**FEDERAL (LIHTC) HOUSING CREDIT &**

**VERMONT STATE HOUSING CREDIT**

**PROGRAM OVERVIEW**

A. **Introduction**

The Federal Housing Credit (“HC”) is a "tax vehicle" designed by Congress to assist in the creation and preservation of affordable rental housing for low-income households. It provides a direct cost-based reduction in federal tax liability over a 10-year period for owners of qualifying rental housing who agree to conform to certain operating restrictions for at least a 15-year period. The Tax Reform Act of 1986 (and succeeding revisions of that law) set a maximum Housing Credit allocation for each state based on population.

The Vermont Affordable Housing Tax Credit, or State Credit, was established in 2000. It is utilized with the Federal Housing Credit and is taken over a five-year period. The annual amount of State Credit is set by Statute. The Allocation Plan governs the allocation of State Credits as well as federal Housing Credits. This application is used to apply for both types of credit.

B. **Caveats**

The HC program has become increasingly complex. While VHFA has been given certain programmatic authority and responsibility by Congress and the Governor’s Office, knowledge of and compliance with the HC program is ultimately the responsibility of the applicant/taxpayer. Primary enforcement responsibilities lie with the Internal Revenue Service. The IRS also requires that VHFA implement fairly rigorous compliance monitoring procedures. Applicants are strongly encouraged to seek competent legal and/or accounting assistance in fulfilling their responsibilities under this program.

VHFA is charged with allocating Housing Credits, in compliance with an adopted Allocation Plan, to eligible projects in only those amounts necessary to make the selected developments economically feasible. These decisions shall be made solely at the discretion of VHFA, but VHFA in no way represents or warrants to any sponsor, investor, lender, or others that the project is in fact eligible, feasible, viable, or in compliance either before or after the final allocation decision. VHFA makes no representations to the owner or anyone else as to compliance with the Internal Revenue Code, Treasury regulations, or any other laws or regulations governing the HC program.

VHFA's review of documents submitted in connection with this allocation is for its own purposes. However, applicants should understand that any information submitted to VHFA as part of an HC application is public information under Vermont law.

No member, officer, agent, or employee of VHFA shall be personally liable concerning any matters arising out of, or in relation to, the allocation of the Housing Credits.

C. **Program Requirements**

Regulations require VHFA to have a compliance monitoring process for all Housing Credit projects for at least 15 years.

The Federal Department of Housing and Urban Development (HUD) also issued Subsidy Layering Review rules in 1991 which affect HC applications in cases where HUD is being asked to contribute project-based Section 8 certificates, HUD mortgage insurance, or some other direct HUD based subsidy. Congress has now given state credit agencies authority to administer these rules.

Applicants should review the Qualified Allocation Plan (QAP) for additional information.

2. In addition to the existing 15-year compliance period for the rent-restricted units, owners must sign a recordable extended use covenant that extends the restrictions in perpetuity. Also, the owner must provide a Right of First Refusal to a qualified non-profit or VHFA (or its assignee) that can be exercised at year 15 of the compliance period. This Right of First Refusal must be for a price described in the Allocation Plan that will help assure long-term affordability for low-income tenants.

3. VHFA must adopt a formal statewide Allocation Plan, after a public hearing process. The Allocation Plan states the priorities and other evaluation criteria to be used by VHFA in judging applications. VHFA must make a good faith effort to ensure that the amount of any HC allocation does not exceed that necessary for the financial feasibility of the development and must consider the reasonableness of development costs and operating expenses in determining the amount of Housing Credits to issue. The result is that comprehensive financial and sponsor information must be submitted and evaluated by VHFA as part of the allocation process.

4. CDBG funds can be included in the eligible basis when using the 9% credit. HOME funds, however, are eligible for either the 4% credit or the 9% credit. An owner can receive the 9% credit for a project receiving HOME funds if the owner elects to restrict 40% of the units to occupancy by households earning 50% of area median income or less. If, however, a property is located in a Difficult Development Area and an owner elects to take the 9% credit, the project is not eligible for the 130% adjustment factor for Difficult Development Areas. However, if the HOME funds are lent to the project at the Applicable Federal Rate (AFR) or higher, the 130% adjustment may be taken.

5. If more than 50 percent of the development financing is tax-exempt, then the HC allocation may come from "outside the cap." This means that VHFA does not make the allocation (the owner files the relevant tax forms directly with the IRS) and the "out-of-cap" allocation does not reduce Vermont's allotted allocation authority. However, these projects must still satisfy the requirements of the Allocation Plan and must be reviewed by the Allocating Agency. These projects are required only to have a 15-year extended use period (a 30-year tax credit compliance period overall).

D. **Housing Credit Options**

There are two levels of Federal Housing Credits - generically known as the 9% credit and the 4% credit.1[[1]](#footnote-1)Selection of the applicable Housing Credit percentage (either 4% or 9%) depends on whether a project is newly con­structed or an existing building, the extent of rehabilit­ation involved, and whether the project is federally subsidized or not. An example of a federal subsidy is VHFA's tax-exempt bond financing.2 [[2]](#footnote-2) In addition, there is the Vermont Affordable Housing Tax Credit.

E. **Calculating the Housing Credit**

The calculation of the dollar amount of credit available is determined in three steps:

1. Determine the eligible basis of a building or project. Eligible basis is generally any cost that is a depreci­able or capital budget item for all other IRS purposes. Land and working capital are two common project costs that are generally excluded from the eligible basis.

2. Determine if the development is in a Difficult Development Area (see map in Appendix A). If so, multiply the eligible basis by up to 130%.

3. Determine the qualified basis of a project. The "qualified basis" of a rental building is that portion of the "eligible basis" of a building that will be rented to low-income households for the initial 15-year period. The minimum number of units in a building or project that must be rented to low-income households are described in Section I. The percentage used must be the lesser of: 1) The number of low-income units/total units; or 2) The floor space square footage of low-income units/total floor space.

4. Multiply the appropriate Housing Credit percentage (e.g. 4% or 9%) times the "qualified basis" of a rental building.

F. **Eligible Project Types**

Most residential rental properties are eligible for the HC Program, with the exception of owner-occupied properties containing 4 or fewer units, nursing homes, hospitals, sanitariu­ms, life care faciliti­es, retirement homes, and mobile home parks. An owner-occupant in a four-unit (or smaller) building may be eligible if he/she acquires or rehabilitates the building in accordance with a state or local government or qualified non-profit organization sponsored development plan of action. Transient housing (i.e. leases less than 6 months) is not permitted unless the facility is an SRO (Single Room Occupancy) or a homeless shelter.

For projects consisting of more than one property, all sites must be con­tiguous, except that a scattered site project is permitted if 100% of the units are rent restricted (i.e. in compliance with the Housing Credit maximum incomes and rents)4.[[3]](#footnote-3).Buildings used in part for rental purposes and in part for other purposes may qualify for the Housing Credit, but only for that portion of the building which con­stitutes the qualifying rental housing.

A building is generally not eligible for the acquisition credits under the HC Program if it has been acquired or substan­tially improved by any party in a 10-year period prior to the HC applica­tion. However, the building may still be eligible for rehabilit­ation credits.

G. **Example of Housing Credit Calculation**

The example below illustrates the value of the credit to a housing sponsor who acquires a 15-unit building for $120,000, expends $200,000 on substantial rehabilitation, and subsequently rents 6 of the units (i.e. 40%) to low-income households.

|  |  |  |  |
| --- | --- | --- | --- |
| **Description** | **Rehabilitation**  **Expenses** | **Acquisition**  **Expenses** | **Total** |
| Development Costs | $200,000 | $120,000 |  |
| Less Land | - 0 | - 20,000 |  |
| Eligible Basis | $200,000 | $100,000 |  |
| Difficult Development Area?  If yes, multiply eligible basis by up to 130% | No | No |  |
| Percent of Low-Income Units | x 40% | x 40% |  |
| Qualified Basis | $ 80,000 | $ 40,000 |  |
| Annual Credit Percentage | x 9% | x 4% |  |
| TOTAL ANNUAL CREDIT | $ 7,200 | $ 1,600 | $ 8,800 |
| Period of Credit (years) | x 10 | x 10 | x 10 |
| Value of Credit | $ 72,000 | $ 16,000 | $ 88,000 |

H. **Placed in Service**

The term "Placed in Service" means that a building is completed and ready to be occupied. The Placed in Service date is typically when a municipality issues a certificate of occupancy. A building must generally be Placed in Service in the same year for which the HC is approved, unless a Carryover Allocation is granted by VHFA (See Section O - Carryover Allocations). Owners must receive an allocation of credits (either a Carryover Allocation or a Final Allocation - IRS Form 8609) for a project in the calendar year in which the last building in the project is Placed in Service. Prior to being able to claim the credit, owners must receive the final allocation of credits (IRS Form 8609). The credit may be claimed either in the year the project is Placed in Service or in the subsequent year.

I. **Tenant Income and Rental Restrictions**

In order to qualify for the program, owners must agree to certain tenant income and rental restrictions, which must be continuously maintained for a 30-year compliance period. Tables showing the current income and gross rent limits for each county are located in the Appendix of this application packet. Income limits (and, thus, gross rent limits) are typically adjusted on an annual basis by HUD.

1. Income Restrictions: The owner must irrevocab­ly elect to reserve a minimum of either:

a. 20% of the building units for occupancy by households at or below 50% of the Area Median Income; or

b. 40% of the units for occupancy by households at or below 60% of the Area Median Income; or

c. Deep Skewing - 15% of the building units for occupancy by households below 40% of Area Median Income. In addition, the market rents cannot exceed the deep skewing rents by more than 300%.

2. Rent Restrictions: The gross rent (including an allowance for utilities) paid by residents in the qualifying units cannot exceed 30% of the maximum qualifying income for a family of an assumed size given the number of bedrooms in the unit. Congress has mandated that there shall be an assumed 1.5 persons per bedroom for this purpose.

The rent limitation applies only to payments made directly by tenants and not to rental assistance payments (e.g. Section 8 certificate) paid on a tenant's behalf.

An increase in a tenant's income may result in a unit ceasing to qualify as occupied by a low‑income household. A tenant who initially qualifies will continue to qualify so long as the tenant's income does not increase to more than 140% of the maximum qualifying income, adjusted for family size. If the tenant's income increases to over 140% of the maximum qualifying income, or the family size decreases so that a lower maximum family income applies, that unit is not in compliance as part of the "qualifying basis." However, no penalty is assessed as long as the next unit of comparable or smaller size that becomes vacant is occupied by qualifying tenants.

A household totally comprised of full-time students does not qualify as an eligible low-income household regardless of income level. However, there are exceptions for married students, TANF recipients, students involved in federal job training programs, and single parent households.

J. **Utility Allowances**

As indicated in the previous Section, utility allowances (shown in Appendix F) are subtracted from the maximum rents (shown Appendix E) that can be paid by residents in qualifying units. 5[[4]](#footnote-4)

The IRS rules regarding utility allowances can be summarized as follows:

1. Owners of HUD regulated buildings must use HUD utility allowances.

1. If the building or any tenant is receiving U.S.D.A. Rural Development (RD)

assis­tance, RD utility allowances must be used.

3. All other owners must use the utility allowances calculated by the Vermont State Housing Authority, unless the local Public Housing Authority has published its own utility allowances. However, any interested party (e.g. owner, tenant, local housing authority) can request a utility cost estimate from a local utility company and this estimate must be used, whether higher or lower. The estimate of the local utility will govern, except for individual units receiving assistance under the HUD Section 8 Certificate or Voucher Program. Units receiving such assistance shall use the utility allowances prepared by the local or state housing authority.

For information about the utility allowances for HUD regulated buildings, contact the HUD Office of Housing, Office of the Deputy Assistant Secretary for Multifamily Housing Programs at (202) 708-2495.

The Vermont State Housing Authority (VSHA) revises their utility allowances once per year, in November. A copy of the most current VSHA utility allowance figures is attached in Appendix F. For additional information, contact Holly Fancher at (802) 828-3020.

The Burlington, Winooski, Hartford, and Springfield Housing Authorities are the only local Public Housing Authorities known to VHFA which publish their own utility allowance figures. The Burlington Housing Authority publishes their utility allowances once a year in June. A copy of the most current Burlington Electric Department utility allowances is attached in Appendix F. For additional information about Burlington utility allowances, contact Claudia Donovan at (802) 864-4650 extension 207.

RD utility allowances are set on a project-by-project basis. Additional information can be secured from Sandra Mercier of Rural Development (RD) at (802) 828-6028.

K. **IRS Reporting Requirements**

The taxpayer must file certifications to the Secretary of the Treasury no later than the 90th day following the close of the first taxable year in the credit period. IRS Forms 8586 "Low-Income Housing Credit" and 8609 "Low-Income Housing Credit Allocation Certifica­tion" (including Schedule A) are the forms to be used for reporting purposes. VHFA will send a completed copy of Form 8609 to the taxpayer after the building is Placed in Service, all eligible costs have been certified by the owner (see Section Q), and a HC Housing Subsidy Covenant has been signed. The original signed Form 8609 is sent directly by VHFA to the IRS. It is the taxpayer's responsibility to obtain and file all the relevant IRS Forms and to seek appropriate accounting and tax advice for reporting and programmatic compliance.

L. **Compliance Monitoring**

VHFA is now required by law to perform program compliance monitoring on all developments that have received the benefit of Housing Credits. IRS regulations mandate that compliance monitoring procedures be set forth in the State Allocation Plan. A compliance monitoring fee should be incorporated into the operating budget. More information can be found on our website.

M. **Application Process and Fees**

The Allocation Plan includes a description of the Application Process. Before an application for ceiling credit is submitted, a pre-application meeting between VHFA staff and the developer is held. The purpose of the meeting is to discuss: the project concept; how compatible the project is with the evaluation criteria in the Plan; assumptions about other funding sources; the compatibility of the use with the proposed site.

Once the initial meeting has taken place, site control has been obtained, and the developer has met with other funding agency staff, the Application can be submitted. The following must be submitted with the application:

* Purchase & Sales Agreement, Option, Deed or other form of Site Control;
* Elevation drawings or computer-generated image of buildings on site, and Site Plan (if project includes new construction) and photographs of building (for rehabs);
* Evidence of meeting with town zoning administrator (for new construction, adaptive re-use, and rehab projects which add units);
* Market Study;
* Capital Needs Assessment (for any rehab project that is not a gut-rehab. For new construction projects and gut-rehab projects, the CNA can be submitted at completion);
* Other documentation (See Submission Timing Chart for detail);
* Application Fee (see detail below).

An Application for Reservation of the Housing Credits is made to VHFA, using the Project and Sponsor Information, the attached HC Submittal Letter along with completed HC Worksheet.Each HC application must include a non-refundable application fee of $250 (due upon submission of the completed application). An additional reservation fee of 4% of the annual credit will be due upon issuance of the Reservation Certificate. The reservation fee will be refundable until the project receives either a Carryover Allocation or Final Allocation, whichever is earliest. These amounts do not include the fees discussed under Section L - Compliance Monitoring.

N. **Vermont Policy Priorities** See the attached Allocation Plan for a listing of Vermont's Policy Priorities.

O. **Carryover Allocations** If a project will not be completed (i.e. Placed in Service) before December 31, of its credit year, VHFA has the authority to grant a Carryover Allocation. The applicant must have spent at least 10% of the owner's ultimate "reasonably expected basis" (depreciable real basis plus land) in the project by the end December and have a real ownership interest in the land and/or buildings. If a project receives a carryover allocation based on an award of credits that occurred in the second half of the calendar year (i.e. after July 1), the Sponsor has 6 months from the date of the carryover allocation to incur the 10% costs and document this to VHFA. A VHFA-approved cost certification will be required prior to the issuance of a Carryover Allocation. The project must be Placed in Service within two years after allocation at the latest.

P. **Binding Rate Election** Federal regulations permit the applicant to elect the credit percentage rate in effect any time the Agency and the owner enter into a binding agreement pursuant to IRS Regulation 1.42-8. If no election to bind the Housing Credit percentage rate is made, the credit percentage that is applied is that rate in effect at the time the project is Placed in Service.

Q. **IRS Final Form 8609 and Final Cost Certification** VHFA requires final cost certifications for all projects prior to issuance of IRS Form(s) 8609 which should be prepared based on the following guidelines:For projects of fewer than 10 units, final cost certifications prepared by the owner will be accepted.

For projects of 10 units or more, an independent CPA must prepare the final cost certification. If this is not possible prior to the end of the calendar year in which the last building is Placed in Service, VHFA will issue the IRS Form 8609 on the basis of an owner’s final cost certification and supporting documentation, but requires the CPA cost certification to be submitted as soon thereafter as possible.

1. 1 Note that the 4% and 9% Housing Credit figures are ap­proximate. The U.S. Treasury Department is respon­sible for revising the Housing Credit figures monthly based on present value calcula­tions using current interest rates. The rates are set to give the investor a credit yield equal to either 30% or 70% (depending on the type of credit requested) of the value of the qualified basis of the building, for a ten-year period. From an investor's perspective, the net effect of the monthly changes in the Housing Credit rate should be fairly minimal. As of March 2004, the two actual rates were 3.41%and 7.95%. Current rates are posted on VHFA’s website under “Development”. [↑](#footnote-ref-1)
2. 2 Note that federal rental subsidies to individual renters through Section 8 certificates (or vouchers) do not affect the Housing Credit eligibility of those units. Thus, rental income from Section 8 units can exceed the HC rent limits, but the units are still considered HC rent restricted units. In these cases, the tenant contribution towards the contract rent cannot exceed the HC rent limits. [↑](#footnote-ref-2)
3. 4 A developer may choose to submit a scattered site proposal as one application with the understanding that, for purposes of the Housing Credit Program, each building or group of contiguous buildings will receive separate allocations and will not, in that regard, be treated as separate projects. The loss of any building, however, will mean that the entire reservation/allocation will be returned. Alternatively, a developer may submit a separate application for each building/group of adjacent buildings. Under this situation, the loss of a building would require only that building’s reservation/allocation be returned and the developer could proceed with the remaining buildings. [↑](#footnote-ref-3)
4. 5 Subtract utility allowances for those utility costs paid by the tenant. If the landlord pays a particular cost, no utility allowance needs to be deducted. [↑](#footnote-ref-4)