to 60 percent of area median gross income.

- A -

Acquisition Cost

Acquisition cost is the cost of acquiring an existing building.

Acceleration

Acceleration is a provision included in many of the bond documents requiring the immediate payment of all the bond principal, generally caused by the borrower's default.

Adjusted Basis

Adjusted basis is the cost basis of a building adjusted for capital improvements minus depreciation allowable.

Adjusted Investor Equity

Adjusted investor equity is the aggregate amount of cash taxpayers invested increased by cost-of-living adjustment.

Applicable Federal Rate (AFR)

Applicable federal rate is a short term, mid-term and long-term debt rate that is redetermined on a monthly basis.

Applicable Fraction

Applicable fraction is the percentage of a building that is treated as low-income use and generally eligible for the LIHC. The applicable fraction is the lesser of the unit fraction or the floor space fraction.

Applicable Percentage

Applicable percentage describes the technical term for the credit percentage that a qualified low-income housing project is eligible for.

Arbitrage Yield Restriction

Arbitrage occurs when tax-exempt bond proceeds are invested in securities that yield a greater return than the interest charged on the bonds. Restrictions exist on the amount of arbitrage bonds can earn without putting the tax-exempt status of the bonds in peril. In instances where the restriction is violated, exceptions exist that allow for the tax-exempt status of the bonds to remain intact.

Area Median Gross Income (AMGI)

Area median gross income is the gross income level that half the families in an area are below.

At-Risk Rule

The at-risk rule is the rule that limits the ability to include in eligible basis property purchased with nonrecourse financing. An exception exists for nonrecourse financing that meets the definition of Qualified Commercial Financing.

- B -

Balloon Payment

A balloon payment is a single future payment of the entire bond principal when the borrower makes periodic interest-only payments.

Basis Point

A basis point is one-one-hundredth of a percentage point (.01%).

Below Market Federal Loan

A below market federal loan is any loan funded by federal funds if the interest rate payable on such loan is less than the applicable federal rate.

Bond Counsel

Bond counsel is the attorney representing the bond issuer and bondholders. The attorney provides an opinion that the interest on the bonds is exempt from federal taxation. He/she is responsible for the bond inducement resolution, bonds, the bond indenture, the financing agreement, the regulatory agreement and the tax opinion.

Bond Issuance Costs

Bond issuance costs are the costs incurred to issue the bonds, including legal fees, underwriting fees, rating agency fees, trustee fees, printing, etc.

Bond Issuer

A bond issuer is the governmental or non-profit entity responsible for issuing bonds.

Bond Purchase Agreement

A bond purchase agreement is an agreement between the borrower, issuer and underwriter allowing the underwriter to sell the bonds, subject to responsibilities, warranties, and agreements agreed to by the issuer.

Bond Trustee

The bond trustee is responsible for collecting the interest and principal payments and forwarding these payments to bondholders. The trustee invests the bond proceeds, as applicable, and administers the indenture agreement.

- C -

Call Premium

A call premium is a payment made to the bondholder if the borrower pays off the bonds before they mature.

Call Protection

Call protection describes the provisions in a bond issuance that preclude the borrower from prepaying the bonds for a specified period of time.

Comfort Letter

A comfort letter is a letter provided by a certified public accountant when the bond purchase agreement is executed. This letter confirms that the issuer's (or borrower's) financial information included in the official statements is presented in conformity with generally accepted auditing standards and that no changes in the financial position of the borrower since the date of the last audited financial statements, other than those changes disclosed in the comfort letter or in the official statement, have occurred.

Compliance Period

The compliance period is the 15 year period over which a project must continue to satisfy the various LIHC requirements in order to avoid tax credit recapture. The compliance period begins with the first taxable year of the credit period.

Constitutional Home Rule Subdivision

Constitutional home rules subdivision describes a political subdivision with home rule powers under the state constitution. These subdivisions receive special treatment under the LIHC state allocation rules.

Credit Enhancer

The credit enhancer guarantees, for a fee, that the bondholders will receive scheduled bond payments.

Credit Period

The credit period is the 10-year period over which the LIHC is claimed. This period generally begins on the date a property is placed in service, but a taxpayer may elect to start the credit period as of the beginning of the year following the year the LIHC property is placed in service.

Credit Recapture Amount

Credit recapture amount is the amount of credit that is recaptured upon disposition of the LIHC project during the compliance period. The maximum recapture is two-thirds of the previously claimed credit and an interest charge applies.

- D -

Deep Rent Skewing Set-Aside

Deep rent skewing set-aside is a special set-aside test that applies for purposes of determining if existing tenants qualify as low-income tenants. This special test is elective and must be met in addition to the general set-aside test (i.e. 20-50, 40-60 and 25-60).

Defeasance

Defeasance describes the retirement of bonds through the issuance of new bonds.

Difficult Development Area

A difficult development area is any area designated by the U.S. Department of Housing & Urban Development, which has high construction, land or utility costs relative to area median gross income.

- E -

Eligible Basis

Eligible basis is a component of the qualified basis of an LIHC project. It is generally equal to the adjusted basis of the building, excluding land but including amenities and common areas.

Existing Building

An existing building is a building that has been previously placed in service.

Extended Low-Income Housing Commitment

An extended low-income housing commitment is any agreement between the taxpayer and the housing credit agency that extends the low-income housing requirements for a full 30 years.

Extended Use Period

The extended use period is the period beginning on the first day that the building is part of a qualified low-income housing project and ending on the date specified by the agency or 15 years after the close of the compliance period.

- F -

Federally Assisted Building

A federally assisted building is any building that is substantially assisted, financed or operated under laws in effect the date of enactment of the Tax Reform Act of 1986.

Federally Subsidized

Federally subsidized is a term used to describe a building that is financed with a below-market federal loan or with a loan for which the interest income earned by the holder of the loan is exempt from tax under Internal Revenue Code Section 13.

Financing Agreement

The financing agreement is entered into between the bond issuer, trustee and borrower. The agreement covers how the bonds will be issued, serviced by the trustee and paid for by the borrower.

Float

Float is interest earned on bond payments made to the trustee that have yet to be remitted to the bondholders. The borrower generally makes debt service payments monthly while bondholders are paid semi-annually. The interest reduces the amount the borrower has to pay to service the bonds, effectively reducing the interest rate.

Floor Space Fraction

The floor space fraction is obtained by dividing the total floor space of the low-income units in the building by the total floor space of all residential units in the building (whether or not occupied).

- G -

Grant

A grant is funds received from a private foundation or charitable group, federal, state or local government that do not have to be repaid.

Gross Income

Gross income is all income from whatever source derived, including the value of property or services as well as cash.

Gross Rent

Gross rent excludes any amounts received from a rental assistance program, utility allowance or fee paid to the owner of the unit owner by any governmental assistance program.

- H -

Housing Credit Agency

The housing credit agency is a state or local housing agency that has the authority to allocate and commit federal low-income housing tax credits to a building.

- I -

Imputed Income Limitation

The imputed income limitation would apply to a unit based on an assumed family size that is a function of the number of bedrooms in the unit.

Indenture

The indenture is an agreement between the bond issuer and the trustee containing the terms and procedures for payment of the bonds.

Inducement Resolution

An inducement resolution is the resolution passed by the bond issuer communicating the intent to issue bonds for a specific activity.

- L -

Low-Income Occupancy Percentage

See Applicable Fraction.

Low-Income Unit

A low-income unit is (1) rent restricted and (2) has individuals occupying it who meet the income limitation applicable under the elected minimum set-aside test.

- M -

Mandatory Redemption

Mandatory redemption is a provision allowing a borrower to prepay bonds regardless of call provisions, due to special circumstances (e.g. foreclosure or condemnation).

MBS Trustee

The MBS trustee holds the MBS that collateralize the bonds. The MBS trustee remits the proceeds from the MBS to bond trustee, who then pays the bondholders.

Minimum Set-Aside Test

The minimum set-aside test is generally used to determine if a building is a qualified low-income housing project. There are three different minimum set-aside tests with varying applicability. The tests are 20-50 test, the 40-60 test, and the 25-60 test. (See 20-50 test, 40-60 test and 25-60 test).

Mortgage Backed Security (MBS)

Mortgage Backed Security is collateral provided by credit enhancers that is used to guarantee the bonds.

- N -

Negative Arbitrage

Negative arbitrage occurs when undisbursed bond proceeds earn a lower interest rate than the bond interest rate.

New Building

A new building is a building whose original use begins with the taxpayer. A new building also includes qualifying substantial rehabilitation costs incurred with respect to existing buildings.

Nonqualified Nonrecourse Financing

Nonqualified nonrecourse financing is nonrecourse financing that is not qualified commercial financing. This definition is used for purposes of low-income housing tax credit at-risk rules.

Nonqualified Substantial Improvement

Nonqualified substantial improvement is a term used to determine if an existing building is eligible for the acquisition credit; is any substantial improvement for which Section 167 (k) was elected or pre- 1986 Tax Reform Act depreciation rules apply.

- O -

Official Statement

The official statement is a marketing prospectus used by underwriters to sell the bonds. The official statement summarizes the terms of the bonds and other information relevant to the investment decision.

- P -

Placed-In-Service Date

The placed-in-service date generally marks the beginning of the credit period. It is defined as the date the property is ready for occupancy.

Pledge

The pledge grants a security interest or lien to provide security for the repayment of the bond principal and interest.

Private Placement

Private placement is the sale of bonds directly from a bond issuer to an investor without the use of an underwriter. An investment banker may act as a placement agent in this type of transaction.

Private Placement Memorandum

A private placement memorandum is a document used in connection with a private placement transaction, instead of the official statement,

- Q -

Qualified Basis

Qualified basis is the base that is multiplied by the credit percentage to determine the annual credit. The qualified basis equals the applicable fraction times the eligible basis.

Qualified Census Tract

A Qualified Census Tract is any census tract in which 50 percent or more of the households have an income which is less than 60 percent of area median gross income.

Qualified Commercial Financing

Qualified commercial financing is the exception to the at-risk rules. To qualify, financing must generally be nonrecourse, the lender must generally be actively engaged in the business of lending, the lender must not have previously owned the property, and the lender must not earn a fee in connection with the acquisition of the property.

Qualified Contract

A qualified contract is a bona fide contract to acquire a LIHC project for the sum of the existing debt, adjusted investor equity and other capital contributions, less project cash distributions.

Qualified Low-Income Building

A qualified low-income building is part of a qualified low-income housing project throughout the compliance period and for which prior law depreciation rules do not apply.

Qualified Low-Income Housing Project

A qualified low-income housing project is a residential rental project that satisfies the elected minimum set-aside test.

Qualified Non-profit Organization

A qualified non-profit organization, which is described in Section 501 (C)(3) or (4), is exempt from tax under Section 501(a). Its exempt purpose is to foster low-income housing, among other purposes.

- R -

Rating Agency

A rating agency determines or "rates" the investment risk of bonds. Examples include Standard & Poor's and Moody's Investors Service.

Rebate

A rebate is payment of the excess arbitrage proceeds to the federal government to retain the tax-exempt status of the bonds. Special rules allow a borrower to avoid a rebate of arbitrage proceeds.

Regulation D

Regulation D is a securities law regulation that explains the rules for three private offering exemptions from the general rules that requires securities registration.

Regulatory Agreement

A regulatory agreement is an agreement entered into between the borrower, bond issuer and trustee specifying the income rent and income restrictions a project owner must comply with for the bonds to retain their tax-exempt status.

Rehabilitation Expenditures

Rehabilitation expenditures are amounts incurred in improving or making additions to property in connection with the rehabilitation of an existing building.

Rent-Restricted Unit

A rent-restricted unit is a unit for which the rent charged to tenants is limited to 30 percent of the income limitation applicable under the elected minimum set-aside test.

- S -

Scattered Site Project

A scattered site project is a qualified low-income housing project located on multiple sites.

Secondary Market

The secondary market is the subsequent sale of bonds from bondholder, after the original sale of the bonds by the bond issuer.

Section 167(k) Election

Section 167(k) is any election available before the Tax Reform Act of 1986 which allowed building owners to amortize rehabilitation costs over 60 months.

State Housing Credit Ceiling

The state housing credit ceiling is the maximum LIHC amount a state may allocate in a given year. It is calculated at \$1.75 per resident.

Substantial Improvement

Substantial improvement is used in connection with determining the eligibility of an existing building for the LIHC. It is any amount incurred during a 24-month period equal to or exceeding 25 percent of the adjusted basis of the building as of the first day of such period.

Supportive Service

Supportive service is any service provided under a planned program of services designed to enable residents to remain independent and avoid placement in a hospital, nursing home or intermediate care facility.

- T -

Tax Shelter Registration

Certain partnerships or other investments with significant tax benefits must register as tax shelters with the Internal Revenue Service and certain state tax agencies.

TEFRA Hearing

The Tax Equity and Fiscal Responsibility Act (TEFRA) Hearing is the bond issuer's public notice, public hearing and approval by elected officials of a bond issuance.

- U -

Underwriter

The underwriter is an investment bank that underwrites and markets the bonds to investors.

Underwriter's Counsel

Underwriter's counsel is an attorney who verifies that the documents used to market the bonds comply with the applicable securities regulations.

Unit Fraction

The unit fraction is the fraction obtained by dividing the number of low-income units in a building by the total number of units in the building (whether or not occupied).

Utility Allowance

The utility allowance is the amount, determined by the Secretary of the Department of the Treasury, to be the average cost of tenant utilities.

- V -

Volume Cap

The volume cap is the maximum amount of LIHCs and tax-exempt bonds each state is allowed to allocate annually. The tax credit volume cap is \$1.75 per state resident. The bond volume cap is \$75 per person per state, with a \$225 million minimum per state. Beginning in 2003, the volume cap will be indexed to inflation