# General Instructions

Section references are to the Internal Revenue Code unless otherwise noted.

## Purpose of Form

Use Form 8586 to claim the low-income housing credit. This general business credit is allowed for each new qualified low-income building placed in service after 1986. Generally, it is taken over a 10-year credit period.

The portion of the low-income housing credit attributable to buildings placed in service after 2007 is not limited by tentative minimum tax and cannot be reported on page 1 of Form 3800. Part II is used to figure this portion of the credit.

Taxpayers that are not partnerships, S corporations, estates, or trusts, and whose only source of this credit is from buildings placed in service before 2008 from those pass-through entities, are not required to complete or file this form. Instead, they can report this credit directly on line 1d of Form 3800, General Business Credit.

## Qualified Low-Income Housing Project

The credit cannot exceed the amount allocated to the building. See section 42(h)(1) for details.

The low-income housing credit can only be claimed for residential rental buildings in low-income housing projects that meet one of the minimum set-aside tests. For details, see the Instructions for Form 8609, Part II, line 10c.

Except for buildings financed with certain tax-exempt bonds, you may not take a low-income housing credit on a building if it has not received an allocation from the housing credit agency. No allocation is needed when 50% or more of the aggregate basis of the building and the land on which the building is located is financed with certain tax-exempt bonds. The owner still must get a Form 8609 from the appropriate housing credit agency (with the applicable items completed, including an assigned BIN). "Land on which the building is located" includes only land that is functionally related and subordinate to the qualified low-income building (see Regulations sections 1.103-8(a)(3) and 1.103-8(b)(4)(iii)).

## Recapture of Credit

There is a 15-year compliance period during which the residential rental building must continue to meet certain requirements. If, as of the close of any tax year in this period, there is a reduction in the qualified basis of the building from the previous year, you may have to recapture a part of the credit you have taken. Similarly, you may have to recapture part of the credits taken in previous years upon certain dispositions of the building or interests therein, unless you follow the procedures to prevent recapture. See *Recapture and building dispositions* in the Instructions for Form 8609-A, Annual Statement for Low-Income Housing Credit, for details. If you must recapture credits, use Form 8611, Recapture of Low-Income Housing Credit. See section 42(j) for details.

## Recordkeeping

Keep a copy of this Form 8586 together with all Forms 8609, Schedules A (Form 8609) (and successor Forms 8609-A), and Forms 8611 for 3 years after the 15-year compliance period ends.

# Specific Instructions

**Line 2.** A decrease in qualified basis will result in recapture if the qualified basis at the close of the tax year is less than the qualified basis at the close of the first year of the credit period.

If the reduction in qualified basis at the close of the tax year also results in a violation of the minimum set-aside requirement, then no credit is allowable for the year.

**Line 3.** The credit for the year is figured on Form 8609-A for each building. Attach a copy of each Form 8609-A you completed for the t year to Form 8586. Enter on line 3 the total credit from attached Form 8609-A for buildings placed in service before 2008.

**Line 6.** Allocate the amount on line 5 between the estate or trust and the beneficiaries in the same proportion as income was allocated and enter the beneficiaries' share on line 6.

**Line 9.** A decrease in qualified basis will result in recapture if the qualified basis at the close of the tax year is less than the qualified basis at the close of the first year of the credit period.

If the reduction in qualified basis at the close of the tax year also results in a violation of the minimum set-aside requirement, then no credit is allowable for the year.

**Line 10.** The credit for the year is figured on Form 8609-A for each building. Attach a copy of each Form 8609-A you completed for the tax year to Form 8586. Enter on line 10 the total credit for attached Form(s) 8609-A for buildings placed in service after 2007.

**Line 13.** Enter the amount included on line 12 that is from a passive activity. Generally, a passive activity is a trade or business in which you did not materially participate. Rental activities are generally considered passive activities, whether or not you materially participate. For details, see Form 8582-CR, Passive Activity Credit Limitations (for individuals, estates, and trusts), or Form 8810, Corporate Passive Activity Loss and Credit Limitations (for corporations).

**Line 15.** Enter the passive activity low-income housing credit allowed for 2009 from Form 8582-CR or Form 8810.

**Line 16.** Enter any carryforward of the credit to 2009 attributable to buildings placed in service after 2007. Enter any carryforward of the credit to 2009 attributable to buildings placed in service before 2008 on Form 3800, line 6.

**Line 17.** Enter any carryback if you amend your 2009 return to carry back an unused low-income housing credit from 2010.

**Line 19.** Allocate the amount on line 18 between the estate or trust a the beneficiaries in the same proportion as income was allocated and enter the beneficiaries' share on line 19.

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**Paperwork Reduction Act Notice.** We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated burden for individual taxpayers filing this form is approved under OMB control number 1545-0074 and is included in the estimates shown in the instructions for their individual income tax return. The estimated burden for all other taxpayers who file this form is:

| | |
|---|---|
| **Recordkeeping** | 5 hr., 44 min. |
| **Learning about the law or the form** | 52 min. |
| **Preparing the form** | 1 hr., 55 min. |
| **Copying, assembling, and sending the form to the IRS** | 16 min. |

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. See the instructions for the tax return with which this form is filed.

Form **8611**
(Rev. January 2009)
Department of the Treasury
Internal Revenue Service

# Recapture of Low-Income Housing Credit

▶ Attach to your return.

Note: *Complete a separate Form 8611 for each building to which recapture applies.*

OMB No. 1545-1035

Attachment Sequence No. **90**

| A Name(s) shown on return | B Identifying number |
|---|---|
| C Address of building (as shown on Form 8609) | D Building identification number (BIN) / E Date placed in service (from Form 8609) |
| F If building is financed in whole or part with tax-exempt bonds, see instructions and furnish: (1) Issuer's name | (2) Date of issue |
| (3) Name of issue | (4) CUSIP number |

**Note:** *Skip lines 1–7 and go to line 8 if recapture is passed through from a flow-through entity (partnership, S corporation, estate, or trust).*

| | | | |
|---|---|---|---|
| 1 | Enter total credits reported on Form 8586 in prior years for this building | 1 | |
| 2 | Credits included on line 1 attributable to additions to qualified basis (see instructions) | 2 | |
| 3 | Credits subject to recapture. Subtract line 2 from line 1 | 3 | |
| 4 | Credit recapture percentage (see instructions) | 4 | . |
| 5 | Accelerated portion of credit. Multiply line 3 by line 4 | 5 | |
| 6 | Percentage decrease in qualified basis. Express as a decimal amount carried out to at least 3 places (see instructions) | 6 | . |
| 7 | Amount of accelerated portion recaptured (see instructions if prior recapture on building). Multiply line 5 by line 6. Section 42(j)(5) partnerships, go to line 16. All other flow-through entities (except electing large partnerships), enter the result here and enter each recipient's share in the appropriate box of Schedule K-1. Generally, flow-through entities other than electing large partnerships will stop here. (**Note:** *An estate or trust enters on line 8 only its share of recapture amount attributable to the credit amount reported on its Form 8586.*) | 7 | |
| 8 | Enter recapture amount from flow-through entity (see **Note** above) | 8 | |
| 9 | Enter the unused portion of the accelerated amount from line 7 (see instructions) | 9 | |
| 10 | Net recapture. Subtract line 9 from line 7 or line 8. If less than zero, enter -0- | 10 | |
| 11 | Enter interest on the line 10 recapture amount (see instructions) | 11 | |
| 12 | Total amount subject to recapture. Add lines 10 and 11 | 12 | |
| 13 | Unused credits attributable to this building reduced by the accelerated portion included on line 9 (see instructions) | 13 | |
| 14 | **Recapture tax.** Subtract line 13 from line 12. If zero or less, enter -0-. Enter the result here and on the appropriate line of your tax return (see instructions). If more than one Form 8611 is filed, add the line 14 amounts from all forms and enter the total on the appropriate line of your return. Electing large partnerships, see instructions | 14 | |
| 15 | **Carryforward of the low-income housing credit attributable to this building.** Subtract line 12 from line 13. If zero or less, enter -0- (see instructions) | 15 | |

**Only Section 42(j)(5) partnerships need to complete lines 16 and 17.**

| | | | |
|---|---|---|---|
| 16 | Enter interest on the line 7 recapture amount (see instructions) | 16 | |
| 17 | Total recapture. Add lines 7 and 16 (see instructions) | 17 | |

# General Instructions

*Section references are to the Internal Revenue Code.*

## Purpose of Form

Use this form if you must recapture part of the low-income housing credit you claimed in previous years because the qualified basis decreased from one year to the next or you disposed of a building, or your interest therein, and you did not follow the procedures that would have prevented recapture of the credit.

**Decrease in qualified basis.** The decrease may result from a change in the eligible basis, or the building no longer meets the minimum set aside requirements of section 42(g)(1), the gross rent requirements of section 42(g)(2), or the other requirements for the units which are set aside.

**Building dispositions.** The disposition of a building, or an interest therein, will generate the recapture of the credit. You can prevent the recapture if you follow the procedures below, relative to the date of the disposition of the building or the interest therein.

***Building dispositions before July 31, 2008.*** Disposing of a building or an interest therein during the tax year will generate a credit recapture, unless you timely post a satisfactory bond or pledge eligible U.S. Treasury securities as collateral. For details on the rules for posting or pledging, see Rev. Rul. 90-60, 1990-2 C.B. 3, and Rev. Proc. 99-11, 1999-1 C.B. 275.

**Note.** You may discontinue maintaining a bond or pledging eligible U.S. Treasury securities by making the election described in Rev. Proc. 2008-60, 2008-43 I.R.B. 1006, and if it is reasonably expected that the building will continue to be operated as a qualified low-income building for the remainder of the building's compliance period. See Rev. Proc. 2008-60 for the details on making the election.

***Building dispositions after July 30, 2008.*** Disposing of a building or an interest therein will generate a credit recapture, unless it is reasonably expected that the building will continue to be operated as a qualified low-income building for the remainder of the building's compliance period.

See section 42(j) for more information.

**Note.** If the decrease in qualified basis is because of a change in the amount for which you are financially at risk on the building, then you must first recalculate the amount of credit taken in prior years under section 42(k) before you calculate the recapture amount on this form.

To complete this form you will need copies of the following forms that you have filed:

- Form 8586, Low-Income Housing Credit (and Form 3800, General Business Credit, if applicable);
- Form 8609, Low-Income Housing Credit Allocation and Certification (or predecessor, Form 8609, Low-Income Housing Credit Allocation Certification);
- Form 8609-A, Annual Statement for Low-Income Housing Credit (or predecessor, Schedule A (Form 8609), Annual Statement); and
- Form 8611.

**Note.** Flow-through entities must give partners, shareholders, and beneficiaries the information that is reported in items C, D, E, and F of Form 8611.

Recapture does not apply if:

- You disposed of the building or an ownership interest in it and you satisfy the requirements for avoiding recapture as outlined earlier under *Building dispositions*;
- You disposed of not more than 33⅓% in the aggregate of your ownership interest in a building that you held through a partnership, or you disposed of an ownership interest in a building that you held through a partnership to which section 42(j)(5) applies or through an electing large partnership;
- The decrease in qualified basis does not exceed the additions to qualified basis for which credits were allowable in years after the year the building was placed in service;
- You correct a noncompliance event within a reasonable period after it is discovered or should have been discovered;
- The qualified basis is reduced because of a casualty loss, provided the property is restored or replaced within a reasonable period.

### Recordkeeping

In order to verify changes in qualified basis from year to year, keep a copy of all Forms 8586, 8609, 8609-A (or predecessor, Schedule A (Form 8609)), 8611, and 8693 for 3 years after the 15-year compliance period ends.

# Specific Instructions

**Note.** If recapture is passed through from a flow-through entity (partnership, S corporation, estate, or trust), skip lines 1–7 and go to line 8.

**Item F.** If the building is financed with tax-exempt bonds, furnish the following information: (1) name of the entity that issued the bond (not the name of the entity receiving the benefit of the financing); (2) date of issue, generally the first date there is a physical exchange of the bonds for the purchase price; (3) name of the issue, or if not named, other identification of the issue; and (4) CUSIP number of the bond with the latest maturity date. If the issue does not have a CUSIP number, enter "None."

**Line 1.** Enter the total credits claimed on the building for all prior years from all Forms 8586 (before reduction due to the tax liability limit) you have filed. Prior to the December 2006 revision of Form 8586, the credits (before reduction due to the tax liability limit) were reported in Part I. Do not include credits taken by a previous owner.

## Line 2 Worksheet (*Line reference is to Form 8609-A (or predecessor, Schedule A (Form 8609).)

| | | |
|---|---|---|
| a | Enter the amount from line 10* | a |
| b | Multiply **a** by 2 | b |
| c | Enter the amount from line 11* | c |
| d | Subtract **c** from **b** | d |
| e | Enter decimal amount figured in step **1** of the instructions for line 14*. If line 14* does not apply to you, enter -0- | e |
| f | Multiply **d** by **e** | f |
| g | Subtract **f** from **d** | g |
| h | Divide line 16* by line 15*. Enter the result here | h |
| i | Multiply **g** by **h**. Enter this amount on line 2. (If more than one worksheet is completed, add the amounts on **i** from all worksheets and enter the total on line 2.) | i |

**Line 2.** Determine the amount to enter on this line by completing a separate Line 2 Worksheet (on page 2) for each prior year for which line 7 of Form 8609-A (or predecessor, Schedule A (Form 8609)) was completed.

**Line 4.** Enter the credit recapture percentage, expressed as a decimal carried to at least 3 places, from the table below:

| IF the recapture event occurs in . . . | THEN enter on line 4 . . . |
|---|---|
| Years 2 through 11 | .333 |
| Year 12 | .267 |
| Year 13 | .200 |
| Year 14 | .133 |
| Year 15 | .067 |

**Line 6.** Enter the percentage decrease in qualified basis during the current year.

For this purpose, figure qualified basis without regard to any additions to qualified basis after the first year of the credit period. Compare any decrease in qualified basis first to additions to qualified basis. Recapture applies only if the decrease in qualified basis exceeds additions to qualified basis after the first year of the credit period.

If you disposed of the building or an ownership interest in it and did not satisfy the requirements for avoiding recapture as outlined earlier under *Building dispositions*, you must recapture all of the accelerated portion shown on line 5. Enter 1.000 on line 6.

**Note.** If the decrease causes the qualified basis to fall below the minimum set-aside requirements of section 42(g)(1) (the 20-50 test or the 40-60 test), then 100% of the amount shown on line 5 must be recaptured. Enter 1.000 on line 6. If you elected the 40-60 test for this building and the decrease causes you to fall below 40%, you cannot switch to the 20-50 test to meet the set-aside requirements. You must recapture the entire amount shown on line 5.

**Line 7.** If there was a prior recapture of accelerated credits on the building, do not recapture that amount again as the result of the current reduction in qualified basis. The example below demonstrates how to incorporate into the current (Year 4) recapture the first year (Year 1) accelerated portion as a result of a prior year (Year 2) recapture event.

**Line 9.** Compute the unused portion of the accelerated amount on line 7 by:

Step 1. Totaling the credits attributable to the building that you could not use in prior years.*

Step 2. Reducing the result of step 1 by any unused credits attributable to additions to qualified basis.

Step 3. Multiplying the result of step 2 by the decimal amount on line 4.

Step 4. Multiplying the result of step 3 by the decimal amount on line 6.

Step 5. Enter the result of step 4 on line 9.

*Generally, this is the amount of credit reported on line 1 of this Form 8611 reduced by the total low-income housing credits allowed on Form 8586 or Form 3800 for each year.

**Special rule for electing large partnerships.** Enter zero on line 9. An electing large partnership is treated as having fully used all prior year credits.

**Line 11.** Compute the interest separately for each prior tax year for which a credit is being recaptured. Interest must be computed at the overpayment rate determined under section 6621(a)(1) and compounded on a daily basis from the due date (not including extensions) of the return for the prior year until the earlier of (a) the due date (not including extensions) of the return for the recapture year, or (b) the date the return for the recapture year is filed and any income tax due for that year has been fully paid.

Tables of interest factors to compute daily compound interest were published in Rev. Proc. 95-17, 1995-1 C.B. 556. The interest rate in effect through March 31, 2009, is shown in Rev. Rul. 2008-54, 2008-52 I.R.B. 1352. For periods after March 31, 2009, use the overpayment rate under section 6621(a)(1) in the revenue rulings published quarterly in the Internal Revenue Bulletin.

**Note.** If the line 8 recapture amount is from a section 42(j)(5) partnership, the partnership will figure the interest and include it in the recapture amount reported to you. Enter "-0-" on line 11 and write "Section 42(j)(5)" to the left of the entry space for line 11.

**Line 13.** Subtract the amount on line 9 from the total of all prior year unused credits attributable to the building (Step 1 of the line 9 instruction above). Enter the result on line 13.

**Line 14.**

| For information on how to report the recapture tax on... | See the instructions for the... |
|---|---|
| Form 1040 | "Total tax" line in the instructions for Form 1040 |
| Form 1120 | "Other taxes" line in the instructions for Form 1120 |

**Special rule for electing large partnerships.** Subtract the credit shown on Form 8586 from the total of the line 14 amounts from all Forms 8611. Enter the result (but not less than zero) on Form 1065-B, Part I, line 26.

**Note.** You must also reduce the current year low-income housing credit, before entering it on Schedules K and K-1, by the amount of the reduction to the total of the recapture amounts.

**Line 15.** Carry forward the low-income housing credit attributable to this building to the next tax year. Report any carryforward attributable to buildings placed in service before 2008 on the carryforward line of Form 3800 for the next tax year. Report any carryforward attributable to buildings placed in service after 2007 on the carryforward line of Form 8586 for the next tax year. See the

**Line 7—*Example.*** $2,700 of accelerated portion of low-income housing credit spread over a 10-year period and not falling below the minimum set-asides for the building. Also, there was a 20% reduction in qualified basis in Year 2 and 30% in Year 4.

| | Year 1 | Year 2 | Year 3 | Year 4* |
|---|---|---|---|---|
| Low-income housing credit | $270 | $216 ($270 × .8 (20% reduction in qualified basis)) | $270 | $189 ($270 × .7 (30% reduction in qualified basis)) |
| Recapture of Year 1 low-income housing credit | | $18 ($270 × .333 × .2 (20% reduction in qualified basis)) | | $9 ($27 ($270 × .333 × .3 (30% reduction in qualified basis) minus $18 Year 2 recapture)) |

* You will have to complete the rest of the form to figure the recapture as the result of the current year reduction in basis as it affects the Year 2 and Year 3 credit.

instructions for Forms 8586 and 3800 for details on how to report the carryforward of unused credits.

**Lines 16 and 17.** Only section 42(j)(5) partnerships complete these lines. This is a partnership (other than an electing large partnership) that has at least 35 partners, unless the partnership elects (or has previously elected) not to be treated as a section 42(j)(5) partnership. For purposes of this definition, a husband and wife are treated as one partner.

For purposes of determining the credit recapture amount, a section 42(j)(5) partnership is treated as the taxpayer to which the low-income housing credit was allowed and as if the amount of credit allowed was the entire amount allowable under section 42(a).

See the instructions for line 11 to figure the interest on line 16. The partnership must attach Form 8611 to its Form 1065 and allocate this amount to each partner on Schedule K-1 (Form 1065) in the same manner as the partnership's taxable income is allocated to each partner.

**Paperwork Reduction Act Notice.** We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated burden for individual taxpayers filing this form is approved under OMB control number 1545-0074 and is included in the estimates shown in the instructions for their individual income tax return. The estimated burden for all other taxpayers who file this form is shown below.

**Recordkeeping** . . . 8 hr., 21 min.

**Learning about the law or the form** . . . . . 1 hr.

**Preparing and sending the form to the IRS** . . 1 hr., 10 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the IRS at the address listed in the instructions for the tax return with which this form is filed.

## Section 42 . – Low-income Housing Credit

*26 CFR 1.42-5: Monitoring compliance with low-income housing credit requirements.*

T. D. 8430

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1 and 602

## Procedure for Monitoring Compliance with Low-Income Housing Credit Requirements

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final Income Tax regulations relating to the requirement that State allocation plans provide a procedure for State and local housing credit agencies to monitor for compliance with the requirements of section 42 of the Internal Revenue Code. State and local housing credit agencies are to report any noncompliance to the Internal Revenue Service. These final regulations affect State and local housing credit agencies, owners of buildings or projects for which the low-income housing credit is claimed, and taxpayers claiming the low-income housing credit.

EFFECTIVE DATE: These final regulations are effective June 30, 1993.

SUPPLEMENTARY INFORMATION:

*Paperwork Reduction Act*

The collection of information contained in this final regulation has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1980 (44 U.S.C. 3504(h)) under control number 1545-1291. The estimated annual burden per State or local government respondent/recordkeeper varies from 10 hours to 1,500 hours, with an estimated average of 250 hours. The estimated annual burden for all other respondent/recordkeepers varies from .5 hours to 3 hours, with an estimated average of 1 hour.

These estimates are an approximation of the average time expected to be necessary for the collection of information. They are based on such information as is available to the Internal Revenue Service. Individual respondents/recordkeepers may require greater or less time, depending on their particular circumstances.

Comments concerning the accuracy of this burden and suggestions for reducing this burden should be directed to the Internal Revenue Service, Attn: IRS Reports Clearance Officer T:FP, Washington, D.C. 20224, and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, D.C. 20503.

*Background*

On December 27, 1991, the Internal Revenue Service published in the Federal Register a notice of proposed rulemaking (56 FR 67018 [PS-78-91, 1992-1 C.B. 1242]) under section 42 of the Internal Revenue Code of 1986 with respect to the low-income housing credit.

A number of public comments were received concerning these regulations, and a public hearing was held on March 4, 1992. After consideration of the written comments and those presented at the hearing, the proposed regulations are adopted, as revised, by this Treasury decision.

*Explanation of Provisions*

Section 42 provides for a low-income housing credit that may be claimed as part of the general business credit under section 38. The credit determined under section 42 is allowable only to the extent the owner of a qualified low-income building receives a housing credit allocation from a State or local housing credit agency ("Agency"), unless the building is exempt from the allocation requirement by reason of section 42(h)(4)(B). Under section 42(m)(1)(A), the housing credit dollar amount for any building is zero unless the amount was allocated pursuant to a qualified allocation plan of the Agency. Similarly, under section 42(m)(1)(D), the housing credit dollar amount for any project qualifying under section 42(h)(4) is zero unless the project satisfies the requirements for allocation of a housing credit dollar amount under the qualified allocation plan of the Agency.

Under section 42(m)(1)(B)(iii), which was amended and renumbered by the Revenue Reconciliation Act of 1990 (the "1990 Act"), an allocation plan is not qualified unless it contains a procedure that the Agency (or an agent of, or private contractor hired by, the Agency) will follow in monitoring compliance with the provisions of section 42. The Agency is to notify the Internal Revenue Service of any noncompliance of which the Agency becomes aware.

Section 42(m)(1)(B)(iii) is effective on January 1, 1992, and applies to all buildings for which the low-income housing credit determined under section 42 is, or has been, allowable at any time.

These final regulations provide guidance on section 42(m)(1)(B)(iii). Under the regulations, an allocation plan meets the requirement of section 42(m)(1)(B)(iii) if it includes a monitoring procedure that contains, in substance, all of the provisions specified in the regulations.

The specified provisions are minimum requirements; a monitoring procedure may contain additional provisions or requirements. Moreover, the language, form, and order of the specified provisions as set forth in the regulations need not be exactly duplicated in an allocation plan in order for the plan to include a monitoring procedure as required by the regulations. As long as the substance of the provisions specified in the regulations is contained in the allocation plan as a whole, the allocation plan satisfies the monitoring procedure required by the regulations.

These regulations only address compliance monitoring procedures of Agencies. They do not address forms and other records that may be required by the Internal Revenue Service on examination or audit.

*Public Comments*

*Comments on recordkeeping and record retention*

One comment suggested that where an allocation of credit has been made on a project basis under section

42(h)(1)(F), the recordkeeping and record retention provisions should also apply on a project basis. This suggestion has not been adopted because only the minimum set-aside requirement under section 42(g)(1) is satisfied on a project-by-project basis. All other requirements of section 42 must be met on a building-by-building basis.

Two comments suggested that owners of low-income housing projects be required to keep records describing how utility allowances are determined. Because utility allowances are taken into account in determining whether a unit is rent-restricted under section 42(g)(2)(B)(ii), the final regulations include utility allowances among the rent records to be retained by owners.

Another comment suggested that owners should be required to keep records showing: (1) the number of occupants in each unit and changes in the number of occupants for those units where rent is determined by the number of occupants per unit; (2) information on unit size, including the number of bedrooms and square footage of the unit; and (3) how the eligible basis was calculated at the end of the first year of the credit period. These suggestions have been adopted by the final regulations. Also in response to this comment, the final regulations clarify that the records of tenant income should be kept on a per unit basis. However, this comment's suggestion that owners be required to retain marketing and advertising materials demonstrating that units are available to the general public has not been adopted by the final regulations because marketing and advertising materials may not be sufficient to demonstrate that a building satisfies the general public use requirement.

One comment suggested that if a building is sold or transferred, the building owner should be required to transfer all records to the new owner. In the case of an audit, the new owner needs at least some of those records in order to demonstrate that any credit is allowable for the building and to avoid recapture. In particular, records of the first year of the credit period are necessary to show that credit is allowable for any later year in the credit period. The final regulations do not address transfers of records to new owners of buildings because these regulations are directed to Agencies and Agencies are not required to monitor prior years of the compliance period once those years end. Nevertheless, even without an Agency requirement, the transferee, as part of its transaction with the transferor, should obtain the first year information from the transferor in order to substantiate credits claimed.

Several comments suggested that tenant participation in a housing assistance program under section 8 of the United States Housing Act of 1937 ("Section 8") should exempt the owner from having to obtain supporting income documentation from that tenant because public housing authorities verify each Section 8 tenant's income and assets. Participation in the Section 8 program does not necessarily guarantee that a tenant has a qualifying income equal to or less than the income limitation under section 42(g). However, in response to this suggestion, the final regulations provide that if public housing authorities submit a statement to the building owner declaring that a Section 8 tenant's income does not exceed the applicable income limit under section 42(g), the owner is not required to obtain other documentation to verify that tenant's income.

Several comments noted that the definition of annual income under the Section 8 program is based on the tenant's anticipated annual income for the 12 months following the income certification. These commentators suggested that federal income tax returns not be considered permissible documentation of income because tax returns only show income for the prior tax year. This suggestion has not been adopted by the final regulations because, although the determination of annual income is not based upon gross income for federal income tax purposes (tenant income is calculated in a manner consistent with the determination of annual income under Section 8), tax returns do supply evidence of a tenant's sources of income and are signed under penalty of perjury.

Several comments stated that the requirement that owners retain each year's records for 6 years beyond the end of the building's compliance period is unreasonable. In response to these comments, the final regulations do not require owners to retain a year's records for more than 6 years after the due date (with extensions) for filing the federal income tax return for that year. However, because under the final regulations the records for the first year of the credit period are needed to prove the building's eligibility for the credit each year, those records must be retained for at least 6 years beyond the due date (with extensions) for filing the federal income tax return for the last year of the building's compliance period. This is appropriate because, as noted above, these records may be needed to show that credit is allowable.

Two comments questioned whether records should be kept for the extended, use period under section 42(h)(6)(D). The final regulations do not contain any such requirement because recapture of the credit can result only from noncompliance occurring during the compliance period. However, an Agency may require retention of records for a longer period if it desires.

One comment questioned the period for which an Agency should retain its records. In response, the final regulations provide that an Agency must retain records of noncompliance or failure to certify for 6 years beyond the Agency's filing of the respective Form 8823, "Low-Income Housing Credit Agencies Report of Noncompliance." In all other cases, the Agency must retain the certifications and records for 3 years from the end of the calendar year the Agency receives the certifications and records.

*Comments on certification and review*

Two comments suggested that building owners be required to certify the applicable fraction and eligible basis claimed on the last filed Form 8609 (Schedule A), "Annual Statement." This suggestion has not been adopted because this information is already available to the Examination Division of the Internal Revenue Service. The Service bears the responsibility for determining whether a building owner has claimed the correct amount of credit each year and whether the building owner is subject to recapture. It is not the intent of these regulations to have Agencies audit income tax returns. However, in response to this comment, the final

regulations add to the list of certifications a requirement that owners certify that the applicable fraction under section 42(c)(1)(B) has not changed from the prior year or, if the applicable fraction has changed, that the owners describe the change.

Several comments questioned whether an Agency is required to choose the reporting period the certifications cover or whether the certifications must cover the owner's taxable year. Those comments also suggested that the certifications should cover the preceding 12-month period. In response to this suggestion, the final regulations state that the annual owner certifications should cover the preceding 12-month period. However, an Agency is free to require more frequent certifications covering shorter time periods provided that all months within each 12-month period are subject to certification.

One comment suggested that the review provision should include monitoring for violations of the rent restrictions under section 42(g)(2). This suggestion has been adopted by the final regulations.

Another comment suggested that the final regulations provide that the "next available unit" rule is not violated, and credit is not recaptured, if a vacant low-income unit of comparable or smaller size is rented on a temporary basis to a market-rate tenant. This suggestion has not been adopted. The issue of whether temporary rentals result in recapture of the credit is not properly addressed in regulations on compliance monitoring, but will be addressed in future guidance on credit recapture.

Two comments suggested that owners of buildings with 100 percent low-income occupancy should be required to submit tenant income certifications only for those units that became vacant after the previous year's compliance certifications were submitted. This suggestion has not been adopted because the determination of whether a tenant qualifies for purposes of the low-income set-aside is made on a continuing basis, both with regard to the tenant's income and the qualifying area income, rather than only on the date the tenant initially occupies the unit. *See* 2 H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. 11-93 (1986), 1986-3 (Vol. 4) C.B. 93.

Numerous comments suggested that the review provision be revised to provide for random sampling in both review choices. In addition, the comments requested guidance as to the number of projects that must be inspected each year and the number of units in each project that must be examined. The comments also requested additional flexibility in designing a review procedure than that available under the proposed regulations. In response to these suggestions, the review provision of the final regulations has been revised to provide Agencies with more flexibility and certainty in designing monitoring procedures. The final regulations permit a review provision containing any one or more of the following three sets of requirements: (1) the owners of at least 50 percent of all low-income housing projects in the Agency's jurisdiction must submit to the Agency for compliance review a copy of the annual income certification, the documentation the owner has received to support that certification, and the rent record for each low-income tenant in at least 20 percent of the low-income units in their projects; (2) the Agency must inspect at least 20 percent of the low-income housing projects in the Agency's jurisdiction each year and must inspect the low-income certification, the documentation the owner has received to support that certification, and the rent record for each low-income tenant in at least 20 percent of the low-income units in those projects; or (3) the owners of all low-income housing projects in the Agency's jurisdiction must submit to the Agency each year information on tenant income and rent for each low-income unit, in the form and manner designated by the Agency, and the owners of at least 20 percent of the projects in the Agency's jurisdiction must submit to the Agency for compliance review a copy of the annual income certification, the documentation the owner has received to support that certification, and the rent record for each low-income tenant in at least 20 percent of the low-income units in their projects. The Agency should determine which tenants' records are to be submitted by the owners for review.

Numerous comments questioned how the permitted exception would operate with respect to certain buildings financed with tax-exempt bond proceeds or with loans made under the Farmers Home Administration (FmHA) section 515 program. In response to these comments, the final regulations clarify this exception. Under the final regulations, a monitoring procedure may except FmHA-financed or bond-financed buildings from the review provision if the FmHA or tax-exempt bond issuer agrees to provide information concerning the income and rent of the tenants in the building to the Agency. The Agency may assume the accuracy of the information provided by the FmHA or the tax-exempt bond issuer without verification. The Agency must review the information and determine that the income limitation and rent restriction of section 42(g)(1) and (2) are met. However, if the information provided by the FmHA or tax-exempt bond issuer is not sufficient for the Agency to make this determination, the Agency must request the necessary additional income or rent information from the owner of the buildings.

*Comments on auditing*

One comment suggested that the use of the term "auditing" in the proposed regulations is misleading because it implies that the Agency is to audit the tax records of the owner of the building for the Service. In response to this suggestion, the final regulations substitute the term "inspection."

Another comment noted that the proposed regulations could be interpreted as prohibiting a separate physical inspection of a building without a review of the records. This interpretation was not intended. An inspection may include, but is not required to include, a review of records.

*Comments on notification of noncompliance*

Several comments suggested that notification of noncompliance to the Service not be required where the noncompliance has been corrected within a reasonable amount of time. This suggestion has not been adopted because it may not always be easy or even possible for an Agency to determine whether corrected noncompliance results in recapture of the credit. Accordingly, under the final regulations,

all noncompliance, whether or not corrected, must be reported so that the Service can determine whether the taxpayer is subject to recapture of the credit.

Another comment suggested that any change in a building's eligible basis should be considered noncompliance that must be reported to the Service. The commentator reasons that this is necessary to ensure that the information being provided on the annual certifications and Form 8586, "Low-Income Housing Credit," and Form 8609 (Schedule A) are consistent. Changes in eligible basis and the applicable fraction that result in a decrease in qualified basis result in recapture of credit. Therefore, the final regulations provide that any change in either the applicable fraction or eligible basis that results in a decrease in the project's qualified basis should be considered noncompliance that must be reported to the Service.

One comment suggested that tenant fraud should be reported to the Service. No specific changes to the regulations have been made in response to this suggestion. If tenant fraud results in noncompliance, the noncompliance should be reported.

Comments suggested that any notice sent to a building owner and the Form 8823 sent to the Service should be required to be sent by certified mail. These suggestions have not been adopted; although an Agency is free to use certified mail, it is not required to do so.

One comment suggested that any fees paid to an agent or other private contractor for delegated compliance monitoring should not be contingent upon a finding of compliance or noncompliance. The final regulations do not contain this suggested provision. However, it is the view of the Treasury and the Service that if an Agency makes the payment of compliance monitoring fees to an agent or private contractor contingent upon a finding of compliance or noncompliance, the Agency may not be using reasonable diligence to ensure that the agent or private contractor properly performs the delegated compliance monitoring responsibilities.

One comment suggested that an Agency be permitted to delegate monitoring responsibilities to another Agency, including the responsibility of notifying the Service of any noncompliance of which the delegated Agency becomes aware. In response to this suggestion, the final regulations allow Agencies to delegate some or all of their compliance monitoring responsibilities for a building to another Agency within the State.

One comment suggested that although compliance monitoring is not required of Agencies before January 1, 1992, if an Agency becomes aware of noncompliance that occurred before that date, the Agency should be required to notify the Service of that noncompliance. The final regulations adopt this comment which reflects section 42(m)(1)(B)(iii) as effective before its amendment by the 1990 Act.

Several comments suggested that the regulations should expressly permit an Agency to establish reasonable administrative fees for covering an Agency's expenses in monitoring compliance, and other comments suggested that the failure to pay monitoring fees should be considered non-compliance. Section 42 does not prohibit an Agency from charging an administrative fee to cover the Agency's expenses in monitoring for compliance, but this is a matter for the determination of the Agency, rather than the Service. Accordingly, the regulations do not address any issues concerning Agency fees.

*Special Analyses*

It has been determined that these rules are not major rules as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a final Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking for the regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

*Drafting Information*

The principal author of these regulations is Paul F. Handleman, Office of the Assistant Chief Counsel (Passthroughs and Special Industries), Internal Revenue Service. However other personnel from the Service and the Treasury Department participated i their development

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*Adoption of Amendments to the Regulations*

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority citation for part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805 * * * Section 1.42-5 is also issued under 26 U.S.C. 42(n) * * *

Par. 2. New §1.42-5 is added to read as follows:

*§1.42-5 Monitoring compliance with low-income housing credit requirements.*

(a) *Compliance monitoring requirement* —(1) *In general.* Under section 42(m)(1)(B)(iii), an allocation plan is not qualified unless it contains a procedure that the State or local housing credit agency ("Agency") (or an agent of, or other private contractor hired by, the Agency) will follow in monitoring for noncompliance with the provisions of section 42 and in notifying the Internal Revenue Service of any noncompliance of which the Agency becomes aware. These regulations only address compliance monitoring procedures required of Agencies. The regulations do not address forms and other records that may be required by the Service on examination or audit. For example, if a building is sold or otherwise transferred by the owner, the transferee should obtain from the transferor information related to the first year of the credit period so that the transferee can substantiate credits claimed.

(2) *Requirements for a monitoring procedure* —(i) *In general.* A procedure for monitoring for noncompliance under section 42(m)(1)(B)(iii) must include—

(A) The recordkeeping and record retention provisions of paragraph (b) of this section;

(B) The certification and review provisions of paragraph (c) of this section;

(C) The inspection provision of paragraph (d) of this section; and

(D) The notification-of-noncompliance provisions of paragraph (e) of this section.

(ii) *Order and form.* A monitoring procedure will meet the requirements of section 42(m)(1)(B)(iii) if it contains the substance of these provisions. The particular order and form of the provisions in the allocation plan is not material. A monitoring procedure may contain additional provisions or requirements.

(b) *Recordkeeping and record retention provisions* —(1) *Recordkeeping provision.* Under the recordkeeping provision, the owner of a low-income housing project must be required to keep records for each qualified low-income building in the project that show for each year in the compliance period—

(i) The total number of residential rental units in the building (including the number of bedrooms and the size in square feet of each residential rental unit);

(ii) The percentage of residential rental units in the building that are low-income units;

(iii) The rent charged on each residential rental unit in the building (including any utility allowances);

(iv) The number of occupants in each low-income unit, but only if rent is determined by the number of occupants in each unit under section 42(g)(2) (as in effect before the amendments made by the Revenue Reconciliation Act of 1989);

(v) The low-income unit vacancies in the building and information that shows when, and to whom, the next available units were rented;

(vi) The annual income certification of each low-income tenant per unit;

(vii) Documentation to support each low-income tenant's income certification (for example, a copy of the tenant's federal income tax return, Forms W-2, or verifications of income from third parties such as employers or state agencies paying unemployment compensation). Tenant income is calculated in a manner 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. In the case of a tenant receiving housing assistance payments under Section 8, the documentation requirement of this paragraph (b)(1)(vii) is satisfied if the public housing authority provides a statement to the building owner declaring that the tenant's income does not exceed the applicable income limit under section 42(g);

(viii) The eligible basis and qualified basis of the building at the end of the first year of the credit period; and

(ix) The character and use of the nonresidential portion of the building included in the building's eligible basis under section 42(d) (*e.g.*, tenant facilities that are available on a comparable basis to all tenants and for which no separate fee is charged for use of the facilities, or facilities reasonably required by the project).

(2) *Record retention provision.* Under the record retention provision, the owner of a low-income housing project must be required to retain the records described in paragraph (b)(1) of this section for at least 6 years after the due date (with extensions) for filing the federal income tax return for that year. The records for the first year of the credit period, however, must be retained for at least 6 years beyond the due date (with extensions) for filing the federal income tax return for the last year of the compliance period of the building.

(c) *Certification and review provisions*—(1) *Certification.* Under the certification provision, the owner of a low-income housing project must be required to certify at least annually to the Agency that, for the preceding 12-month period —

(i) The project met the requirements of:

(A) The 20-50 test under section 42(g)(1)(A), the 40-60 test under section 42(g)(1)(B), or the 25-60 test under sections 42(g)(4) and 142(d)(6) for New York City, whichever minimum set-aside test was applicable to the project; and

(B) If applicable to the project, the 15-40 test under sections 42(g)(4) and 142(d)(4)(B) for "deep rent skewed" projects;

(ii) There was no change in the applicable fraction (as defined in section 42(c)(1)(B)) of any building in the project, or that there was a change, and a description of the change;

(iii) The owner has received an annual income certification from each low-income tenant, and documentation to support that certification; or, in the case of a tenant receiving Section 8 housing assistance payments, the statement from a public housing authority described in paragraph (b)(1)(vii) of this section;

(iv) Each low-income unit in the project was rent-restricted under section 42(g)(2);

(v) All units in the project were for use by the general public and used on a non transient basis (except for transitional housing for the homeless provided under section 42(i)(3)(B)(iii));

(vi) Each building in the project was suitable for occupancy, taking into account local health, safety, and building codes;

(vii) There was no change in the eligible basis (as defined in section 42(d)) of any building in the project, or if there was a change, the nature of the change ( *e.g.*, a common area has become commercial space, or a fee is now charged for a tenant facility formerly provided without charge);

(viii) All tenant facilities included in the eligible basis under section 42(d) of any building in the project, such as swimming pools, other recreational facilities, and parking areas, were provided on a comparable basis without charge to all tenants in the building;

(ix) If a low-income unit in the project became 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 to tenants having a qualifying income before any units in the project were or will be rented to tenants not having a qualifying income;

(x) If the income of tenants of a low-income unit in the project increased above the limit allowed in section 42(g)(2)(D)(ii), the next available unit of comparable or smaller size in the project was or will be rented to tenants having a qualifying income; and

(xi) An extended low-income housing commitment as described in section 42(h)(6) was in effect (for

buildings subject to section 7108-(c)(1) of the Revenue Reconciliation Act of 1989).

(2) *Review.* The review provision must—

(i) Require that the Agency review the certifications submitted under paragraph (c)(1) of this section for compliance with the requirements of section 42;

(ii) Contain at least one of the following requirements:

(A) The owners of at least 50 percent of all low-income housing projects in the Agency's jurisdiction must submit to the Agency for compliance review a copy of the annual income certification, the documentation the owner has received to support that certification, and the rent record for each low-income tenant in at least 20 percent of the low-income units in their projects;

(B) The Agency must inspect at least 20 percent of low-income housing projects each year and must inspect the low-income certification, the documentation the owner has received to support that certification, and the rent record for each low-income tenant in at least 20 percent of the low-income units in those projects; or

(C) The owners of all low-income housing projects must submit to the Agency each year information on tenant income and rent for each low-income unit, in the form and manner designated by the Agency, and the owners of at least 20 percent of the projects must submit to the Agency for compliance review a copy of the annual income certification, the documentation the owner has received to support that certification, and the rent record for each low-income tenant in at least 20 percent of the low-income units in their projects; and

(iii) require that the Agency determine which tenants' records are to be inspected or submitted by the owners for review. If a monitoring procedure includes the review provision described in paragraph (c)(2)(ii)(B) of this section, the records to be inspected must be chosen in a manner that will not give owners of low-income housing projects advance notice that their records for a particular year will or will not be inspected. However, an Agency may give an owner reasonable notice that an inspection will occur so that the owner may assemble records (for example, 30 days notice of inspection). *See* paragraph (d) of this section for the inspection provision that is required to be included in all monitoring procedures.

(3) *Frequency and form of certification.* A monitoring procedure must require that the certifications and reviews of paragraph (c)(1) and (2) of this section be made at least annually covering each year of the 15-year compliance period under section 42(i)(1). The certifications must be made under penalty of perjury. A monitoring procedure may require certifications and reviews more frequently than on a 12-month basis, provided that all months within each 12-month period are subject to certification.

(4) *Exception for certain buildings* —(i) *In general.* The review requirements under paragraph (c)(2)(ii)(A), (B), and (C) of this section may provide that owners are not required to submit, and the Agency is not required to review, the tenant income certifications, supporting documentation, and rent records for buildings financed by the Farmers Home Administration (FmHA) under the section 515 program, or buildings of which 50 percent or more of the aggregate basis (taking into account the building and the land) is financed with the proceeds of obligations the interest on which is exempt from tax under section 103 (tax-exempt bonds). In order for a monitoring procedure to except these buildings, the Agency must meet the requirements of paragraph (c)(4)(ii) of this section.

(ii) *Agreement and review.* The Agency must enter into an agreement with the FmHA or tax-exempt bond issuer. Under the agreement, the FmHA or tax-exempt bond issuer must agree to provide information concerning the income and rent of the tenants in the building to the Agency. The Agency may assume the accuracy of the information provided by FmHA or the tax-exempt bond issuer without verification. The Agency must review the information and determine that the income limitation and rent restriction of section 42(g)(1) and (2) are met. However, if the information provided by the FmHA or tax-exempt bond issuer is not sufficient for the Agency to make this determination, the Agency must request the necessary additional income or rent information from the owner of the buildings. For example, because FmHA determines tenant eligibility based on it definition of "adjusted annual income,' rather than "annual income" as defined under Section 8, the Agency may have to calculate the tenant's income for section 42 purposes and may need to request additional income information from the owner.

(iii) *Example.* The exception permitted under paragraph (c)(4)(i) and (ii) of this section is illustrated by the following example.

*Example.* An Agency chooses the review requirement of paragraph (c)(2)(ii)(A) of this section and some of the buildings selected for review are buildings financed by the FmHA. The Agency has entered into an agreement described in paragraph (c)(4)(ii) of this section with the FmHA with respect to those buildings. In reviewing the FmHA-financed buildings, the Agency obtains the tenant income and rent information from the FmHA for 20 percent of the low-income units in each of those buildings. The Agency calculates the tenant income and rent to determine whether the tenants meet the income and rent limitation of section 42(g)(1) and (2). In order to make this determination, the Agency may need to request additional income or rent information from the owner of the FmHA buildings if the information provided by the FmHA is not sufficient.

(d) *Inspection provision.* Under the inspection provision, the Agency must have the right to perform an on-site inspection of any low-income housing project at least through the end of the compliance period of the buildings in the project. The inspection provision of this paragraph (d) is separate from any review of low-income certifications, supporting documents, and rent records under paragraph (c)(2)(ii) of this section.

(e) *Notification-of-noncompliance provisions* —(1) *In general* Under the notification-of-noncompliance provisions, the Agency must be required to give the notice described in paragraph (e)(2) of this section to the owner of a low-income housing project and the notice described in paragraph (e)(3) of this section to the Service.

(2) *Notice to owner.* The Agency must be required to provide prompt written notice to the owner of a low income housing project if the Agency does not receive the certification described in paragraph (c)(1) of this section, or does not receive or is

not permitted to inspect the tenant income certifications, supporting documentation, and rent records described in paragraph (c)(2)(ii)(A), (B), or (C) of this section (whichever is applicable), or discovers by inspection, review, or in some other manner, that the project is not in compliance with the provisions of section 42.

(3) *Notice to Internal Revenue Service* —(i) *In general.* The Agency must be required to file Form 8823, "Low-Income Housing Credit Agencies Report of Noncompliance," with the Service no later than 45 days after the end of the correction period (as described in paragraph (e)(4) of this section, including extensions permitted under that paragraph) and no earlier than the end of the correction period, whether or not the noncompliance or failure to certify is corrected. The Agency must explain on Form 8823 the nature of the noncompliance or failure to certify and indicate whether the owner has corrected the noncompliance or failure to certify. Any change in either the applicable fraction or eligible basis under paragraph (c)(1)(ii) and (vii) of this section, respectively, that results in a decrease in the qualified basis of the project under section 42(c)(1)(A) is noncompliance that must be reported to the Service under this paragraph (e)(3). If an Agency reports on Form 8823 that a building is entirely out of compliance and will not be in compliance at any time in the future, the Agency need not file Form 8823 in subsequent years to report that building's noncompliance.

(ii) *Agency retention of records.* An Agency must retain records of noncompliance or failure to certify for 6 years beyond the Agency's filing of the respective Form 8823. In all other cases, the Agency must retain the certifications and records described in paragraph (c) of this section for 3 years from the end of the calendar year the Agency receives the certifications and records.

(4) *Correction period.* The correction period shall be that period specified in the monitoring procedure during which an owner must supply any missing certifications and bring the project into compliance with the provisions of section 42. The correction period is not to exceed 90 days from the date of the notice to the owner described in paragraph (e)(2) of this section. An Agency may extend the correction period for up to 6 months, but only if the Agency determines there is good cause for granting the extension.

(f) *Delegation of authority* —(1) *Agencies permitted to delegate compliance monitoring functions* —(i) *In general.* An Agency may retain an agent or other private contractor ("Authorized Delegate") to perform compliance monitoring. The Authorized Delegate must be unrelated to the owner of any building that the Authorized Delegate monitors. The Authorized Delegate may be delegated all of the functions of the Agency, except for the responsibility of notifying the Service under paragraph (e)(3) of this section. For example, the Authorized Delegate may be delegated the responsibility of reviewing tenant certifications and documentation under paragraph (c)(1) and (2) of this section, the right to inspect buildings and records as described in paragraph (d) of this section, and the responsibility of notifying building owners of lack of certification or noncompliance under paragraph (e)(2) of this section. The Authorized Delegate must notify the Agency of any noncompliance or failure to certify.

(ii) *Limitations.* An Agency that delegates compliance monitoring to an Authorized Delegate under paragraph (f)(1)(i) of this section must use reasonable diligence to ensure that the Authorized Delegate properly performs the delegated monitoring functions. Delegation by an Agency of compliance monitoring functions to an Authorized Delegate does not relieve the Agency of its obligation to notify the Service of any noncompliance of which the Agency becomes aware.

(2) *Agencies permitted to delegate compliance monitoring functions to another Agency.* An Agency may delegate all or some of its compliance monitoring responsibilities for a building to another Agency within the State. This delegation may include the responsibility of notifying the Service under paragraph (e)(3) of this section.

(g) *Liability.* Compliance with the requirements of section 42 is the responsibility of the owner of the building for which the credit is allowable. The Agency's obligation to monitor for compliance with the requirements of section 42 does not make the Agency liable for an owner's non-compliance.

(h) *Effective date.* Allocation plans must comply with these regulations by June 30, 1993. The requirement of section 42(m)(1)(B)(iii) that allocation plans contain a procedure for monitoring for noncompliance becomes effective on January 1, 1992, and applies to buildings for which a low-income housing credit is, or has been, allowable at any time. Thus, allocation plans must comply with section 42(m)(1)(B)(iii) prior to June 30, 1993, the effective date of these regulations. An allocation plan that complies with these regulations, with the notice of proposed rulemaking published in the Federal Register on December 27, 1991, or with a reasonable interpretation of section 42(m)(1)(B)(iii) will satisfy the requirements of section 42(m)(1)(B)(iii) for periods before June 30, 1993. Section 42(m)(1)(B)(iii) and these regulations do not require monitoring for whether a building or project is in compliance with the requirements of section 42 prior to January 1, 1992. However, if an Agency becomes aware of noncompliance that occurred prior to January 1, 1992, the Agency is required to notify the Service of that noncompliance.

## PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. Section 602.101(c) is amended by adding the following entry to the table:

"1.42-5 .... 1545-1291".

Michael P. Dolan,
*Acting Commissioner of Internal Revenue.*

Approved August 4, 1992.

Fred T. Goldberg, Jr.,
*Assistant Secretary of the Treasury.*

(Filed by the Office of the Federal Register on September 1, 1992, 8:45 a.m., and published in the issue of the Federal Register for September 2, 1992, 57 F.R. 40118)

appropriate percentage for the month tax-exempt bonds are issued must--

(i) Be in writing;

(ii) Reference section 42(b)(2)(A)-(ii)(II);

(iii) Specify the percentage of the aggregate basis of the building and the land on which the building is located that is financed with the proceeds of obligations described in section 42(h)(4)(A) (tax-exempt bonds);

(iv) State the month in which the tax-exempt bonds are issued;

(v) State that the month in which the tax-exempt bonds are issued is the month elected for the appropriate percentage to be used for the building;

(vi) Be signed by the taxpayer; and

(vii) Be notarized by the 5th day following the end of the month in which the bonds are issued.

(2) *Bonds issued in more than one month.* If a building described in section 42(h)(4)(B) (substantially bond-financed building) is financed with tax-exempt bonds issued in more than one month, the taxpayer may elect the appropriate percentage for any month in which the bonds are issued. Once the election is made, the appropriate percentage elected applies for the building even if all bonds are not issued in that month. The requirements of this paragraph (b), including the time limitation contained in paragraph (b)(1)(vii) of this section, must also be met.

(3) *Limitations on appropriate percentage.* Under section 42(m)(2)(D), the credit allowable for a substantially bond-financed building is limited to the amount necessary to assure the project's feasibility. Accordingly, in making the determination under section 42(m)(2), an Agency may use an applicable percentage that is less, but not greater than, the appropriate percentage for the month the building is placed in service, or the month elected by the taxpayer under section 42(b)(2)(A)(ii)(II).

(4) *Procedures--(i) Taxpayer.* The taxpayer must provide the original notarized election statement to the Agency before the close of the 5th calendar day following the end of the month in which the bonds are issued. If an authority other than the Agency issues the tax-exempt bonds, the taxpayer must also give the Agency a signed statement from the issuing authority that certifies the information described in paragraphs (b)(1)(iii) and (iv) of this section. The taxpayer must also retain a copy of the election statement.

(ii) *Agency.* The Agency must retain the original of the election statement and a copy of the Form 8609 that reflects the election statement. The Agency must file an additional copy of the Form 8609 with the Agency's Form 8610 that reflects the calendar year the Form 8609 is issued.

*§ 1.42-9 For use by the general public.*

(a) *General rule.* If a residential rental unit in a building is not for use by the general public, the unit is not eligible for a section 42 credit. A residential rental unit is for use by the general public if the unit is rented in a manner consistent with housing policy governing non-discrimination, as evidenced by rules or regulations of the Department of Housing and Urban Development (HUD) (24 CFR subtitle A and chapters I through XX). See HUD Handbook 4350.3 (or its successor). A copy of HUD Handbook 4350.3 may be requested by writing to: HUD, Directives Distribution Section, room B-100, 451 7th Street, SW., Washington, DC 20410.

(b) *Limitations.* Notwithstanding paragraph (a) of this section, if a residential rental unit is provided only for a member of a social organization or provided by an employer for its employees, the unit is not for use by the general public and is not eligible for credit under section 42. In addition, any residential rental unit that is part of a hospital, nursing home, sanitarium, lifecare facility, trailer park, or intermediate care facility for the mentally and physically handicapped is not for use by the general public and is not eligible for credit under section 42.

(c) *Treatment of units not for use by the general public.* The costs attributable to a residential rental unit that is not for use by the general public are not excludable from eligible basis by reason of the unit's ineligibility for the credit under this section. However, in calculating the applicable fraction, the unit is treated as a residential rental unit that is not a low-income unit.

§ 1.42-10 *Utility allowances.*

(a) *Inclusion of utility allowances in gross rent.* If the cost of any utilities (other than telephone) for a residential rental unit are paid directly by the tenant(s), the gross rent for that unit includes the applicable utility allowanc determined under this section. This section only applies for purposes of determining gross rent under section 42(g)(2)(B)(ii) as to rent-restricted units.

(b) *Applicable utility allowances--(1) FmHA-assisted buildings.* If a building receives assistance from the Farmers Home Administration (FmHA-assisted building), the applicable utility allowance for all rent-restricted units in the building is the utility allowance determined under the method prescribed by the Farmers Home Administration (FmHA) for the building. For example, if a building receives assistance under FmHA's section 515 program (whether or not the building or its tenants also receive other state or federal assistance), the applicable utility allowance for all rent-restricted units in the building is determined using Exhibit A-6 of 7 CFR part 1944, subpart E (or a successor method of determining utility allowances).

(2) *Buildings with FmHA assiste tenants.* If any tenant in a building receives FmHA rental assistance payments (FmHA tenant assistance), the applicable utility allowance for all rent-restricted units in the building (including any units occupied by tenants receiving HUD rental assistance payments) is the applicable FmHA utility allowance.

(3) *HUD-regulated buildings.* If neither a building nor any tenant in the building receives FmHA housing assistance, and the rents and utility allowances of the building are reviewed by HUD on an annual basis (HUD-regulated building), the applicable utility allowance for all rent-restricted units in the building is the applicable HUD utility allowance.

(4) *Other buildings.* If a building is neither an FmHA-assisted nor a HUD-regulated building, and no tenant in the building receives FmHA tenant assistance, the applicable utility allowance for rent-restricted units in th building is determined under the following methods.

(i) Tenants receiving HUD rental assistance. The applicable utility al-

lowance for any rent-restricted units occupied by tenants receiving HUD rental assistance payments (HUD tenant assistance) is the applicable Public Housing Authority (PHA) utility allowance established for the Section 8 Existing Housing Program.

(ii) Other tenants--(A) General rule. If none of the rules of paragraphs (b)(1), (2), (3), and (4)(i) of this section apply to any rent-restricted units in a building, the appropriate utility allowance for the units is the applicable PHA utility allowance. However, if a local utility company estimate is obtained for any unit in the building in accordance with paragraph (b)(4)(ii)(B) of this section, that estimate becomes the appropriate utility allowance for all rent-restricted units of similar size and construction in the building. This local utility company estimate procedure is not available for and does not apply to units to which the rules of paragraphs (b) (1), (2), (3), or (4)(i) of this section apply.

(B) Utility company estimate. Any interested party (including a low-income tenant, a building owner, or an Agency) may obtain a local utility company estimate for a unit. The estimate is obtained when the interested party receives, in writing, information from a local utility company providing the estimated cost of that utility for a unit of similar size and construction for the geographic area in which the building containing the unit is located. The local utility company estimate may be obtained by an interested party at any time during the building's extended use period (see section 42(h)(6)(D)) or, if the building does not have an extended use period, during the building's compliance period (see section 42(i)(1)). Unless the parties agree otherwise, costs incurred in obtaining the estimate are borne by the initiating party. The interested party that obtains the local utility company estimate (the initiating party) must retain the original of the utility company estimate and must furnish a copy of the local utility company estimate to the owner of the building (where the initiating party is not the owner), and the Agency that allocated credit to the building (where the initiating party is not the Agency). The owner of the building must make available copies of the utility company estimate to the tenants in the building.

(c) Changes in applicable utility allowance. If at any time during the building's extended use period (or, if the building does not have an extended use period, the building's compliance period), the applicable utility allowance for a unit changes, the new utility allowance must be used to compute gross rents of rent-restricted units due 90 days after the change. For example, if rent must be lowered because a local utility company estimate is obtained that shows a higher utility cost than the otherwise applicable PHA utility allowance, the lower rent must be in effect for rent due more than 90 days after the date of the local utility company estimate.

*§ 1.42-11 Provision of services.*

(a) General rule. The furnishing to tenants of services other than housing (whether or not the services are significant) does not prevent the units occupied by the tenants from qualifying as residential rental property eligible for credit under section 42. However, any charges to low-income tenants for services that are not optional generally must be included in gross rent for purposes of section 42(g).

(b) Services that are optional--(1) General rule. A service is optional if payment for the service is not required as a condition of occupancy. For example, for a qualified low-income building with a common dining facility, the cost of meals is not included in gross rent for purposes of section 42(g)(2)(A) if payment for the meals in the facility is not required as a condition of occupancy and a practical alternative exists for tenants to obtain meals other than from the dining facility.

(2) Continual or frequent services. If continual or frequent nursing, medical, or psychiatric services are provided, it is presumed that the services are not optional and the building is ineligible for the credit, as is the case with a hospital, nursing home, sanitarium, lifecare facility, or intermediate care facility for the mentally and physically handicapped. See also Sec. 1.42-9(b).

(3) Required services--(i) General rule. The cost of services that are required as a condition of occupancy must be included in gross rent even if federal or state law requires that the services be offered to tenants by building owners.

(ii) Exceptions--(A) Supportive services. Section 42(g)(2)(B)(iii) provides an exception for certain fees paid for supportive services. For purposes of section 42(g)(2)(B)(iii), a supportive service is any service provided under a planned program of services designed to enable residents of a residential rental property to remain independent and avoid placement in a hospital, nursing home, or intermediate care facility for the mentally or physically handicapped. For a building described in section 42(i)(3)(B)(iii) (relating to transitional housing for the homeless) or section 42(i)(3)(B)(iv) (relating to single-room occupancy), a supportive service includes any service provided to assist tenants in locating and retaining permanent housing.

(B) Specific project exception. Gross rent does not include the cost of mandatory meals in any federally-assisted project for the elderly and handicapped (in existence on or before January 9, 1989) that is authorized by 24 CFR 278 to provide a mandatory meals program.

*§ 1.42-12 Effective dates and transitional rules.*

(a) *Effective date.* The rules set forth in §§1.42-6 and 1.42-8 through 1.42-12 are effective May 2, 1994. However, binding agreements, election statements, and carryover allocation documents entered into before May 2, 1994, that follow the guidance set forth in Notice 89-1, 1989-1 C.B. 620 (see §601.601 (d)(2)(ii)(b) of this chapter) need not be changed to conform to the rules set forth in §§1.42-6 and 1.42-8 through 1.42-12.

(b) *Prior Periods.* Notice 89-1, 1989-1 C.B. 620 and Notice 89-6, 1989-1 C.B. 625 (see §601.601 (d)(2)(ii)(b) of this chapter) may be applied for periods prior to May 2, 1994.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 3. Part 602 is amended as follows:

1. The authority citation continues to read as follows:

Authority: 26 U.S.C. 7805

2. Section 602.10(c) is amended by adding entries in numerical order to the table to read as follows:

*§602.101 OMB control numbers.*

* * * * * *

(c) ***

# Internal Revenue Service
# Revenue Ruling 90-89
(Minimum Set-Aside Requirements)

*(Also Section 142.)*

**Low-income housing credit; minimum set-aside requirements.** For purposes of determining whether a building meets the minimum set-aside requirements of section 42(g)(1) of the Code, the combined income of all occupants of an apartment, whether or not legally related, is compared to the appropriate percentage of the median family income for a family with the same number of members.

**Rev. Rul. 90-89**

ISSUE

For purposes of determining whether a building meets the minimum set-aside requirements of section 42(g)(1) of the Internal Revenue Code, how is the appropriate percentage of the area median gross income determined for occupants of an apartment when those occupants are not legally related?

FACTS

The owner of a newly constructed building wants to qualify the building for the **low-income housing** credit under section 42(a) of the Code. The owner has elected to qualify under the 40-60 minimum set-aside requirement of section 42(g)(1)(B), under which 40 percent or more of the building's aggregate residential rental units must be occupied by individuals with incomes of 60 percent or less of the area median gross income.

A and *B* are unrelated individuals who want to rent a two-bedroom apartment in the building. A and *B* each has income that does not exceed 60 percent of the area median gross income for one individual. However, A and B's combined income exceeds 60 percent of the area median gross income for a two-individual family.

LAW AND ANALYSIS

Section 38(a) of the Code provides for a general business credit against tax that includes the amount of the current year business credit. Section 38(b)(5) provides that the amount of the current year business credit includes the **low-income housing** credit determined under section 42(a).

Section 42(a) of the Code provides that, for purposes of section 38, the amount of the **low-income housing** credit determined under section 42 for any tax year in the credit period shall be an amount equal to the "applicable percentage" of the qualified basis of each qualified low-income building.

Section 42(c)(2) of the Code defines the term "qualified low-income building" as any building: (A) that is part of a qualified **low-income housing** project at all times during the period (i) beginning on the first day in the compliance period on which the building is part of such a project, and (ii) ending on the last day of the compliance period with respect to the building, and (B) to which the amendments made by section 201(a) of the Tax Reform Act of 1986 apply.

Section 42(g)(1) of the Code defines the term "qualified low-income housing project" as any project for residential rental property if the project meets the requirements of subparagraphs (A) or (B), whichever the taxpayer elects. The election is irrevocable. The project meets the requirements of section 42(g)(1)(A) if 20 percent or more of the residential units in the project are both rent restricted and occupied by individuals whose income is 50 percent or less of area median gross income. The project meets the requirements of section 42(g)(1)(B) if 40 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 60 percent or less of area median gross income. This rule is known as the "minimum set-aside" requirement. 2 H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. II-92 (1986), 1986-3 (Vol. 4) C.B. 92.

Section 42(g)(4) of the Code provides, in part, that section 142(d)(2)(B) applies for purposes of determining whether any project is a **low income housing** project and whether any unit is a low-income unit. Section 142(d)(2)(B) states that the income of individuals and area median gross income shall be determined in a manner consistent with determinations of lower income families and area median gross income under section 8 of the United States Housing Act of 1937 (or, if the prograr is terminated, under the program as in effect immediately before such termination). Determinations of area median gross income under the preceding sentence are adjusted for family size. The determination of an individual's or family's income for purposes of section 8 of the Housing Act of 1937 may differ materially from that individual's or family's income for federal income tax purposes.

In order to satisfy the minimum set-aside requirements of section 42(g)(1) of the Code, a specified percentage of apartments in a **low income housing** project must be occupied by low-income tenants who meet the income limits of section 42(g)(1). Under sections 42(g)(1) and 142(d)(2)(B), tenants are considered low income by reference to the area median gross income as adjusted for family size. These sections require that the income of all individuals in a family that share an apartment be aggregated and compared to the area median gros. income for a family of the same size to determine if the minimum set-aside requirement is satisfied. Similarly, the income of all unrelated individuals who share an apartment should be aggregated and compared to the area median gross income for a family of the same size to determine if the minimum set-aside requirement is satisfied.

In this case, if A and *B* rent the apartment, that apartment does not count towards satisfying the minimum set-aside requirement of section 42(g)(1)(B) because A and *B's* combined income exceeds 60 percent of the area median gross income for a two-individual family.

HOLDING

For purposes of determining whether a building meets the minimum set-aside requirements of section 42(g)(1) of the Code, the combined income of all occupants of an apartment, whether or not legally related, is compared to the appropriate percentage of the median family income for a family with the number of members.

DRAFTING INFORMATION

The principal author of this revenue ruling is Paul F. Handleman of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue ruling contact Mr. Handleman on (202) 377-6349 (not a toll free call).

# Revenue Ruling 92-61
# Internal Revenue Service

# (Treatment of Resident Manager's Unit)

**Section 42.-Low-Income Housing Credit**

*(Also Sections 103, 142; 1.103-8.)*

**Full-time resident manager in building eligible for low-income housing credit.** The adjusted basis of a unit occupied by a full-time resident manager is included in the eligible basis of a qualified low-income building under section 42(d)(1) of the Code, but the unit is excluded from the applicable fraction under section 42(c)(1)(B) for purposes of determining the building's qualified basis.

**Rev. Rul. 92-61**

ISSUE

If a unit in a qualified low-income building is occupied by a full-time resident manager, is the adjusted basis of that unit included in the building's eligible basis under section 42(d)(1) of the Internal Revenue Code and is that unit included in the applicable fraction under section 42(c)(1)(B) for determining the qualified basis of the building?

FACTS

At the beginning of 1990, LP, a limited partnership with a calendar tax year, placed in service a newly constructed apartment building that qualified for the low-income housing credit under section 42(a) of the Code. *LP* elected to meet the 40-60 test of section 42(g)(1)(B), which requires that at least 40 percent of the units in the building be rent-restricted and occupied by tenants whose incomes are 60 percent or less of area median gross income. Throughout 1990, the first year of the building's credit period, 69 of the 70 units in the building were rent-restricted and occupied by tenants whose incomes were 60 percent or less of area median gross income. The remaining unit in the building was occupied by a resident manager who was hired by *LP* to manage the building and to be on call to attend to the maintenance needs of the other tenants. All of the units in the building meet the same standard of quality and have the same amount of floor space.

LAW AND ANALYSIS

Section 42(a) of the Code provides that the amount of the low-income housing credit determined for any tax year in the credit period is an amount equal to the applicable percentage of the qualified basis of each low income building.

Section 42(c)(1)(A) of the Code defines the qualified basis of any qualified low-income building for any tax year as an amount equal to the applicable fraction, determined as of the close of the tax year, of the eligible basis of the building, determined under section 42(d)(5).

Sections 42(c)(1)(B) of the Code defines the applicable fraction as the smaller of the unit fraction or the floor space fraction. Section 42(c)(1)(B) defines the unit fraction as the fraction the numerator of which is the number of low-income units in the building and the denominator of which is the number of residential rental units, whether or not occupied, in the building. Section 42(c)(1)(D) defines the floor space fraction as the fraction the numerator of which is the total floor space of the low income units in the building and the denominator of which is the total floor space of the residential rental units, whether or not occupied, in the building. In general, under section 42(i)(3)(B), a low-income unit is any unit that is rent-restricted and occupied by individuals meeting the income limitation applicable to the building.

Section 42(d)(1) of the Code provides that the eligible basis of a new building is its adjusted basis as of the close of the first tax year of the credit period. Section 42(d)(4)(A) provides that, except as provided in section 42(d)(4)(B), the adjusted basis of any building is determined without regard to the adjusted basis of any property that is not residential rental property. Section 42(d)(4)(B) provides that the adjusted basis of any building includes the adjusted basis of property of a character subject to the allowance for depreciation used in common areas or provided as comparable amenities to all residential rental units in the building.

The legislative history of section 42 of the Code states that residential rental property, for purposes of the low-income housing credit, has the same meaning as residential rental property within section 103. The legislative history of section 42 further states that residential rental property thus includes residential rental units, facilities for use by the tenants, and other facilities reasonably required by the project. 2 H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. II-89 (1986), 1986-3 (Vol. 4) C.B. 89. Under section 1.103-8(b)(4) of the Income Tax Regulations, facilities that are functionally related and subordinate to residential rental units are considered residential rental property. Section 1.103-8(b)(4)(iii) provides that facilities that are functionally related and subordinate to residential rental units include facilities for use by the tenants, such as swimming pools and similar recreational facilities, parking areas, and other facilities reasonably required for the project. The examples given by section 1.103-8(b)(4)(iii) of facilities reasonably required for a project specifically include units for resident managers or maintenance personnel.

Accordingly, the unit occupied by *LP's* resident manager is residential rental property for purposes of section 42 of the Code. The adjusted basis of the unit is includible in the building's eligible basis under section 42(d)(1). The inclusion of the adjusted basis of the resident manager's unit in eligible basis will not be affected by a later conversion of that apartment to a residential rental unit.

The term "residential rental unit" has a narrower meaning under section 42 of the Code than residential rental property. As noted above, under the legislative history of section 42, residential rental property includes facilities for use by the tenants and other facilities reasonably required by the project, as well as residential rental units. Under section 1.103-8(b)(4) of the regulations, units for resident

managers or maintenance personnel are not classified as residential rental units, but rather as facilities reasonably required by a project that are functionally related and subordinate to residential rental units.

LP's resident manager's unit is properly considered a facility reasonably required by the project, not a residential rental unit for purposes of section 42 of the Code. Consequently, the unit is not included in either the numerator or denominator of the applicable fraction under section 42(c)(1)(B) for purposes of determining the qualified basis of the building for the first year of the credit period.

Therefore, as of the end of the first year of the credit period, the adjusted basis of the unit occupied by *LP's* resident manager is included in the building's eligible basis under section 42(d)(1) of the Code, but the unit is excluded from the applicable fraction under section 42(c)(1)(B). Because all of the residential rental units in *LP's* building are low-income units, the applicable fraction for the building is "one" (69/69, using the unit fraction).

If in a later year of the credit period, the resident manager's unit is converted to a residential rental unit, the unit will be included in the denominator of the applicable fraction for that year. If the unit also becomes a low-income unit in that year, the unit will be included in the numerator of the applicable fraction for that year. In this case, the applicable fraction will also be "one" (70/70, using the unit fraction).

HOLDING

The adjusted basis of a unit occupied by a full-time resident manager is included in the eligible basis of a qualified low-income building under section 42(d)(1) of the Code, but the unit is excluded from the applicable fraction under section 42(c)(1)(B) for purposes of determining the building's qualified basis.

EFFECTIVE DATE

The Internal Revenue Service will not apply this revenue ruling to any building placed in service prior to September 9, 1992, or to any building receiving an allocation of credit prior to September 9, 1992, unless the owner files or has filed a return that is consistent with this ruling. Similarly, the Service will not apply this revenue ruling to any building described in section 42(h)(4)(B) of the Code with respect to which bonds were issued prior to September 9, 1992, unless the owner files or has filed a return that is consistent with this ruling.

DRAFTING INFORMATION

The principal author of this revenue ruling is Paul F. Handleman of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue ruling contact Mr. Handleman on (20) 622-3040 (not a toll free call).

# Revenue Ruling 94-57 Internal Revenue Service
## (Changes in Area Median Gross Income)

**Section 42. -- Low-Income Housing Credit**

*(Also Section 142.)*

**Low-income housing credit; changes in area median gross income; tenant qualification; available unit rule.** This ruling concludes that (1) the income limitation used to initially qualify tenants in a low-income unit fluctuates with changes in area median gross income, and (2) owners must use the current area median gross income to determine when the available unit rule of section 42(g)(2)(ii) applies. Rev. Rul. 89-24 modified and superseded.

**Rev . Rul. 94-57**

ISSUES

For the **low-income housing** credit under § 42 of the Internal Revenue Code:

(1) What is the effect of a change in area median gross income (AMGI) on the income limitation used to determine whether a tenant qualifies as a low-income tenant under § 42(g)(1)?

(2) What is the effect of a change in AMGI on the determination of whether any available residential unit must be rented to a new low-income tenant under § 42(g)(2)(D)(ii)?

FACTS

The Project, a single-building, qualified **low-income housing** project, received a housing credit dollar amount allocation from a housing credit agency (the Agency) in 1990. The Project was placed in service and began its credit period in 1991. When the Project owner first filed the Project's Form 8609, **Low-Income Housing** Credit Allocation Certification, the Project owner elected the 40-60 test of § 42(g)(1)(B).

In January 1992, the Tenant took initial occupancy of a rent-restricted residential unit in the Project. At the time the Tenant initially occupied the unit, 60 percent of AMGI, as adjusted for family size, in the area in which the Project is located, as defined in Rev. Rul. 89-24, 1989-1 C.B. 24, was $30x and the Tenant's annual income was $29x. Therefore, the unit that the Tenant occupied qualified as a low-income unit under § 42(i)(3).

On May 5, 1993, AMGI, as determined in a manner consistent with section 8 of the United States Housing Act of 1937 (H.U.D. section 8), decreased so that 60 percent of AMGI, as adjusted for family size, in the area in which the Project is located was $25x.

On March 30, 1994, the Tenant's annual income was recertified under § 1.42-5(b)(1)(vi) of the Income Tax Regulations at $36x.

On April 1, 1994, another residential unit in the Project, which was not a low-income unit, became vacant. That unit is of comparable size to the unit occupied by the Tenant. As of April 1, 1994, 60 percent of AMGI remained $25x, as adjusted for family size. At all times, the unit occupied by the Tenant remained rent restricted.

LAW

Section 42(g)(1) defines a "qualified **low-income housing** project" as any project for residential rental use that meets one of the following requirements: (A) 20 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 50 percent or less of AMGI, as adjusted for family size, or (B) 40 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 60 percent or less of AMGI, as adjusted for family size. These requirements are referred to as the minimum set-asides. Section 142(d)(1) contains similar requirements for exempt facility bonds the net proceeds of which are to be used to provide qualified residential rental projects.

Section 42(i)(3)(A) defines the term "low-income unit" as any unit in a building if: (i) the unit is rent restricted (as defined in § 42(g)(2)), and (ii) the individuals occupying the unit meet the income limitation applicable under § 42(g)(1) to the project of which the building is a part (low income tenants).

Section 42(g)(2)(D)(i) provides that, except as provided in § 42(g)(2)(D)(ii), notwithstanding an increase in the income of the occupant of a low-income unit above the income limitation applicable under § 42(g)(1), the unit continues to be treated as a low-income unit if the income of the occupants initially met the income limitation and the unit continues to be rent-restricted. Section 42(g)(2)(D)(ii) provides, however, that if the income of the occupants of the unit increases above 140 percent of the income limitation applicable under § 42(g)(1), a unit ceases to qualify as a low-income unit if any residential unit in the building (of a size comparable to, or smaller than, the unit) is occupied by a new resident whose income exceeds the income limitation. Section 142(d)(3) contains similar requirements for exempt facility bonds the net proceeds of which are to be used to provide qualified residential rental projects.

Under § 42(g)(4), § 142(d)(2)(B) applies when determining whether any project is a qualified **low-income housing** project and whether any unit is a low-income unit. Section 142(d)(2)(B) provides that the income of individuals and AMG1 is determined in a manner consistent with determinations of lower income families and AMGI under H.U.D. section 8. Accordingly, the determinations of lower income families and AMGI under H.U.D. section 8 apply to § 42(g)(1) and, therefore, to § 42(g)(2) and § 42(i)(3).

ANALYSIS

Issue 1. For a unit to be a low income unit, a low-income tenant must meet the applicable income limitation elected by a project owner under § 42(g)(1) at the time the tenant initially occupies a rent-restricted residential unit in the owner's project. If a tenant initially satisfied the applicable income limitation, the unit remains a low-income unit, except as provided in § 42(g)(2)(D)(ii), notwithstanding an increase in the tenant's income (assuming the unit continues to be rent-restricted). See 2 H.R. Conf. Rep. No. 841, 99th Cong.,

2d Sess. II-93 (1986). Similarly, if AMGI decreases in a project's area, a low-income tenant who occupied a residential unit prior to the decrease in AMGI will continue to qualify as a low-income tenant if the tenant qualified as a low-income tenant at the time of the tenant's initial occupancy. Thus, a change in a tenant's income or a change in AMG1 occurring subsequent to the tenant's initial occupancy does not cause that tenant to cease to be a low-income tenant as of initial occupancy.

On the other hand, a decrease in AMGI commensurately decreases the income limitation under § 42(g)(1) used to determine whether a tenant initially qualifies as a low-income tenant if the tenant's initial occupancy occurs on or after the effective date of the decrease in AMGI. Likewise, an increase in AMGI commensurately increases the income limitation under § 42(g)(1) used to determine whether a tenant initially qualifies as a low income tenant if the tenant's initial occupancy occurs on or after the effective date of the increase in AMGI. Therefore, a tenant that initially occupies a residential unit after the effective date of a change in AMGI (whether AMGI increases or decreases for the area) must qualify based on the AMGI in effect at the time the tenant initially occupies the unit.

Under the facts presented, as of its initial occupancy, the Tenant is a low-income tenant because the Tenant's annual income at the time the Tenant initially occupied a residential unit in the Project, $29x, was less than the income limitation applicable to the Project, $30x, as adjusted for family size. The result would be the same under § 142(d)(1).

*Issue 2.* Notwithstanding the analy *sis of Issue 1,* if the income of the occupants in a low-income unit increases above 140 percent of the income limitation under § 42(g)(1), that unit ceases to qualify as a low-income unit unless the project owner rents any available residential unit of comparable or smaller size to a new low-income tenant. A decrease in AMGI decreases the income limitation under § 42(g)(1). Accordingly, a decrease in AMGI decreases the income limitation used to calculate whether a project owner must rent any available residential unit of comparable or smaller size to a new low-income tenant under § 42(g)(2)(D)(ii). Likewise, an increase in AMGI increases the income limitation under § 42(g)(2)(D)(ii) used to calculate whether a project owner must rent any available residential unit of comparable or smaller size to a new low-income tenant.

On April 1, 1994, 140 percent of the applicable income limitation for the Project was $35x (1.4 times $25x), as adjusted for family size. Because the Tenant's annual income is $36x, for the Tenant's unit to continue to qualify as a low-income unit, the Project owner must rent the residential unit that became vacant on April 1, 1994, to a tenant whose income does not exceed the applicable income limitation *of* $25x, as adjusted for family size. The result would be the same under § 142(d)(3).

HOLDINGS

(1) A decrease in AMGI commensurately decreases the income limitation under § 42(g)(1) used to determine whether a tenant initially qualifies as a low-income tenant if the tenant's initial occupancy occurs on or after the effective date of the decrease in AMGI. Likewise, an increase in AMGI commensurately increases the income limitation under § 42(g)(1) used to determine whether a tenant initially qualifies as a low-income tenant if the tenant's initial occupancy occurs on or after the effective date of the increase in AMGI. This holding would also apply under § 142(d)(1).

(2) A decrease in AMGI decreases the income limitation used to calculate whether a project owner must rent any available residential unit of comparable or smaller size to a new low-income tenant under § 42(g)(2)(D)(ii). Likewise, an increase in AMGI increases the income limitation used to calculate whether a project owner must rent any available residential unit of comparable or smaller size to a new low-income tenant under § 42(g)(2)(D)(ii). This holding would also apply under § 142(d)(3).

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 89-24, 1989-1 C.B. 24, 25, provides that a list of income limits released by the Department of Housing and Urban Development (HUD) may be relied upon until 30 days after the Internal Revenue Service publishes an announcement or notice in the Internal Revenue Bulletin indicating that HUD has released updated income limits. Rev. Rul. 89-24 is modified and superseded. In the future, taxpayers may rely on a list of income limits released by HUD until 45 days after HUD releases a new list of income limits, or until HUD's effective date for this new list, whichever is later. However, under § 7805(b), taxpayers may rely on the income limits in effect prior to May 5, 1993, until 30 days after September 12, 1994.

PROSPECTIVE APPLICATION

The Service will not retroactively apply the holdings in this revenue ruling to the extent the holdings in this revenue ruling adversely affect taxpayers.

DRAFTING INFORMATION

The principal author of this revenue ruling is Jeffrey A. Erickson of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue ruling contact Mr. Erickson at (202) 377-6349 (not a toll free call).

# Internal Revenue Service Revenue Procedure 94-57
## (Gross Rent Floor)

**Rev. Proc. 94-57**

**1. PURPOSE**

This revenue procedure informs owners of qualified low-income housing projects and housing credit agencies (Agencies) when the gross rent floor in section 42(g)(2)(A) of the Internal Revenue Code takes effect.

**2. BACKGROUND**

On May 5, 1993, new area median gross income (AMGI) figures went into effect for the United States Department of Housing and Urban Development programs and other federal programs that use AMGI figures, including the section 42 low-income housing tax credit program. In some areas, the AMGI level fell below previous levels.

Section 42(g)(1) defines a qualified low-income housing project as any project for residential rental use that meets one of the following requirements: (A) 20 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 50 percent or less of AMGI, as adjusted for family size, or (B) 40 percent or more of the residential units in the project are both rent restricted and occupied by individuals whose income is 60 percent or less of AMGI, as adjusted for family size.

Section 42(g)(2)(A) provides that, under section 42(g)(1), a residential unit is rent restricted if the gross rent for the unit does not exceed 30 percent of the imputed income limitation applicable to the unit. Under section 42(g)(2)(C), the imputed income limitation applicable to a unit is the income limitation that would apply under section 42(g)(1) to individuals occupying the unit if the number of individuals occupying the unit were as follows: (i) in the case of a unit that does not have a separate bedroom, one individual, or (ii) in the case of a unit that has one or more separate bedrooms, 1.5 individuals for each separate bedroom.

For calculating gross rent on a rent-restricted unit, section 7108(e)(2) of the Revenue Reconciliation Act of 1989, 1990-1 C.B. 214, 220, amended section 42(g)(2)(A) to provide that the amount of the income limitation under section 42(g)(1) applicable for any period is not less than the limitation applicable for the earliest period the building that contains the unit was included in the determination of whether the project is a qualified low-income housing project (the gross rent floor). Section 42(g)(3)(A) provides that, except as otherwise provided in section 42(g)(3), a building is treated as a qualified low-income building only if the project (of which the building is a part) meets the requirements of section 42(g)(1) not later than the close of the first year of the credit period for the building.

Section 42(h)(1)(A) provides that the amount of credit determined under section 42 for any taxable year for any building shall not exceed the housing credit dollar amount allocated to the building under section 42(h). Under section 42(m)(2)(A), the housing credit dollar amount allocated to a project shall not exceed the amount an Agency determines is necessary for the financia feasibility of the project and its viability as a qualified low- income housing project throughout the credit period. Section 42(m)(2)(B) provides that in making the determination under section 42(m)(2)(A), an Agency shall consider (i) the sources and uses of funds and the total financing planned for the project, (ii) any proceeds or receipts expected to be generated by reason of tax benefits, (iii) the percentage of housing credit dollar amounts used for project costs other than the cost of intermediaries, and (iv) the reasonableness of the developmental and operational costs of the project. The gross rent under section 42(g)(2)(A) that a low-income housing project may generate is a source of funds an Agency must consider in making the determination under section 42(m)(2)(A).

Section 42(h)(4)(A) provides that section 42(h)(1) does not apply to the portion of any credit allowable under section 42(a) that is attributable to eligible basis financed by any obligation the interest on which is exempt from tax under section 103 if (i) the obligation is taken into account under section 146,

and (ii) principal payments on the financing are applied within a reasonable period to redeem obligations the proceeds of which were used to provide the financing. Section 42(h)(4)(B) provides that for purposes of section 42(h)(4)(A), if 50 percent or more of the aggregate basis of any building and the land on which the building is located is financed by an obligation described in section 42(h)(4)(A), section 42(h)(1) does not apply to any portion of the credit allowable under section 42(a) for the building. Section 42(m)(2)(D) provides that section 42(h)(4) does not apply to any project unless the governmental unit that issued the bonds (or on behalf of which the bonds were issued) makes a determination under rules similar to the rules of section 42(m)(2)(A) and (B). Upon making this determination, an Agency will issue a "determination letter" to a building.

Under section 1.42-13(a) of the Income Tax Regulations, the Secretary may provide guidance through various publications in the Internal Revenue Bulletin to carry out the purposes of section 42.

**3. SCOPE**

This revenue procedure applies to Agencies and owners of qualified low-income housing projects, as defined by section 42(g)(1).

**4. PROCEDURE**

Except for a low-income building described in section 42(h)(4)(B) (a bond-financed building), the Internal Revenue Service will treat the gross rent floor in section 42(g)(2)(A) as taking effect on the date an Agency initially allocates a housing credit dollar amount to the building under section 42(h)(1). However, the Service will treat the gross rent floor as taking effect on a building's placed in service date if the building owner designates that date as the date on which the gross rent floor will take effect for the building. An owner must make this designation to use the placed in service date and inform the Agency that made the allocation to the building no later than the date on which the building is placed in service.

For a bond-financed building, the Service will treat the gross rent floor in section 42(g)(2)(A) as taking effect on the date an Agency initially issues a determination letter to the building. However, the Service will treat the gross rent floor as taking effect on a building's placed in service date if the building owner designates that date as the date on which the gross rent floor will take effect for the building. An owner must make this designation to use the placed in service date and inform the Agency that issued the determination letter to the building no later than the date on which the building is placed in service.

An Agency should establish a procedure that will allow an owner to inform the Agency of this designation no later than the date the owner's building is placed in service.

For the effect of a change in AMGI on the initial qualification of a tenant as a low income tenant and the available unit rule, see Rev. Rul. 94-57.

**5. EFFECTIVE DATE**

This revenue procedure is effective for low-income housing projects receiving initial allocations or determination letters issued after * . For those projects that received initial allocations or determination letters prior to this effective date, for purposes of establishing the gross rent floor in section 42(g)(2)(A), owners and Agencies may use a date based on a reasonable interpretation of section 42.

**DRAFTING INFORMATION**

The principal author of this revenue procedure is Jeffrey A. Erickson of the Office of the Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure, contact Mr. Erickson at (202) 622-3040 (not a toll free call).

# Internal Revenue Service Notice 88-80

(Income Determination)

Regulations will be issued under Section 42(gX1) stating that, for purposes of determining qualification as a low-income housing project, the income of individuals and area median gross income will be determined in a manner consistent with the determination of annual income and the estimates for median family income under Section 8 of the U.S. Housing Act of 1937.

Under Section 8 of the Housing Act, median family income estimates are based on decennial Census data updated with Bureau of the Census P-60 income data and Department of Commerce County Business Patterns employment and earnings data. For purposes of these estimates, the term income includes some items that are not included in a taxpayer's gross income for federal income tax purposes.

Full Text: The purpose of this Notice is to inform taxpayers that regulations to be issued under section 42(gX1) of the Internal Revenue Code of 1986 (the "Code") (relating to the determination of a qualified low-income housing project) will provide that the income of individuals and area median gross income (adjusted for family size) are to be made in a manner consistent with the determination of annual income and the estimates for median family income under section 8 of the United States Housing Act of 1937 (H.U.D. section 8).

For purposes of H.U.D. section 8, annual income is defined under 24 CFR 813.106 (1987). HUD section 8 median family income estimates (i.e., area median gross income estimates are based on decennial Census data updated with Bureau of the Census P-60 income data and the Department of Commerce County Business Patterns employment and earnings data. The determination of annual income and median family income estimates are based on definitions of income that include some items of income that are not included in a taxpayer's gross income for purposes of computing Federal Income Tax liability. Thus, the income of individuals and are median gross income (adjusted for family size) for the purposes of section 42(gX1) of the Code will not be made by reference to items of income used in determining gross income for purposes of computing Federal Income Tax liability.

This document serves as an "administrative pronouncement" as that term is described in section 1.6661-3(bX2) of the Income Tax Regulations and may be relied upon to the same extent as a revenue ruling or revenue procedure.

The principal author of this Notice is Christopher J. Wilson of the Legislation and Regulations Division. For further information regarding this Notice contact Mr. Wilson on (202) 566-4336 (not a toll-free call).

# INTERNAL REVENUE SERVICE'S ADVANCE NOTICE 88-116, ON THE LOW-INCOME HOUSING TAX CREDIT, ISSUED OCT. 12, 1988

## (Placement in Service)

Notice 88-116

Low-Income Housing Tax Credit--Carryover of 1989 Credits for Certain Projects in Progress, Description of Construction, Reconstruction or Rehabilitation, Placed in Service

Section 42(n)(1) of the Internal Revenue Code (the "Code") provides, generally, that the State housing credit ceiling under section 42(h) shall be zero for any calendar year after 1989. Thus, in general, all buildings eligible for the low-income housing credit must be placed in service before January 1, 1990. Under section 42(n)(2), however, 1989 credit amounts that are not allocated in 1989 may be applied to a building placed in service in 1990 if such building is constructed, reconstructed, or rehabilitated by the taxpayer and more than 10 percent of the reasonably anticipated cost of such construction, reconstruction, or rehabilitation has been incurred as of January 1, 1989. The purpose of this Notice is to provide guidance to taxpayers under section 42(n) of the Code regarding (1) what costs will be considered construction, reconstruction, or rehabilitation costs; and (2) when such costs will be considered to be incurred. In addition, this Notice provides guidance regarding when a building will be considered to be placed in service for purposes of section 42.

CONSTRUCTION, RECONSTRUCTION OR REHABILITATION COSTS

For purposes of section 42(n), the term construction, reconstruction, or rehabilitation costs means any amount that is (1) properly chargeable to a capital account and (2) incurred before or on January 1, 1989. Amounts are chargeable to a capital account if they are properly includible in computing eligible basis under section 42(d). Amounts treated as an expense and deducted in the year they are paid or incurred or amounts that are otherwise not added to eligible basis do not qualify. For example, the cost of acquisition of an existing building is a qualifying cost. Amounts incurred for taxes and architectural and engineering fees, site survey fees, legal expenses, insurance premiums, development fees, and other construction related costs satisfy the definition of construction, reconstruction, or rehabilitation costs if they are included in the eligible basis of the building. Production period interest (within the meaning of section 263A(f)) allocable to the construction, reconstruction, or rehabilitation of a building is a qualifying cost. The cost of land is not a qualifying cost. For purposes of section 42(n), the total anticipated costs of construction, reconstruction, or rehabilitation shall be determined by reference to a reasonable estimate, on or before January 1, 1989, of such amount.

COSTS INCURRED AS OF JANUARY 1, 1989

Construction, reconstruction, or rehabilitation costs are incurred for purposes <Page 450> of this section on the date such expenditures would be considered incurred under an accrual method of accounting, regardless of the method of accounting used by the taxpayer incurring the costs with respect to other items of income and expense.

PLACED IN SERVICE

For purposes of section 42, the term "placed in service" has two definitions--one for buildings and one for rehabilitation expenditures that are treated as a separate new building (section 42(e)(4)(A)). The placed-in-service date for a new or existing building used as residential rental property is the date on which the building is ready and available for its specifically assigned function, i.e., the date on which the first unit in the building is certified as being suitable for occupancy in accordance with state or local law. 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.

Under section 42(e)(4)(A) of the Code, rehabilitation expenditures that are treated as a separate new building are placed in service at the close of any 24-month period, over which such expenditures are aggregated. The placed-in-service date of section 42(e)(4)(A) applies even if the building is occupied during the rehabilitation period.

A building may be placed in service even if the rental units in the building are not currently occupied by low-income tenants.

This document serves as an "administrative pronouncement" as that term is described in 1.661-3(b)(2) of the Income Tax Regulations and may be relied upon to the same extent as a revenue ruling or revenue procedure.

# Revenue Ruling 89-24
# Internal Revenue Service

**Section 142.-Exempt Facility Bond**

*(Also Sections 42, 103, 6652; 1.42-1T, 1.103-8.)*

**Exempt facility bonds; low-income housing credit** . Guidance is provided for computing the income limits applicable to exempt facility bonds issued to provide for qualified residential rental projects under section 142 of the Code and to low-income housing credits under section 42.

**Rev. Rul. 89-24**

This revenue ruling provides the manner in which properly to compute the income limits applicable both to exempt facility bonds issued to provide for qualified residential rental projects under section 142 of the Internal Revenue Code and to low-income housing credits under section 42.

LAW

**Section 1301** of the **Tax Reform Act** of 1986, 1986-3 (Vol. 1) C.B. 524 (the Act), revised the income limits applicable to exempt facility bonds issued to provide for multifamily residential rental projects. *Compare* section 142(d) and former section 103(b)(4)(A) of the Code.

In general. in order for interest on an exempt facility bond issued to provide for a multifamily residential rental project to be tax-exempt, the project must meet the income limit requirement of section 142(d)(1) of the Code. Under section 142(d)(1), a "qualified residential rental project" is defined to include only residential rental projects where. either (A) 20 percent or more of the residential units in the project are occupied by individuals whose income is 50 percent or less of the area median gross income (the 20-50 requirement), or (B) 40 percent or more of the residential units in the project are occupied by individuals whose income is 60 percent or less of the area median gross income (the 40-60 requirement), whichever is elected by the issuer of the bonds providing for such project.

Section 142(d)(4) of the Code provides that, in the case of a deep rent skewed project, 15 percent or more of the low-income units must be occupied by individuals whose income is 40 percent or less of the area median gross income.

Section 142(d)(2) of the Code provides that the income of individuals and the area median gross income shall be determined by the Secretary in a manner consistent with determinations of lower income families and area median gross income under section 8 of the United States Housing Act of 1937 or, if such program is terminated, under such program as in effect immediately before such termination. Determinations under the preceding sentence shall include adjustments for family size.

Section 252 of the Act enacted section 42 of the Code, which provides a new federal income tax credit that may be claimed by owners of residential rental projects providing low-income housing. Section 42(a) provides that the amount of the credit shall be based on an applicable percentage of the qualified basis of each qualified low-income building. Section 42(c)(2) defines the term "qualified low-income building" to mean, in part, any building that at all times during the compliance period with respect to such building is part of a qualified low-income housing project.

Section 42(g)(1) provides that the term "qualified low-income housing project" means any project for residential rental property if, either (A) 20 percent or more of the units in the project are both rent restricted and occupied by individuals whose income is 50 percent or less of the area median gross income, or (B) 40 percent or more of the units in the project are both rent-restricted and occupied by individuals whose income is 60 percent or less of the area median gross income, whichever is elected by the taxpayer.

Section 42(g)(4) of the Code provides, in part, that paragraph (2) (other than subparagraph (A)) and paragraph (4) of section 142(d) shall apply for purposes of determining whether any project is a qualified low-income housing project and whether any unit is a low-income unit.

ANALYSIS AND HOLDING

The income limits applicable to qualified residential rental projects and to qualified low-income housing projects are required to be made in a manner consistent with determinations of lower income families under section 8 of the United States Housing Act of 1937. With respect to the 20-50 requirement of sections 142(d)(1)(A) and 42(g)(1)(A) of the Code, 20 percent or more of the applicable units must be occupied by individuals or families having incomes equal to or less than the income limit tier a "very low-income" family of the same size. With respect to the 40-60 requirement of sections 142(d)(1)(B) and 42(g)(1)(B), 40 percent of the applicable units must be occupied by individuals or families having incomes equal to 120 percent or less of the income limit for a very low-income family of the same size.

With respect to certain deep rent skewed projects, as described in section 142(d)(4), the determination of whether 15 percent of the low-income units are occupied by individuals having incomes equal to 40 percent or less of the area median gross income shall be made by determining whether 15 percent of such units are occupied by individuals or families having incomes equal to or less than 80 percent of the income limit for a very low-income family of the same sire.

The income limits for very low - income families are computed and listed, according to family size, by the Department of Housing and Urban Development (HUD) for every Metropolitan Statistical Area, Primary Metropolitan Statistical Area, and non metropolitan county of the United States and Puerto Rico. HUD also releases income limits for the possessions of Guam and the Virgin Islands.

A list of income limits released by HUD may be relied upon until 30 days alter the Internal Revenue Service publishes an announcement or notice in the Internal Revenue Bulletin indicating that HUD has released updated income limits.

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 8732]

RIN 1545–AT60

## Available Unit Rule

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations concerning the treatment of low-income housing units in a building that is occupied by individuals whose incomes increase above 140 percent of the income limitation applicable under section 42(g)(1). These regulations effect owners of those buildings who claim the low-income housing tax credit.

DATES: These regulations are effective September 26, 1997.

For dates of applicability of these regulations, see § 1.42–15(i).

FOR FURTHER INFORMATION CONTACT: David Selig, (202) 622–3040 (not a tollfree number).

SUPPLEMENTARY INFORMATION:

### Background

On May 30, 1996, the IRS published a notice of proposed rulemaking in the **Federal Register** (PS–29–95 at 61 FR 27036) proposing amendments to the Income Tax Regulations (26 CFR part 1) under section 42(g)(2)(D) of the Internal Revenue Code. A public hearing was scheduled for September 17, 1996, pursuant to a notice of public hearing published simultaneously with the notice of proposed rulemaking. However, the IRS received no requests to speak at the public hearing, and no public hearing was held. Written comments responding to the notice were received. After consideration of all the comments, the proposed regulations are adopted as revised by this Treasury decision.

*Explanation of Revisions and Summary of Comments*

The general rule in section 42(g)(2)(D)(i) provides that if the income

of an occupant of a low-income unit increases above the income limitation applicable under section 42(g)(1), the unit continues to be treated as a low income unit. This general rule only applies if the occupant's income initially met the income limitation and the unit continues to be rent-restricted. Section 42(g)(2)(D)(ii), however, provides an exception to the general rule in section 42(g)(2)(D)(i). Under this exception, the unit ceases being treated as a low-income unit when two conditions occur. The first condition is that the occupant's income increases above 140 percent of the income limitation applicable under section 42(g)(1), or above 170 percent for a deep rent skewed project described in section 142(d)(4)(B) (applicable income limitation). When this occurs, the unit becomes an over-income unit. The second condition is that a new occupant, whose income exceeds the applicable income limitation (non-qualified resident), occupies any residential unit in the building of a compare-able or smaller size (comparable unit).

*Rules and Definitions*

One commentator suggested that the available unit rule under the proposed regulations did not clearly indicate whether the aggregate income of all occuppants of a unit is taken into account. Accordingly, the final regulations clarify that an over-income unit means a low-income unit in which the aggregate income of the occupants of the unit increases above 140 percent of the applicable income limitation under section 42(g)(1), or above 170 percent of the applicable income limitation for deep rent skewed projects described in section 142(d)(4)(B).

Commentators requested that the final regulations specify whether a comparable unit is measured by floor space or number of bedrooms. The final regulations provide that a comparable unit must be measured by the same method the taxpayer used to determine qualified basis for the credit year in which the comparable unit became available.

Some commentators stated that the provision in the proposed regulations that all available comparable units (not just the "next available" unit) must be rented to qualified residents to continue treating an over-income unit as a lowincome unit is inconsistent with the title of section 42(g)(2)(D)(ii). Although the title of that provision uses the term next available unit, the text of the rule provides that if any available comparable unit is occupied by a nonqualified resident, the over-income unit ceases to be treated as a low income unit. This means that if a building has more than one over-income unit, renting any available comparable unit (a comparably sized or smaller unit) to a qualified resident preserves the status of all over-income units as low-income units. Similarly, if any available comparable unit is rented to a nonqualified resident, all over-income units for which the available unit was a comparable unit lose their status as low-income units; thus, comparably sized or larger over-income units would lose their status as low-income units. In operation, this means that the owner must continue to rent any available comparable unit to a qualified resident until the percentage of low-income units in a building (excluding the over income units) is equal to the percentage of low-income units on which the credit is based. At that point, failure to maintain the over-income units as low income units has no immediate significance. (However, the failure to maintain an over-income unit as a low income unit may affect the owner's decision of whether or not to rent a particular available unit at market rate at a later time.) Consequently, the final regulations provide that all available comparable units in the building, not only the next available comparable unit, must be rented to qualified residents to retain the low-income status of the over income units.

*Application of Rules on a Building by Building Basis*

The proposed regulations provide that in a project containing more than one low-income building, the available unit rule applies separately to each building. Some commentators suggested that the regulations should permit residents of over-income units to move to available units in different buildings within the same low-income housing project without violating the available unit rule. However, because the requirements under section 42 must be satisfied on a building by building basis, the final regulations provide that the available unit rule only permits a current resident to move to another unit within the same building of a low-income housing project.

In addition, in response to requests from several commentators, the final regulations make clear that when a current resident moves to a different unit within the same low-income building, the units exchange status. (See example 2 of § 1.42–15(g) of the proposed regulations and § 1.42–15(h) of the final regulations.) Thus, the newly occupied unit adopts the status of the vacated unit, and the vacated unit assumes the status the newly occupied unit had immediately prior to its occupancy by the qualifying residents.

*Timing Issues*

The methods of committing rental units to tenants varies in different jurisdictions. However, it is a common rental practice to have some form of prelimnary reservation for a unit prior to the date on which a lease is signed or the unit is occupied. Thus, several commentators have requested clarification that once a unit is reserved for a prospective tenant, it is no longer treated as available for purposes of the available unit rule. Accordingly, the final regulations provide that a unit is not avail-able for purposes of the available unit rule when the unit is no longer available for rent due to a reservation that is binding under local law.

Finally, financing arrangements using obligations that purport to be exempt facility bonds under section 142 must meet the requirements of sections 103 and 141 through 150 for interest on the obligations to be excluded from gross income under section 103(a). The requirements under section 142(d) may differ from those under section 42. Accordingly, the final regulations provide that the rules under the final regulations are not intended as an interpretation of the applicable rules under section 142.

**Special Analyses**

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information: The principal author of these regulations is David Selig, Office of the Assistant Chief Counsel (Passthroughs and Special Industries), IRS. However, other personnel from the IRS and Treasury Department participated in their development.

**List of Subjects in 26 CFR Part 1**

Income taxes, Reporting and recordkeeping requirements.

**Adoption of Amendments to the Regulations**

Accordingly, 26 CFR part 1 is amended as follows:

**PART 1—INCOME TAXES**

**Paragraph 1.** The authority citation for part 1 is amended by adding an entry in numerical order to read as follows:

**Authority:** 26 U.S.C. 7805 * * * Section 1.42–15 is also issued under 26 U.S.C. 42(n); * * *

**Par. 2.** Section 1.42–15 is added to read as follows:

**§ 1.42–15 Available unit rule.**

(a) *Definitions.* The following definitions apply to this section:

*Applicable income limitation* means the limitation applicable under section 42(g)(1) or, for deep rent skewed projects described in section 142 (d) (4) (B), 40 percent of area median gross income.

*Available unit rule* means the rule in section 42(g)(2)(D)(ii).

*Comparable unit* means a residential unit in a low-income building that is comparably sized or smaller than an over-income unit or, for deep rent skewed projects described in section 142(d)(4)(B), any low-income unit. For purposes of determining whether a residential unit is comparably sized, a comparable unit must be measured by the same method used to determine qualified basis for the credit year in which the comparable unit became available.

*Current resident* means a person who is living in the low-income building.

*Low-income unit* is defined by section 42(i)(3)(A).

*Nonqualified resident* means a new occupant or occupants whose aggregate income exceeds the applicable income limitation.

*Over-income unit* means a low income unit in which the aggregate income of the occupants of the unit increases above 140 percent of the applicable income limitation under section 42(g)(1), or above 170 percent of the applicable income limitation for deep rent skewed projects described in section 142(d)(4)(B).

*Qualified resident* means an occupant either whose aggregate income (combined with the income of all other occupants of the unit) does not exceed the applicable income limitation and who is otherwise a low-income resident under section 42, or who is a current resident.

(b) *General section 42(g)(2)(D)(i) rule.* Except as provided in paragraph (c) of this section, notwithstanding an increase in the income of the occupants of a low-income unit above the applicable income limitation, if the income of the occupants initially met the applicable income limitation, and the unit continues to be rent-restricted—

(1) The unit continues to be treated as a low-income unit; and

(2) The unit continues to be included in the numerator and the denominator of the ratio used to determine whether a project satisfies the applicable minimum set-aside requirement of section 42(g)(1).

(c) *Exception.* A unit ceases to be treated as a low-income unit if it becomes an over-income unit and a nonqualified resident occupies any comparable unit that is available or that subsequently becomes available in the same low-income building. In other words, the owner of a low-income building must rent to qualified residents all comparable units that are available or that subsequently become available in the same building to continue treating the over-income unit as a low income unit. Once the percentage of low-income units in a building (excluding the over-income units) equals the percentage of low-income units on which the credit is based, failure to maintain the over-income units as low-income units has no immediate significance. The failure to maintain the over-income units as low income units, however, may affect the decision of whether or not to rent a particular available unit at market rate at a later time. A unit is not available for purposes of the available unit rule when the unit is no longer available for rent due to contractual arrangements that are binding under local law (for example, a unit is not available if it is subject to a preliminary reservation that is binding on the owner under local law prior to the date a lease is signed or the unit is occupied).

(d) *Effect of current resident moving within building.* When a current resident moves to a different unit within the building, the newly occupied unit adopts the status of the vacated unit. Thus, if a current resident, whose income exceeds the applicable income limitation, moves from an over-income unit to a vacant unit in the same building, the newly occupied unit is treated as an over-income unit. The vacated unit assumes the status the newly occupied unit had immediately before it was occupied by the current resident.

(e) *Available unit rule applies separately to each building in a project.* In a project containing more than one low-income building, the available unit rule applies separately to each building.

(f) *Result of noncompliance with available unit rule.* If any comparable unit that is available or that subsequently becomes available is rented to a nonqualified resident, all over-income units for which the available unit was a comparable unit within the same building lose their status as low-income units; thus, comparably sized or larger over-income units would lose their status as low income units.

(g) *Relationship to tax-exempt bond provisions.* Financing arrangements that purport to be exempt-facility bonds under section 142 must meet the requirements of sections 103 and 141 through 150 for interest on the obligations to be excluded from gross income under section 103(a). This section is not intended as an interpretation under section 142.

(h) *Examples.* The following examples illustrate this section:

*Example 1.* This example illustrates noncompliance with the available unit rule in a low-income building containing three over-income units. On January 1, 1998, a qualified low-income housing project, consisting of one building containing ten identically sized residential units, received a housing credit dollar amount allocation from a state housing credit agency for five low income units. By the close of 1998, the first year of the credit period, the project satisfied the minimum set-aside requirement of section 42(g)(1)(B). Units 1, 2, 3, 4, and 5 were occupied by individuals whose incomes did not exceed the income limitation applicable under section 42(g)(1) and were otherwise low-income residents under section 42. Units 6, 7, 8, and 9 were occupied by market-rate tenants. Unit 10 was vacant. To avoid recapture of credit, the project owner must maintain five of the units as low income units. On November 1, 1999, the certificates of annual income state that annual incomes of the individuals in Units 1, 2, and 3 increased above 140 percent of the income limitation applicable under section 42(g)(1), causing those units to become over income units. On November 30, 1999, Units 8 and 9 became vacant. On December 1, 1999, the project owner rented Units 8 and 9 to qualified residents who were not current residents at rates meeting the rent restriction requirements of section 42(g)(2). On December 31, 1999, the project owner rented Unit 10 to a market-rate tenant. Because Unit 10, an available comparable unit, was leased to a market-rate tenant, Units 1, 2, and 3 ceased to be treated as low-income units. On that date, Units 4, 5, 8, and 9 were the only remaining low-income units. Because the project owner did not maintain five of the residential units as low-income units, the qualified basis in the building is reduced, and credit must be recaptured. If the project owner had rented Unit 10 to a qualified resident who was not a current resident,

eight of the units would be low-income units. At that time, Units 1, 2, and 3, the over income units, could be rented to market-rate tenants because the building would still contain five low-income units.

*Example 2.* This example illustrates the pro-visions of paragraph (d) of this section. A low-income project consists of one six-floor building. The residential units in the building are identically sized. The building contains two over-income units on the sixth floor and two vacant units on the first floor. The project owner, desiring to maintain the over-income units as low-income units, wants to rent the available units to qualified residents. J, a resident of one of the over income units, wishes to occupy a unit on the first floor. J's income has recently increased above the applicable income limitation. The project owner permits J to move into one of the units on the first floor. Despite J's income exceeding the applicable income limitation, J is a qualified resident under the available unit rule because J is a current resident of the building. The unit newly occupied by J becomes an over-income unit under the available unit rule. The unit vacated by J assumes the status the newly occupied unit had immediately before J occupied the unit. The over-income units in the building continue to be treated as low-income units.

(i) *Effective date.* This section applies to leases entered into or renewed on and after September 26, 1997.

**Michael P. Dolan,**
*Acting Commissioner of Internal Revenue.*

Approved: August 26, 1997.

**Donald C. Lubick,**
*Acting Assistant Secretary of the Treasury.*

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# Section 1: Determining Annual Income

## 5-3 Key Regulations

This paragraph identifies the key regulatory citation pertaining to Section 1: Determining Annual Income. The citation and its title are listed below.

- 24 CFR 5.609 Annual Income

## 5-4 Key Requirements

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

1. 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

2. All amounts anticipated to be received from a source outside the family during the 12-month period following admission or annual recertification effective date.

B. Annual income includes all amounts that are not specifically excluded by regulation. Exhibit 5-1, Income Inclusions and Exclusions, provides the complete list of income inclusions and exclusions published in the regulations and *Federal Register* notices.

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

## 5-5 Methods for Projecting and Calculating Annual Income

A. The requirements for determining whether a family is eligible for assistance, and the amount of rent the family will pay, require the owner to project or estimate the annual income that the family expects to receive. There are several ways to make this projection. The following are two acceptable methods for calculating the annual income anticipated for the coming year:

1. Generally the owner must use current circumstances to anticipate income. The owner calculates projected annual income by annualizing *current* income. Income that may not last for a full 12 months (e.g., unemployment compensation) should be calculated assuming current circumstances will last a full 12 months. If changes occur later in the year, an interim recertification can be conducted to change the family's rent.

2. If information is available on changes expected to occur during the year, use that information to determine the total *anticipated* income from all known sources during the year**. For example, if a verification source reports that a union contract calls for a 2% pay increase midway through

the year, the owner may add the total income for the months before, and the total for the months after the increase**.

**Example – Calculating Anticipated Annual Income**

A teacher's assistant works nine months annually and receives $1,300 per month. During the summer recess, the teacher's assistant works for the Parks and Recreation Department for $600 per month. The owner may calculate the family's income using either of the following two methods:

1. Calculate annual income based on current income: $15,600 ($1,300 x 12 months).

   The owner would then conduct an interim recertification at the end of the school year to recalculate the family's income during the summer months at reduced annualized amount of $7,200 ($600 x 12 months). The owner would conduct another interim recertification when the tenant returns to the nine-month job.

2. Calculate annual income based on anticipated changes through the year:

   $11,700 ($1,300 x 9 months)

   + 1,800 ($ 600 x 3 months)

   $13,500

   Using the second method, the owner would not conduct an interim re-examination at the end of the school year. In order to use this method effectively, history of income from all sources in prior years should be available.

B. Once all sources of income are known and verified, owners must convert reported income to an annual figure. Convert periodic wages to annual income by multiplying:

   1. Hourly wages by the number of hours worked per year (2,080 hours for full-time employment with a 40-hour week and no overtime);

   2. Weekly wages by 52;

   3. Bi-weekly wages (paid every other week) by 26;

   4. Semi-monthly wages (paid twice each month) by 24; and

   5. Monthly wages by 12.

   To annualize other than full-time income, multiply the wages by the actual number of hours or weeks the person is expected to work.

**Example – Anticipated Increase in Hourly Rate**

February 1 Certification effective date
$7.50/hour Current hourly rate
$8.00/hour New rate to be effective March 15

(40 hours per week x 52 weeks = 2,080 hours per year)

| | |
|---|---|
| February 1 through March 15 = | 6 weeks |
| 6 weeks x 40 hours = | 240 hours |
| 2,080 hours minus 240 hours = | 1,840 hours |

(check: 240 hours + 1,840 hours = 2,080 hours)

Annual Income is calculated as follows:

| | | |
|---|---|---|
| 240 hours x $7.50 = | $1,800 | |
| $1,840 hours x $8.00 = | $14,720 | |
| Annual Income | | $16,520 |

(See **Appendix 8** for an explanation of the correct approach to rounding numbers.)

C. Some circumstances present more than the usual challenges to estimating anticipated income. Examples of challenging situations include a family that has sporadic work or seasonal income or a tenant who is self-employed. In all instances, owners are expected to make a reasonable judgment as to the most reliable approach to estimating what the tenant will receive during the year. In many of these challenging situations, midyear or interim recertifications may be required to reflect changing circumstances. Some examples of approaches to more complex situations are provided below.

**Examples – Irregular Employment Income**

Seasonal work. Clyde Kunkel is a roofer. He works from April through September. He does not work in rain or windstorms. His employer is able to provide information showing the total number of regular and overtime hours Clyde worked during the past three years. To calculate Clyde's anticipated income, use the average number of regular hours over the past three years times his current regular pay rate, and the average overtime hours times his current overtime rate.

Sporadic work. Justine Cowan is not always well enough to work full-time. When she is well, she works as a typist with a temporary agency. Last year was a good year and she worked a total of nearly six months. This year, however, she has more medical problems and does not know when or how much she will be able to work. Because she is not working at the time of her recertification, it will be best to exclude her employment income and remind her that she must return for an interim recertification when she resumes work.

**Examples – Irregular Employment Income**

Sporadic work. Sam Daniels receives social security disability. He reports that he works as a handyman periodically. He cannot remember when or how often he worked last year: he says it was a couple of times. Sam's earnings appear to fit into the category of nonrecurring, sporadic income that is not included in annual income. Tell Sam that his earnings are not being included in annual income this year, but he must report to the owner any regular work or steady jobs he takes.

Self-employment income. Mary James sells beauty products door-to-door on consignment. She makes most of her money in the months prior to Christmas but has some income throughout the year. She has no formal records of her income other than a copy of the IRS Form 1040 she files each year. With no other information available, the owner will use the income reflected on Mary's copy of her form 1040 as her annual income.

## 5-6 Calculating Income—Elements of Annual Income

### A. Income of Adults and Dependents

1. Figure 5-2 summarizes whose income is counted.

2. Adults. Count the annual income of the head, spouse or co-head, and other adult members of the family. In addition, persons under the age of 18 who have entered into a lease under state law are treated as adults, and their annual income must also be counted. These persons will be either the head, spouse, or co-head; they are sometimes referred to as emancipated minors.

   **NOTE**: If an emancipated minor is residing with a family as a member other than the head, spouse, or co-head, the individual would be considered a dependent and his or her income handled in accordance with subparagraph 3 below.

3. Dependents. A dependent is a family member who is under 18 years of age, is disabled, or is a full-time student

   The head of the family, spouse, co-head, foster child, or live-in aide are never dependents. Some income received on behalf of family dependents is counted and some is not.

   a. *Earned* income of minors (family members under 18) is not counted.

   b. Benefits or other *unearned* income of minors is counted.

**Figure 5-2: Whose Income is Counted?**

| Members | Employment Income | Other Income (including income from assets) |
|---|---|---|
| Head | Yes | Yes |
| Spouse | Yes | Yes |
| Co-head | Yes | Yes |
| Other adult *(including foster adult)* | Yes | Yes |
| Dependents | | |
| -Child under 18 | No | Yes |
| Full-time student over 18 | See Note | Yes |
| *Foster child under 18 | No | Yes* |
| **Nonmembers** | | |
| Live-in aide | No | No |

**NOTE:** The earned income of a full-time student 18 years old or older who is a dependent is excluded to the extent that it exceeds $480.

c. When more than one family shares custody of a child and both families live in assisted housing, only one family at a time can claim the dependent deduction. The family that counts the dependent deduction also counts the unearned income of the child. The other family claims neither the dependent deduction nor the unearned income of the child.

d. When full-time students who are 18 years of age or older are dependents, a small amount of their earned income will be counted. Count only earned income up to a maximum of $480 per year for full-time students, age 18 or older, who are not the head of the family or spouse or co-head. If the income is less than $480 annually, count all the income. If the annual income exceeds $480, count $480 and exclude the amount that exceeds $480.

e. The income of full-time students 18 years of age or older who are members of the household but away at school is counted the same as the income for other full-time students. The income of minors who are members of the household but away at school is counted as the income for other minors.

f. All income of a full-time student, 18 years of age or older, is counted if that person is the head of the family, spouse, or co-head.

g. Payments received by the family for the care of foster children or foster adults are *not* counted. This rule applies only to payments

made through the official foster care relationships with local welfare agencies.

h. Adoption assistance payments in excess of $480 are not counted.

B. **Income of Temporarily Absent Family Members**

1. Owners must count all income of family members approved to reside in the unit, even if some members are temporarily absent.

2. If the owner determines that an absent person is no longer a family member, the individual must be removed from the lease and the HUD-50059.

3. A temporarily absent individual on active military duty must be removed from the family, and his or her income must not be counted unless that person is the head of the family, spouse, or co-head.

   a. However, if the spouse or a dependent of the person on active military duty resides in the unit, that person's income must be counted in full, even if the military member is not the head, or spouse of the head of the family.

   b. The income of the head, spouse, or co-head will be counted even if that person is temporarily absent for active military duty.

**Examples – Income of Temporarily Absent Family Members**

- John Chouse works as an accountant. However, he suffers from a disability that periodically requires lengthy stays at a rehabilitation center. When he is confined to the rehabilitation center, he receives disability payments equaling 80% of his usual income.

  During the time he is not in the unit, he will continue to be considered a family member. The owner will conduct an interim recertification. Even though he is not currently in the unit, his total disability income will be counted as part of the family's annual income.

- Mirna Martinez accepts temporary employment in another location and needs a portion of her income to cover living expenses in the new location. The full amount of the income must be included in annual income.

- Charlotte Paul is on active military duty. Her permanent residence is her parents' assisted unit where her husband and children live. Charlotte is not currently exposed to hostile fire. Therefore, because her spouse and children are in the assisted unit, her military pay must be included in annual income. (If her dependents or spouse were not in the unit, she would not be considered a family member and her income would not be included in annual income.)

C. ***Deployment of Military Personnel to Active Duty**

Owners are encouraged to be as lenient as responsibly possible to support affected households in situation where persons are called to active duty in the Armed Forces. Specific actions that owners should undertake to support military households include, but are not limited to:*

1. *Allow a guardian to move into the assisted unit on a temporary basis to provide care for any dependents the military person leaves in the unit. Income of the guardian temporarily living in the unit for this purpose is not counted as income.

2. Allow a tenant living in an assisted unit to provide care for any dependents of persons called to active duty in the Armed Forces on a temporary basis, as long as the head and/or co-head of household continues to serve in active duty. Income of the child (e.g., SSI benefits, military benefits) is not counted as income of the person providing the care.

3. Exclude from annual income special pay received by a household member serving in the Armed Services who is exposed to hostile fire (see Exhibit 5-1).

4. Give consideration for any case involving delayed payment of tenant rent. Determine whether it is appropriate to accept a late payment.

5. Allow the assistance payment and the lease to remain in effect for a reasonable period of time (depending on the length of deployment) beyond that required by the Soldiers' and Sailors' Civil Relief Act of 1940, 50 U.S.C. §§ 501-591, even though the adult members of the military family are temporarily absent from the assisted unit.*

## D. Income of Permanently Confined Family Members

1. An individual permanently confined to a nursing home or hospital may not be named as family head, spouse, or co-head but may continue as a family member at the family's discretion. The family's decision on whether or not to include the permanently confined family member as a family member determines if that person's income will be counted.

   a. *Include* the individual as a family member and the income and allowable deductions related to the medical care of the permanently confined individual are counted; or

   b. *Exclude* the individual as a family member and the income and allowances based on the medical care of the permanently confined individual are not counted.

2. If the family elects to include the permanently confined member, the individual is listed on the HUD-50059 as an adult who is not the head, spouse, or co-head, even when the permanently confined family member is married to the person who is or will become the head of the family. The owner should consider extenuating circumstances that may prevent the confined member from being able to sign the HUD-50059. If the owner determines the confined member is unable to sign the HUD-50059,

the owner must document the file why the signature was not obtained. If the family elects not to include the permanently confined member, the individual would not be listed on the HUD-50059.**

E. **Educational Scholarships or Grants**

All forms of student financial assistance (grants, scholarships, educational entitlements, work study programs, and financial aid packages) are excluded from annual income **except for students receiving Section 8 assistance.** This is true whether the assistance is paid to the student or directly to the educational institution

**For students receiving Section 8 assistance, all financial assistance a student receives (1) under the Higher Education Act of 1965, (2) from private sources, or (3) from an institution of higher education that is in excess of amounts received for tuition is included in annual income except if the student is over the age of 23 with dependent children or the student is living with his or her parents who are receiving Section 8 assistance. See Paragraph 3-13 for further information on eligibility of students to receive Section 8 assistance and the Glossary for the definition of Student Financial Assistance.**

F. **Alimony or Child Support**

Owners must count alimony or child support amounts awarded by the court unless the applicant certifies that payments are not being made *and* that he or she has taken all reasonable legal actions to collect amounts due, including filing with the appropriate courts or agencies responsible for enforcing payment.

1. The owner may accept printouts from the court or agency responsible for enforcing support payments, or other evidence indicating the frequency and amount of support payments actually received.

2. Child support paid to the custodial parent through a state child support enforcement or welfare agency may be included in the family's monthly welfare check and may be designated in different ways. In some states these payments are not identified as separate from the welfare grant. In these states, it is important to determine which portion is child support and not to count it twice. In other states, the payment may be listed as child support or as "pass-through" payments. These amounts must be counted as annual income.

3. When no documentation of child support, divorce, or separation is available, either because there was no marriage or for another reason, the owner may require the family to sign a certification stating the amount of child support received.

G. **Regular Cash Contributions and Gifts**

1. Owners must count as income any regular contributions and gifts from persons not living in the unit. These sources may include rent and utility

payments paid on behalf of the family, and other cash or noncash contributions provided on a regular basis.

**Examples – Regular Cash Contributions**

- The father of a young single parent pays her monthly utility bills. On average he provides $100 each month. The $100 per month must be included in the family's annual income.
- The daughter of an elderly tenant pays her mother's $175 share of rent each month. The $175 value must be included in the tenant's annual income.

2. Groceries and/or contributions paid directly to the childcare provider by persons not living in the unit are excluded from annual income.

3. Temporary, nonrecurring, or sporadic income (including gifts) is not counted.

## H. Income from a Business

When calculating annual income, owners must include the net income from operation of a business or profession including self-employment income. Net income is gross income less business expenses, interest on loans, and depreciation computed on a straight-line basis.

1. In addition to net income, owners must count any salaries or other amounts distributed to family members from the business, and cash or assets withdrawn by family members, except when the withdrawal is a reimbursement of cash or assets invested in the business.

2. When calculating net income, owners must not deduct principal payments on loans, interest on loans for business expansion or capital improvements, other expenses for business expansion, or outlays for capital improvements.

3. If the net income from a business is negative, it must be counted as zero income. A negative amount must not be used to offset other family income.

## I. **Periodic Social Security Payments

Count the gross amount, before deductions for Medicare, etc., of periodic Social Security payments. Include payments received by adults on behalf of individuals under the age of 18 or by individuals under the age of 18 for their own support.**

## J. Adjustments for Prior Overpayment of Benefits

If an agency is reducing a family's benefits to adjust for a prior overpayment (e.g., social security, SSI, TANF, or unemployment benefits), count the amount that is actually provided after the adjustment.

**Example – Adjustment for Prior Overpayment of Benefits**

Lee Park's social security payment of $250 per month is being reduced by $25 per month for a period of six months to make up for a prior overpayment. Count his social security income as $225 per month for the next six months and as $250 per month for the remaining six months.

## K. Public Assistance Income in As-Paid Localities

1. Special calculations of public assistance income are required for "as-paid" state, county, or local public assistance programs. An "as-paid" system is one:

   a. In which the family receives an amount from a public agency specifically for shelter and utilities; and

   b. In which the amount is adjusted based upon the actual amount the family pays for shelter and utilities.

2. The public assistance amount specifically designated for rent and utilities is called the "welfare rent."

3. To determine annual income for public assistance recipients in "as-paid" localities, include the following:

   a. The amount of the family's grant for other than shelter and utilities; and

   b. The maximum amount the welfare department can pay for shelter and utilities for a family of that size (i.e., the welfare rent). This may be different from the amount the family is actually receiving.

4. Each as-paid locality works somewhat differently, and many are subject to court-ordered modifications to the basic policy. Owners should discuss how the rules are applied with the HUD Field Office.

**Example – Welfare Income in "As Paid" Localities**

At application, a family's welfare grant is $300, which includes $125 for basic needs and $175 for shelter and utilities (based upon where the family is now living). However, the maximum the welfare agency could allow for shelter and utilities for this size family is $190.

Count the following as income:

| | |
|---|---|
| $125 | Amount family receives for basic needs |
| $190 | Maximum for shelter and utilities |
| $315 | Monthly public assistance income |

## L. Periodic Payments from Long-Term Care Insurance, Pensions, Annuities, and Disability or Death Benefits

1. The full amount of periodic payments from annuities, insurance policies, retirement funds, pensions, and disability or death benefits is included in annual income. (See subparagraph O below for information on the withdrawal of cash or assets from an investment.) Payments such as Black Lung Sick Benefits, Veterans Disability, and Dependent Indemnity Compensation for the Widow of a Killed in Action Serviceman are examples of such periodic payments.

2. Withdrawals from retirement savings accounts such as Individual Retirement Accounts and 401K accounts that are not periodic payments do not fall in this category and are not counted in annual income (see paragraph 5.7 G.4).

**Example – Withdrawals from IRAs or 401K Accounts**

Isaac Freeman retired recently. He has an IRA account but is not receiving periodic payments from it because his pension is adequate for his routine expenses. However, he has withdrawn $2,000 for a trip with his children. The withdrawal is not a periodic payment and is not counted as income.

3. If the tenant is receiving long-term care insurance payments, any payments in excess of $180 per day must be counted toward the gross annual income. (**NOTE:** Payment of long-term care insurance premiums are an eligible medical expense – see paragraph 5-10 D.8.k.)

4. *Federal Government/Uniformed Services pension funds paid to a former spouse.*

*Federal Government/Uniformed Services pension funds paid directly to* an applicant's/tenant's former spouse pursuant to the terms of a court decree of divorce, annulment, or legal separation are not counted as annual income. The state court has, in the settlement of the parties' marital assets, determined the extent to which each party shares in the ownership of the pension. That portion of the pension that is ordered by the court (and authorized by the Office of Personnel Management (OPM), to be paid to the applicant's/tenant's former spouse is no longer an asset of the applicant/tenant and therefore is not counted as income. However, any pension funds authorized by OPM, pursuant to a court order, to be paid to the former spouse of a Federal government employee is counted as income for a tenant/applicant receiving such funds.

**Example**: Joan Carson is a retired Federal government employee receiving a retirement pension. She is also the recipient of Section 8 housing assistance and involved in a divorce proceeding. In settling the assets of the marriage between Mrs. Carson and her former husband, the court ordered that one half of her pension be paid directly to her former husband in the amount of $20,000. The court provided OPM with clear, specific and express instructions acceptable for OPM to process the payment to Mrs. Carson's former husband. OPM authorized the payment of pension benefits to Mrs. Carson's former husband in the amount of $20,000. The $20,000 represents an asset disposed of as a result of a court decree. At the interim reexamination of her income, Mrs. Carson indicated a change in her income due to the court ordered payment of pension benefits to her former husband. The PHA requested that Mrs. Carson provide a copy of her statement from OPM evidencing the payment of pension benefits to her (her statement reflected the line item payment to her former husband due to the court order). That portion of the pension paid to her former husband no longer belongs to Mrs. Carson and is not counted as income.

The OPM is responsible for handling court orders (any judgments or property settlements issued by or approved by any court of any state, the

District of Columbia, the Commonwealth of Puerto Rico, Guam, The Northern Mariana Islands, or the Virgin Islands in connection with the divorce, annulment of marriage, or legal separation of a Federal government employee or retiree) affecting current and retired Federal government employees. See 5 C.F.R. § 838.103. OPM must comply with court orders, decrees, or court-approved property settlement agreements in connection with divorces, annulments of marriage, or legal separations of employees that award a portion of the former Federal government employee's retirement benefits. Id. at § 838.101(a)(1). State courts ordering a judgment or property settlement in connection with divorce, annulment of marriage, or legal separation have the responsibility of issuing clear, specific, and express instructions to OPM with regards to providing benefits to former spouses. Id. at § 838.122. In response to instructions from state courts, OPM will authorize payments to the former spouses. Id. at § 838.121. Once the payments have been

authorized by OPM, the reduced pension amount paid to the retired Federal employee (the tenant/applicant) will be reflected in the tenant's/applicant's statement from OPM. Former spouses of Federal government employees receiving court ordered pension benefits are provided a Form-1099 reflecting pension benefits received from the retired Federal government employee. In verifying the income of tenants/applicants, owners should require that tenants/applicants provide any copies of statements from OPM verifying pension benefits (including any reductions pursuant to a court order, decree or court-approved property settlement agreement), and any evidence of survivor benefits, pensions or annuities received from retired Federal government employees including, but not limited to, a Form-1099. (See Paragraph 5-7.G.5 for more information on the treatment of income from Federal government pensions.)

5. *Other State, local government, social security or private pensions paid to a former spouse.

   Other state, local government, social security or private pension funds paid directly to an applicant's/tenant's former spouse pursuant to the terms of a court decree of divorce, annulment, or legal separation are also not counted as annual income and should be handled in the same manner as 4, above. The decree and copies of statements should be obtained in order to verify the net amount of the pension that should be applied in order to determine eligibility and calculate rent.*

## M. Income from Training Programs

1. Amounts received under HUD-funded training programs are excluded from annual income.

2. Incremental earnings and benefits received by any family member due to participation in qualifying state or local employment training programs are excluded. Income from training programs not affiliated with a local government, and income from the training of a family member resident to serve on the management staff, is also excluded.

   a. Excluded income must be received under employment training programs with clearly defined goals and objectives and for a specific, limited time period. The initial enrollment must not exceed one year, although income earned during extensions for additional specific time periods may also be eligible for exclusion

   b. Training income may be excluded only for the period during which the family member participates in the employment training program.

   c. Exclusions include stipends, wages, transportation or child care payments, or reimbursements.

d. Income received as compensation for employment is excluded only if the employment is a component of a job training program. Once training is completed, the employment income becomes income that is counted.

e. Amounts received during the training period from sources that are unrelated to the job training program, such as welfare benefits, social security payments, or other employment, are not excluded.

2. Owners may ask to use project funds or funds from the Residual Receipts account to underwrite all or a portion of the cost of developing, maintaining, and managing a job training program for project residents if funds are available.

a. The Field Office will make the determination if the job training program may be approved, and if project funds are sufficient to fund the job training program and maintain the physical and financial integrity of the project. Job training programs may be either on-site at the project or off-site. For example, job training programs that have partnerships with local colleges, community based organizations, or local business, may have in-house job training programs designed for project residents.

b. Funds that an owner may choose to use to underwrite a job training program may include Section 8 funds, Community Development Block Grant funds, or housing authority funds. These funds may be used to cover the costs of various components of a job training program, including course materials, computer software, computer hardware, or personnel costs. Also, contractors and subcontractors, in connection with work performed under a Flexible Subsidy contract, may elect to hire project residents to perform certain skills required under the contract. If the employment of the project residents was pursuant to an apprenticeship program, this could constitute a training program using HUD funds, and income received by the tenants in the apprenticeship program will qualify as an exclusion from income.

## N. Resident Services Stipends

Resident services stipends are generally modest amounts of money received by residents for performing services such as hall monitoring, fire patrol, lawn maintenance, and resident management.

1. If the resident stipend exceeds $200 per month, owners must include the entire amount in annual income.

2. If the resident stipend is $200 or less per month, owners must exclude the resident services stipend from annual income.

O. **Income Received by a Resident of an Intermediate Care Facility for the Mentally Retarded or for the Developmentally Disabled (ICF/MR or ICF/DD) and Assisted Living Units in Elderly Projects**

1. An intermediate care facility is a group home for mentally retarded or developmentally disabled individuals (ICF/MR or ICF/DD). The term "intermediate care facility" is one used by state mental health departments for group homes serving these residents.

2. Assisted living units are units in projects developed for elderly residents with project-based assistance that have been converted to assisted living units.

3. The local agency responsible for Medicaid provides funds directly to group home operators and assisted living providers for services.

4. Annual income at an ICF/MR, ICF/DD, or assisted living unit must include:

   a. The SSI payment a tenant receives or the facility receives on behalf of the tenant; plus

   b. All other income the tenant receives from sources other than SSI that are not excluded from income by HUD regulations (see Exhibit 5-1). Examples of other sources of income include wages, pensions, income from sheltered workshops, income from a trust, or other interest income.

   c. The personal allowance of an individual residing in an ICF/MR or ICF/DD is not included in annual income. If the owner is unable to determine the actual amount of the personal allowance, use $30.

5. Annual income does not include the enhanced benefit portion of the SSI that is provided to pay for services. In some instances, a resident's SSI income may be reduced between annual recertifications if the resident's earnings exceed a specified amount. If this happens, the resident may request an interim recertification.

P. **Withdrawal of Cash or Assets from an Investment**

The withdrawal of cash or assets from an investment received as periodic payments should be counted as income. **Lump sum receipts from pension and retirement funds are counted as assets. If benefits are received through periodic payments, do not count any remaining amounts in the account as an asset. See Paragraph 5-7 G.2 for guidance on calculating income from an asset.**

Q. **Lump Sum Payments Counted as Income**

1. Generally, lump sum amounts received by a family, such as inheritances, insurance settlements, or proceeds from sale of property are considered assets, not income.

2. When social security or SSI benefit income is paid in a lump sum as a result of deferred periodic payments, that amount is *excluded* from annual income.

3. Settlement payments from claim disputes over welfare, unemployment, or similar benefits may be counted as assets, but lump sum payments caused by *delays in processing* periodic payments for unemployment or welfare assistance are included as income.

   How lump sum payments for delayed start of benefits are counted depends upon the following:

   a. When the family reports the change;

   b. When an interim re-examination is conducted; and

   c. Whether the family's income increases or decreases as a result.

   A lump sum payment resulting from delayed benefit income may be treated in either of the two ways illustrated in the example shown in Figure 5-3.

4. Lottery winnings paid in one payment are treated as assets. Lottery winnings *paid in periodic payments* must be counted as income.

## Figure 5-3: Treatment of Delayed Benefit Payments Received in a Lump Sum

Family member loses his/her job on October 19 and applies for unemployment benefits. The family receives a lump sum payment of $700 in December to cover the period from 10/20 to 12/5 and begins to receive $100 a week effective 12/6.

**Option A**: The owner processes one interim re-examination immediately effective 11/1 and a second interim after unemployment benefits are known.

| | 10/1 | 11/1 | 12/1 | 1/1 | 2/1 |
|---|---|---|---|---|---|
| Monthly gross income | 800 | *0 | *0 | 492** | 492** |
| Monthly allowances (three minors x 480 / 12 months) | 120 | - | - | 120 | 120 |
| Monthly adjusted income | 680 | 0 | 0 | 372 | 372 |
| Total tenant payment (TTP) | 204 | 25 | 25 | 25*** | 112*** |

* The family's income is calculated at $0/month beginning November 1, continuing until benefits actually begin and new income is calculated. TTP is set at the minimum rent.

** Family's actual income for 1/1 is $100/week x 52 weeks = $5,200 / 12 = $433.

However, because the family's TTP was calculated at zero income for the months of November and December (the period eventually covered by the $700 lump sum payment), the annual income to be used in calculating monthly gross income should be as follows:

$100/week benefit x 52 weeks = $5,200 + $700 lump sum payment = $5,900 annual gross income/ 12 = $492.

*** Increased rent does not start until 2/1 in order to give the family notice of rent increase.

**Option B:** The owner processes one interim re-examination after unemployment benefits are known.

| | 10/1 | 11/1 | 12/1 | 1/1 | 2/1 |
|---|---|---|---|---|---|
| Monthly gross income | 800 | 0/800* | 0/800* | 433* | 433* |
| Monthly allowances (three minors x 480 / 12 Months) | 120 | 120 | 120 | 120 | 120 |
| Monthly adjusted income | 680 | 0/680 | 0/680 | 313 | 313 |
| Total tenant payment | 204 | 204* | 204* | 94 | 94 |
| Recalculated TTP | - | 94*** | 94* | 94 | 94 |
| Rent credit (204 – 94=) | - | 110 | 110 | - | - |

* Family's actual income for 11/1 and 12/1 is zero, but because the owner does not process an interim re-examination, the family's TTP continues to be calculated using $800 as monthly gross income. Beginning 1/1, monthly gross income is known to be $100/week, or $433/month.

** The lump sum payment is taken into account by making the recertification retroactive to 11/1. Annual income is calculated as $5,200 / 12 = $433 monthly gross income.

*** TTP for November and December recalculated as $433 monthly gross income and $313 monthly adjusted income x .30 = 94 with credit or refund to family of $110/month for each of these two months for difference between TTP paid of $204 and recalculated TTP of $94.

## R. Exclusions from Income

1. Regulations for the multifamily subsidized housing programs covered by this handbook specifically exclude certain types of income from annual income. However, many of the items listed as exclusions from annual income under HUD requirements are items that the IRS includes as taxable income. Therefore, it is important for owners to focus specifically on the HUD program requirements regarding annual income.

2. Among the items that are excluded from annual income are the value of food provided through:

   a. The Meals on Wheels program, food stamps, or other programs that provide food for the needy;

   b. Groceries provided by persons not living in the household; and

   c. Amounts received under the School Lunch Act and the Child Nutrition Act of 1966, including reduced lunches and food under the Special Supplemental Food Program for Women, Infants and Children (WIC).

**Examples – Income Exclusions**

- The Value of Food Provided through the Meals on Wheels Program or Other Programs Providing Food for the Needy. Jack Love receives a hot lunch each day during the week in the community room and an evening meal in his apartment. One meal is provided through the Meals on Wheels program. A local church provides the other. The value of the meals he receives is not counted as income.
- Groceries provided by persons not living in the household. Carrie Sue Colby's mother purchases and delivers groceries each week for Carrie Sue and her two year old. The value of these groceries is not counted as income despite the fact that these are a regular contribution or gift.
- Amounts Received Under WIC or the School Lunch Act. Lydia Jeffries' two children receive a free breakfast and reduced priced lunches at school every day through the Special Supplemental Food Program for Women, Infants and Children (WIC). The value of this food is not counted as income.

**

3. Some additional examples of income that is excluded from the calculation of annual income follow.

**Examples – Income Exclusions**

- Resident service stipends. Rich Fuller receives $50 a month for distributing flyers for management. This amount is excluded from annual income.

- Deferred periodic payments of social security benefits. Germain Johnson received $32,000 in deferred social security benefits following a lengthy eligibility dispute. This delayed payment of social security benefits is treated as an asset, not as income.

- Income from training programs. Jennifer Jones is participating in a qualified state-supported employment training program every afternoon to learn improved computer skills. Each morning, she continues her regular job as a typist. The $250 a week she receives as a part-time typist is included in annual income. The $150 a week she receives for participation in the training program is excluded in annual income.

- Earned Income Tax Credit refund payments. Mary Frances Jackson is eligible for an earned income tax credit. She receives payments from her employer each quarter because of the tax credit. These payments are excluded in annual income.

**

## 5-7 Calculating Income from Assets

Annual income includes amounts derived from assets to which family members have access.

### A. What is Considered to Be an Asset?

1. Assets are items of value that may be turned into cash. A savings account is a cash asset. The bank pays interest on the asset. The interest is the *income* from that asset.

2. Some tenants have assets that are not earning interest. A quantity of money under a mattress is an asset: it is a thing of value that could be used to the benefit of the tenant, but under the mattress it is not producing income.

3. Some belongings of value are not considered assets. Necessary personal property is not counted as an asset. Exhibit 5-2 summarizes the items that are considered assets and those that are not.

### B. Determining Income from Assets

**Note:** For families receiving only BMIR assistance, it is not necessary to determine whether family assets exceed $5,000. The rule for imputing income from assets does not apply to the BMIR program.

1. The calculation to determine the amount of income from assets to include in annual income considers both of the following:

   a. The total cash value of the family's assets; and

   b. The amount of income those assets are earning or could earn.

2. The rule for calculating income from assets differs depending on whether the total cash value of family assets is $5,000 or less, or is more than $5,000.

C. **Determining the Total Cash Value of Family Assets**

1. To comply with the rule for determining the amount of income from assets, it is necessary to first determine whether the total "cash value" of family assets exceeds $5,000.

   a. The "cash value" of an asset is the market value less reasonable expenses that would be incurred in selling or converting the asset to cash, such as the following:

      (1) Penalties for premature withdrawal;

      (2) Broker and legal fees; and

      (3) Settlement costs for real estate transactions.

      The cash value is the amount the family could actually receive in cash, if the family converted an asset to cash.

**Example – Calculating the Cash Value of an Asset**

A family has a certificate of deposit (CD) in the amount of $5,000 paying interest at 4%. The penalty for early withdrawal is three months of interest.

$5,000 x 0.04 = $200 in annual income

$200/12 months = $16.67 interest per month

$16.67 x 3 months = $50.01

$5,000 - $50 = $4,950 cash value of CD

   b. It is essential to note that a family is not required to convert an asset to cash. Determining the cash value of the asset is done simply as a calculation by the owner because it is a required step when determining income from assets under program requirements.

## D. Assets Owned Jointly

1. If assets are owned by more than one person, prorate the assets according to the percentage of ownership. If no percentage is specified or provided by a state or local law, prorate the assets evenly among all owners.

2. If an asset is not effectively owned by an individual, do not count it as an asset. An asset is not effectively owned when the asset is held in an individual's name, but (a) the asset and any income it earns accrue to the benefit of someone else who is not a member of the family, and (b) that other person is responsible for income taxes incurred on income generated by the assets.

3. Determining which individuals have ownership of an asset requires collecting as much information as is available and making the best judgment possible based on that information.

**Example – Determining the Cash Value of an Asset**

The "cash value" of an asset is the amount a family would receive if the family turned a noncash asset into cash.

The cash value is the market value—or the amount another person would pay to acquire the asset—less the cost to turn the asset into cash.

If a family owns real estate, it may be necessary to consider the family's equity in the property as well as the expense to sell the property.

To determine the family's equity, subtract amounts owed on the property from its market value:

Market value
- Mortgage amount owed
Equity in the property

Calculate the cash value by subtracting the expense of selling the property:

Equity
- Expense of selling
Cash Value

Juanita Player owns a rental house. The market value is $100,000. She owes $60,000. The cost to dispose of this house would be $8,000. The owner would determine the cash value as follows:

| | |
|---|---|
| Market Value | $100,000 |
| Mortgage amount | - $60,000 |
| | 40,000 |
| Cost of disposing of the asset (real estate commission, and other costs of sale) | - $8,000 |
| **Cash Value** | **$32,000** |

a. In some instances, but not all, knowing whose social security number is connected with the asset may help in identifying ownership. Owners should be aware that there are many situations in which a social security number connected with an asset does not indicate ownership and other situations where there is ownership without connection to a social security number.

b. Determining who has contributed to an asset or who is paying taxes on the asset may assist in identifying ownership.

**Examples – Jointly Owned Assets**

- Helen Wright is an assisted-housing tenant. She and her daughter, Elsie Duncan, have a joint savings account. Mother and daughter both contribute to the account. They have used the account for trips together and to cover emergency needs for either of them. Assume in this example that state law does not specify ownership. Even though either Helen Wright or Elsie Duncan could withdraw the entire asset for her own use, count Helen's ownership as 50% of the account.
- Jean Boucher's name is on her mother's savings account to ensure that she can access the funds for her mother's care. The account is not effectively owned by Jean and should not be counted as her asset.

## E. Calculating Income from Assets When Assets Total $5,000 or Less

If the total cash value of all the family's assets is $5,000 or less, the actual income the family receives from assets is the amount that is included in annual income as income from assets.

## F. Calculating Income from Assets When Assets Exceed $5,000

1. When net family assets are more than $5,000, annual income includes the greater of the following:

   a. Actual income from assets; or

   b. A percentage of the value of family assets based upon the current passbook savings rate as established by HUD. This is called *imputed* income from assets. The passbook rate is currently set at 2%.

2. To begin this calculation, first add the cash value of all assets. Multiply the total cash value of all assets by .02. The product is the "imputed income" from assets. Then, add the actual income from all assets. The greater of the imputed income from assets or the actual income from assets is included in the calculation of annual income.

**Example – Use Actual Income from Assets When Total Net Family Assets are $5,000 or Less**

| Type of Asset | Cash Value | Actual Yearly Income |
|---|---|---|
| *Certificate of Deposit*<br>$1,000<br>withdrawal fee $50<br>interest @ 4% | $950 | $40 |
| *Savings Account*<br>$500<br>interest @ 2.5% | $500 | $13 |
| *Stock*<br>$300<br>Not paying dividends | $300 | $0 |
| Total | $1,750 | $53 |

The total cash value of the family's assets is $1,750. Therefore, the amount that is added to annual income as income from assets is the actual income earned or $53.

**Example – Imputed Income from Assets**

"Imputed" means "attributed" or "assigned." Imputing income from assets is "assigning" an amount of income solely for the sake of the annual income calculation. The imputed income is not real income.

For example, money under a mattress is not earning income. If the money were put in a savings account it would earn interest. Imputed income from such an asset is the interest the money would earn if it were put in a savings account.

A family with cash under a mattress is not required to put the cash in a savings account; but when the owner is calculating income for a family with more than $5,000 in assets, the owner must assign an amount that cash would earn if it were in a savings account.

**Example – Determining Income from Assets When Net Family Assets Exceed $5,000**

| Type of Asset | Cash Value | Actual Yearly Income |
|---|---|---|
| *Checking Account* (non-interest bearing) | $455 | $0 |
| *Savings Account* (interest at 2.5%) | $6,000 | $150 |
| *Stocks* (not paying dividends this year) | $3,000 | $0 |
| Total | $9,455 | $150 |

Total cash value of assets is greater than $5,000. Therefore, it is necessary to compare the actual income from assets to the imputed income from assets.

The total cash value of assets ($9,455) is multiplied by 2% to determine the imputed income from assets.

.02 x $9,455 = $189

$189 is greater than the actual income from assets ($150).

In this case, therefore, the owner will add $189 to the annual income calculation as income from assets.

## G. Calculating Income from Assets - Specific Types of Assets

1. Trusts.

   a. Explanation of trusts.

      (1) A trust is a legal arrangement generally regulated by state law in which one party (the creator or grantor) transfers property to a second party (the trustee) who holds the property for the benefit of one or more third parties (the beneficiaries). A trust can contain cash or other liquid assets or real or personal property that could be turned into cash. Generally, the assets are invested for the benefit of the beneficiaries.

      (2) Trusts may be revocable or nonrevocable. A revocable trust is a trust that the creator of the trust may amend or end (revoke). When there is a revocable trust, the creator has access to the funds in the trust account. When the creator sets up a nonrevocable trust, the creator has no access to the funds in the account.

      (3) The beneficiary frequently will be unable to touch any of the trust funds until a specified date or event (e.g., the

beneficiary's 21st birthday or the grantor's death). In some instances, the beneficiary may receive the regular investment income from the trust but not be able to withdraw any of the principal.

(4) The beneficiary and the grantor may be members of the same family. A parent or grandparent may have placed funds in trust to a child. If the trust is revocable, the funds may be accessible to the parent or grandparent but not to the child.

b. How to treat trusts.

(1) The basis for determining how to treat trusts relies on information about who has access to either the principal in the account or the income from the account.

(2) Revocable trusts. If any member of the tenant family has the right to withdraw the funds in the account, the trust is considered to be an asset and is treated as any other asset. The cash value of the trust (the amount the family member would receive if he or she withdrew all that could be withdrawn) is added to total net assets. The actual income received is added to actual income from assets.

**Example – A Trust Accessible to Family Members**

Assez Charaf lives alone. He has placed $20,000 in trust to his grandson to be available to the grandson upon the death of Assez. The trust is revocable, that is, Assez has control of the principal and interest in the account and can amend the trust or remove the funds at any time. In calculating Assez's income, the owner will add the $20,000 to Assez's net family assets and the actual income received on the trust to actual income from assets.

(3) Nonrevocable trusts. If no family member has access to either the principal or income of the trust at the current time, the trust is not included in the calculation of income from assets or in annual income.

If only the income (and none of the principal) from the trust is currently available to a family member, the income is counted in annual income, but the trust is not included in the calculation of income from assets.

(4) Nonrevocable trust as an asset disposed of for less than fair market value. If a tenant sets up a nonrevocable trust for the benefit of another person while residing in assisted

housing, the trust is considered an asset disposed of for less than fair market value (see subparagraph G.6 below).

– If the trust has been set up so income from the trust is regularly reinvested in the trust and is not paid back to the creator, the trust is calculated as any other asset disposed of for less than fair market value for two years and not taken into consideration thereafter.

**Example – Nonrevocable Trust As an Asset Disposed of for Less Than Fair Market Value**

Sarah Gordy placed $100,000 in a nonrevocable trust for her grandson. Last year, the trust produced $8,000, which was reinvested into the trust.

The trust is treated as an asset disposed of for less than fair market value for two years. (See paragraph 5.7 G.6.) No actual income from the trust is included in Sarah's annual income, but the value of the asset when it was given away, $100,000, is included in net family assets for two years from the date the trust was established.

– Nonrevocable trust distributing income. When a tenant places an asset in a nonrevocable trust but continues to receive income from the trust, the income is added to annual income *and* the trust is counted as an asset disposed of for less than market value for two years. Following the two-year period, the owner will count only the actual income distributed from the trust to the tenant.

**Example – Nonrevocable Trust Distributing Income to the Creator/Tenant**

Reggie Bouchard has established a nonrevocable trust in the amount of $35,000 that no one in the tenant family controls. Income from the trust is paid to Reggie. Last year, he received $3,500.

The owner will count Reggie's actual anticipated income from the trust in next year's annual income.

Because the asset was disposed of for less than fair market value (see paragraph 5.7 G.6), the value of the asset given away, $35,000, is counted as an asset disposed of for less than fair market value for two years.

(5) Payment of principal from a trust. The beneficiary of a trust may receive funds from the trust in different ways. A beneficiary may receive the full value of a trust at one time. In that instance the funds would be considered a lump sum receipt and would be treated as an asset. A trust set up to provide support for a person with disabilities may pay only income from the trust on a periodic basis. Occasionally, however, a beneficiary may be given a portion of the trust principal on a periodic basis. When the principal is paid out on a periodic basis, those payments are considered regular income or gifts and are counted in annual income.

**Example – Payment of Principal Amounts from a Trust**

Jared Leland receives funds from a nonrevocable trust established by his parents for his support. Last year he received $18,000 from the trust. The attorney managing the trust reported that $3,500 of the funds distributed was interest income and $14,500 was from principal. Jared receives a payment of $1,500 each month (an amount that includes both principal and interest from the trust).

The owner will count the entire $18,000 Jared received as annual income.

c. Special needs trusts.

A special needs trust is a trust that may be created under some state laws, often by family members for disabled persons who are not able to make financial decisions for themselves. Generally, the assets within the trust are not accessible to the beneficiary.

(1) If the beneficiary does not have access to income from the trust, then it is not counted as part of income.

(2) If income from the trust is paid to the beneficiary regularly, those payments are counted as income.

**Example – Special Needs Trust**

Daryl Rockland is a 55-year-old person with disabilities, living with his elderly parents. The parents have established a special-needs trust to provide income for their son after they are gone. The trust is not revocable; neither the parents nor the son currently have access to the principal or interest. In calculating the income of the Rocklands, the owner will disregard the trust.

2. Annuities.

a. Annuity facts and terms.

(1) An annuity is a contract sold by an insurance company designed to provide payments, usually to a retired person, at specified intervals. Fixed annuities guarantee a certain payment amount, while variable annuities do not, but have the potential for greater returns.

- A hybrid annuity (also called a combination annuity) combines the features of a fixed annuity and a variable annuity.

- A deferred annuity is an annuity that delays income payments until the holder chooses to receive them. An immediate annuity is one that begins payments immediately upon purchase.

- A life annuity continues to pay out as long as the owner is alive. A single-life annuity provides income benefits for only one person. A joint life annuity is issued on two individuals, and payments continue in whole or in part as long as either individual is alive.

(2) Generally, a person who holds an annuity from which he or she is not yet receiving payments will also be earning income. In most instances, a fixed annuity will be earning interest at a specified fixed rate similar to interest earned by a CD. A variable annuity will earn (or lose) based on market fluctuations, as in a mutual fund.

(3) Most annuities charge surrender or withdrawal fees. In addition, early withdrawal usually results in tax penalties.

(4) Depending on the type of annuity and the current status of the annuity, the owner will need to ask different questions of the verification source, which will normally be the applicant or tenant's insurance broker.

b. Income after the holder begins receiving payments.

(1) When verifying an annuity, owners should ask the verification source whether the holder of the annuity has the right to withdraw the balance of the annuity. For annuities without this right, the annuity is not treated as an asset.

(2) Generally, when the holder has begun receiving annuity payments, the holder can no longer convert it to a lump sum of cash. In this situation, the holder will receive regular payments from the annuity that will be treated as regular income, and no calculations of income from assets will be made. **

c. Calculations when an annuity is considered an asset.

(1) When an applicant or tenant has the option of withdrawing the balance in an annuity, the annuity will be treated like any other asset. **It will be necessary to determine the cash value of the annuity in addition to determining the actual income earned.

(2) In most instances, an annuity from which payments have not yet been made is earning income on the balance in the annuity. A fixed annuity will earn income at a fixed rate in the same manner that a CD earns income. A variable annuity will earn (or lose) based on current market conditions, as with a mutual fund.

(3) The owner will need to verify with the insurance agent or other appropriate source:

- The right of the holder to withdraw the balance (even if penalties are involved).
- The basis on which the annuity may be expected to grow during the coming year.
- The surrender or early withdrawal penalty fee.
- The tax rate and the tax penalty that would apply if the family withdrew the annuity.

(4) The cash value will be the full value of the annuity, less the surrender (or withdrawal) penalty, and less any taxes and tax penalties that would be due.

(5) The actual income is the balance in the annuity times the percentage (either fixed or variable) at which the annuity is expected to grow over the coming year. (This money will be reinvested into the annuity, but it is still considered actual income.)

(6) The imputed income from the asset is calculated only after the cash value of all family assets has been determined.

imputed income from assets is calculated on the total cash value of all family assets.

3. Lump sum receipts counted as assets.

a. Commonly, when a family receives a large amount of money, a lump sum payment, the family will put the money in a checking or savings account, or will purchase stocks or bonds or a CD. Owners must count lump sum payments received by a tenant as assets. Examples of lump sum payments include the following:

(1) Inheritances;

(2) Capital gains;

(3) Lottery winnings paid in one payment;

(4) Cash from the sale of assets;

(5) Insurance settlements (including health and accident insurance, workers compensation, and personal and property losses); and

(6) Any other amounts that are received in one-time lump sum payments.

**Example – Calculating the Cash Value of an Annuity**

Rodrigo Ramirez, site manager at Fernwood Forrest, has interviewed Barbara Barstow, an applicant who reports holding an annuity from which she will not receive payments for another 15 years when she turns 65. The applicant could not provide any more detail on the annuity but did report the name, address, and phone number of her insurance agent.

Rodrigo called the insurance agent and faxed a copy of the applicant's approval for release of information. As a result, Rodrigo learned that the annuity is a fixed annuity, with a current value of $20,400 earning interest at an annual rate of 4.5%. The applicant could withdraw the current balance in the account but would pay a surrender penalty of $3,000. If the annuity is withdrawn, then the applicant will owe $1,200 in tax penalties.

In this example, the important information for calculating cash value is the current value, $20,400; the surrender fee, $3,000; and the tax penalties, $1,200. If the applicant withdrew the cash from the annuity, after paying the surrender fee and tax penalty, then the amount of cash received would be $16,200.

The cash value, $16,200, is recorded as an asset.

Rodrigo will also calculate the actual anticipated income on this asset: $20,400 x .045 = $918.

b. A lump sum payment is counted as an asset only as long as the family continues to possess it. If the family uses the money for something that is not an asset—a car or a vacation or education—the lump sum must not be counted.

c. It is possible that a lump sum or an asset purchased with a lump sum payment may result in enough income to require the family to report the increased income before the next regularly scheduled annual recertification. But this requirement to report an increase in income before the next annual recertification would not apply if the income from the asset was not measurable by the tenant (e.g., gems, stamp collection).

**Examples – Lump Sum Additions to Family Assets (One-Time Payment)**

- JoAnne Wettig won $500 in the lottery and received it in one payment. Do not count the $500 as income. At JoAnne's next annual recertification, she will report all of her assets.

- Mia LaRue, a tenant in a Section 8 property, won $75,000 in one payment in the lottery. She buys a car with some of the money, and puts the remaining amount of $24,000 in the bank. Mia receives her first bank statement and notices that the income on this asset is $205 per month. She must report this increase in income because the family has experienced a cumulative increase in income of more than $200 per month. (See paragraph 7-10 A.4 on rules for reporting interim increases in income.) The owner must perform an interim recertification and count the greater of the actual or imputed income on this asset (since the net family assets are greater than $5,000).

4. Balances held in retirement accounts.

a. Balances held in retirement accounts are counted as assets if the money is accessible to the family member. For individuals still employed, accessible amounts are counted even if withdrawal would result in a penalty. However, amounts that would be accessible only if the person retired are not counted.

b. IRA, Keogh, and similar retirement savings accounts are counted as assets, even though withdrawal would result in a penalty.

c. Include contributions to company retirement/pension funds:

(1) While an individual is employed, count only amounts the family can withdraw without retiring or terminating employment.

(2) After retiring or terminating employment, count as an asset any amount the employee elects to receive as a lump sum.

d. Include in *annual income* any retirement benefits received through periodic payments.

**Examples – Balances Held in an IRA or 401K Retirement Account**

- Jed Dozier's 401K account balance is $35,000. He is able to terminate his participation in the retirement plan without quitting his job, but if he did so he would lose a part of his employer's contribution and would pay a penalty fee. The total cash he could withdraw, $18,000, is the amount that is counted as an asset.

5. *Federal Government/Uniformed Services Pensions

In instances where the applicant/tenant is a retired Federal Government/Uniformed Services employee receiving a pension that is* determined by a state court in a divorce, annulment of marriage, or legal separation proceeding to be a marital asset and the court provides OPM with the appropriate instructions to authorize OPM to provide payment of a portion of the retiree's pension to a former spouse, that portion to be paid directly to the former spouse is not counted as income for the applicant/tenant. However, where the tenant/applicant is the former spouse of a retired Federal Government/Uniformed Services employee, any amounts received pursuant to a court ordered settlement in connection with a divorce, annulment of marriage, or legal separation are reflected on a Form-1099 and is counted as income for the applicant/tenant. (See Paragraph 5-6.K.4 for more information on Federal Government/Uniformed Services pension funds paid to a former spouse.)

6. *Other state, local government, social security or private pensions.

Other state, local government, social security or private pensions where pensions are reduced due to a court ordered settlement in connection with a divorce, annulment of marriage, or legal separation and paid directly to the former spouse are not counted as income for the applicant/tenant and should be handled in the same manner as 5, above.*

7. Mortgage or deed of trust.

a. Occasionally, when an individual sells a piece of real estate, the seller may loan money to the purchaser through a mortgage or deed of trust. This may be referred to as a "contract sale."

b. A mortgage or deed of trust held by a family member is included as an asset. Payments on this type of asset are often received as one combined payment that includes interest and principal. The value of the asset is the unpaid principal as of the effective date of the certification. Each year this balance will decline as more principal is paid off. The interest portion of the payment is counted as actual income from an asset.

8. Assets disposed of for less than fair market value. Applicants and tenants must declare whether an asset has been disposed of for less than fair market value at each certification and recertification. Owners must count assets disposed of for less than fair market value during the two years preceding certification or recertification. The amount counted as an asset is the difference between the cash value and the amount actually received. (This provision does not apply to families receiving only BMIR assistance.)

a. Any asset that is disposed of for less than its full value is counted, including cash gifts as well as property. To determine the amount that has been given away, owners must compare the cash value of the asset to any amount received in compensation.

b. However, the rule applies only when the fair market value of all assets given away during the past two years exceeds the gross amount received by more than $1,000.

**Examples – Assets of More or Less Than $1,000 Disposed of for Less Than Fair Market Value**

- During the past two years, Alexis Turner donated $300 to the local food bank, $150 to a camp program, and $200 to her church. The total amount she disposed of for less than fair market value is $650. Since the total is less than $1,000, the donations are not treated as assets disposed of for less than fair market value.
- Jackson Jones gave each of his three children $500. Because the total exceeds $1,000, the gifts are treated as assets disposed of for less than fair market value.

c. When the two-year period expires, the income assigned to the disposed asset also expires. If the two-year period ends in the middle of a recertification year, the tenant may request an interim recertification to remove the disposed asset(s). * However, if the owner elects to only include the income for a partial remaining year as shown in the example below, an interim recertification should not be conducted.*

**Example -- Asset Disposed of for Less Than Fair Market Value**

Margot Lundberg's recertification will be effective January 1. On that date, it will be 18 months since she sold her house to her daughter for $60,000 less than its value. The owner will count income on the $60,000 for only six months. (After six months, the two-year limit on assets disposed of for less than fair market value will have expired.)

d. Assets disposed of for less than fair market value as a result of foreclosure, bankruptcy, divorce, or separation are *not* counted.

e. Assets placed in nonrevocable trusts are considered as assets disposed of for less than fair market value except when the assets placed in trust were received through settlements or judgements.

f. Applicants and tenants must sign a self-verification form at their initial certification and each annual recertification identifying all assets that have been disposed of for less than fair market value or certifying that no assets have been disposed of for less than fair market value.

g. Owners need to verify the tenant self certification only if the information does not appear to agree with other information reported by the tenant/applicant.

# Section 3: Verification

## 5-11 Key Regulations

This paragraph identifies key regulatory citations pertaining to Section 3: Verification. The citations and their titles (or topics) are listed below.

A. 24 CFR part 5, subpart B – Disclosure and Verification of Social Security Numbers and Employer Identification Numbers; Procedures for Obtaining Income Information

B. 24 CFR 5.659 Family Information and Verification

C. 24 CFR 8.24, 8.32, 100.204 (Reasonable accommodation)

## 5-12 Verification Requirements

### A. Key Requirements

1. Owners must verify all income, assets, expenses, deductions, family characteristics, and circumstances that affect family eligibility or level of assistance.

2. Applicants and adult family members must sign consent forms to authorize the owner to collect information to verify eligibility, income, assets, expenses, and deductions. Applicants and tenants who do not sign required consent forms will not receive assistance.

3. Family members 6 years of age and older must provide the owner with a complete and accurate social security number. For any members of the family who do not have a social security number, the applicant or family member must certify that the individual has never received a social security number. This requirement is described in paragraphs 3-9 and 3-**31** of this handbook.

4. The owner must handle any information obtained to verify eligibility or income in accordance with the Privacy Act.

**Figure 5-4: Privacy Act Notice**

The Department of Housing and Urban Development (HUD) is authorized to collect this information by the U.S. Housing Act of 1937 (42 U.S.C. 1437 et. seq.), by Title VI of the Civil Rights Act of 1964 (42 U.S.C. 2000d), and by the Fair Housing Act (42 U.S.C. 3601-19). The Housing and Community Development Act of 1987 (42 U.S.C. 3543) requires applicants and participants to submit the social security number of each household member who is 6 years old or older.

Purpose: Your income and other information are being collected by HUD to determine your eligibility, the appropriate bedroom size, and the amount your family will pay toward rent and utilities.

Other Uses: HUD uses your family income and other information to assist in managing and monitoring HUD-assisted housing programs, to protect the Government's financial interest, and to verify the accuracy of the information you provide. This information may be released to appropriate federal, state, and local agencies, when relevant, and to civil, criminal, or regulatory investigators and prosecutors. However, the information will not be otherwise disclosed or released outside of HUD, except as permitted or required by law.

Penalty: You must provide all of the information requested by the owner, including all social security numbers you, and all other household members age 6 years and older, have and use. Giving the social security numbers of all household members 6 years of age and older is mandatory, and not providing the social security numbers will affect your eligibility. Failure to provide any of the requested information may result in a delay or rejection of your eligibility approval.

## B. Timeframe for Conducting Verifications

Owners conduct verifications at the following three times.

1. Owners must verify income, assets, expenses, and deductions and all eligibility requirements prior to move-in.

2. Owners must verify each family's income, assets, expenses, and deductions as part of the annual recertification process. Refer to Chapter 7, Section 1 for information on annual recertifications.

3. Owners must verify changes in income, allowances, or family characteristics reported between annual recertifications. Refer to Chapter 7, Section 2 for information on interim recertifications.

## 5-13 Acceptable Verification Methods

### A. Methods of Verification

Owners must use verification methods that are acceptable to HUD. The owner is responsible for determining if the verification documentation is adequate and credible. HUD accepts three methods of verification. These are, in order of acceptability, third-party verification, review of documents, and family certification. If third-party verification is not available, owners must document the tenant file to explain why third-party verification was not available. **Appendix 3** provides a detailed list of acceptable forms of verification by type of information.

### B. Third-Party Verification

The following describes ways in which third-party verification may be obtained.

1. Written. Written documentation sent directly by a third-party source is the preferred method of verification. It is assumed that third-party sources will send written verification to the owner through the mail. (For information about electronic documentation, see subparagraph B3 below.)

   The applicant or tenant should not hand-carry the verification to or from the third-party source. If the verification does not contain an original signature or is delivered by the applicant or tenant, the owner should examine the document for evidence of tampering. In these situations, the owner may, but does not have to, accept the document as acceptable verification.

2. Oral. Oral verification, by telephone, from a reliable third-party source is an acceptable verification method. Owners frequently use this method when the third party does not respond to the written verification request. When verifying information over the telephone, it is important to be certain that the person on the telephone is the party he or she claims to be. Generally, it is best to telephone the verification source rather than to accept verification from a source calling the property management office. Oral verification must be documented in the file, as described in paragraph 5-19 C.

   **NOTE: Appendix 3** includes selected phone numbers of verification sources for employment and income records. However, they do not take the place of third party verification. The phone numbers contained in **Appendix 3** are not toll free but such calls are valid project expenses.

3. Electronic. The owner may obtain accurate third-party written verification by facsimile, e-mail, or Internet, if adequate effort is made to ensure that the sender is a valid third-party source.

a. Facsimile. Information sent by fax is most reliable if the owner and the verification source agree to use this method in advance during a telephone conversation. The fax should include the company name and fax number of the verification source.

b. E-mail. Similar to faxed information, information verified by e-mail is more reliable when preceded by a telephone conversation and/or when the e-mail address includes the name of an appropriate individual and firm.

c. Internet. Information verified on the Internet is considered third party verification if the owner is able to view web-based information from a reputable source on the computer screen. Use of a printout from the Internet may also be adequate verification in many instances. Refer to subparagraph C. Review of Documents below.

**Example – Verification by Internet Printout**

Jose Perez maintains a portfolio of stocks and bonds through an Internet-based stockbroker. The broker only provides electronic account statements and will not respond to a written verification request. The owner may accept a printout of Jose's most recent statement if it includes the relevant information required for a third-party verification and an Internet address and header or footer that identifies the company issuing the statement. If the owner has reason to question the authenticity of a document, the owner may require Jose to access the electronic file via the Internet in the owner's office, without providing the owner with username or password information.

## C. Review of Documents

1. An owner may review documents submitted by the applicant or tenant in one of the following situations:

   a. Third-party verification is not possible or is not required. For example, verifying that a family member is over 62 years old is more appropriately accomplished by examining a birth certificate than through third-party verification. **When third party verification is not possible, refer to paragraph 5-19 E for documenting the file.**

   b. Third-party verification is delayed. If information from a third party is not received within two weeks of its request, owners may consider original documents submitted by the tenant.**

**Examples – Appropriate Occasions to Verify Information through a Review of Documents**

- The owner sent a verification request to the tenant's employer but did not receive a response. The owner then made several calls to the employer but has not received a return call. The owner may use a review of documents (pay stubs) for verification. The owner should insist on a series of consecutive, recent pay stubs and should have a standard policy indicating the number of consecutive pay stubs required.
- The tenant's bank charges the bank account a fee for completing verification requests. The owner allows the resident to provide a current savings account statement or checking account statements for the past six months.
- The tenant's employer uses a 900 phone number, which results in a charge to the owner's phone to provide income verification. (In this case, the owner will accept the most recent consecutive eight pay stubs to verify earned income.)
- In cases where there is no third party available, a review of documents will always be appropriate. To verify a person's age, a birth certificate may be used. A social security card is the best verification of a social security number.

2. An owner must place copies of the reviewed documents in the applicant's or tenant's file. If copies cannot be made, the person reviewing the original documents must list the reviewed documents and the information provided on the documents, and must initial and date the notation.

3. Obtaining accurate verification through a review of documents requires the owner to consider the following:

   a. Is the document current? Documentation of public assistance may be inaccurate if it is not recent and does not show any changes in the family's benefits or work and training activities.

   b. Is the documentation complete? Owners may not accept pay stubs to document employment income unless the applicant or tenant provides the most recent **four to six** pay stubs to illustrate variations in hours worked. Actual paychecks or copies of paychecks should never be used to document income because deductions are not shown on the paycheck.

c. Is the document an unaltered original? The greatest shortcoming of documents as a verification source is their susceptibility to undetectable change through the use of high-quality copying equipment. Documents with original signatures are the most reliable. Photocopied documents generally cannot be assumed to be reliable.

### D. Family Certification

An owner may accept a tenant's notarized statement or signed affidavit regarding the veracity of information submitted if the information cannot be verified by another acceptable verification method.

## 5-14 Identifying Appropriate Verification Sources

An owner must only collect information that is necessary to determine the applicant's or tenant's eligibility for assistance or level of assistance. **Appendix 3** provides a list of acceptable forms of third-party verification.

## 5-15 Required Verification and Consent Forms

### A. Consent and Verification Forms

Adult members of assisted families must authorize owners to request independent verification of data required for program participation. To provide owners with this authorization, adult family members must sign two HUD-required consent forms plus the owner's specialized verification forms. Owners must create their own verification forms to request information from employers, child care providers, medical professionals, and others. Families sign these and the two HUD consent forms at the time of move-in certification and annual recertification. All adults in each assisted family must sign the required consent forms or the family must be denied assistance. Owners must give the family a copy of each form the family signed, a HUD Fact Sheet, and the Resident Rights and Responsibilities brochure.

### B. HUD-Required Consent and Release Forms

Applicants and tenants must sign two HUD-required consent forms.

1. Form HUD-9887, *Notice and Consent to the Release of Information to HUD and to a PHA*. Each adult member must sign the form regardless of whether he or she has income. *Each family member who is at least 18 years of age and the head, spouse or co-head, regardless of age, must sign this form at move-in, initial and at each annual recertification. The form must also be signed when a new adult member joins the household.* The form is valid for 15 months from the date of signature. The consent allows HUD or a public housing agency to verify information with the Internal Revenue Service, the Social Security Administration, and with state agencies that maintain wage and unem,ployment claim information. Owners must keep the original signed form in the tenant's

file and provide a copy to the family. Exhibit 5-5 contains a copy of form HUD-9887.

2. Form HUD 9887-A, *Applicant's/Tenant's Consent to the Release of Information – Verification by Owners of Information Supplied by Individuals Who Apply for Housing Assistance*. Owners and the head of household, spouse, co-head and each family member who is at least 18 years of age must sign **a HUD-9887-A** form **at move-in and at each annual recertification**. Each adult member must sign a form regardless of whether he or she has income. The consent allows owners to request and receive information from third-party sources about the applicant or tenant. Owners keep the original form in the tenant's file and provide a copy to the family. Exhibit 5-6 contains a copy of form HUD 9887-A.

## C. Information to Tenants

Owners must provide applicants and tenants with the HUD Fact Sheet and a copy of the Resident Rights and Responsibilities brochure.

1. HUD-9887 Fact Sheet. When applicants and tenants sign form HUD-9887 and form HUD 9887-A, owners must provide each family with a copy of the HUD Fact Sheet. This Fact Sheet describes the verification requirements for applicants and tenants and the tenant protections that are part of the verification process. Exhibit 5-7 contains a copy of the HUD Fact Sheet.

2. Resident Rights and Responsibilities Brochure. In addition, owners must provide applicants and tenants with a copy of the Resident Rights and Responsibilities brochure at move-in and annually at recertification. Copies of the brochure may be obtained by calling the HUD National Multifamily Clearinghouse at 800-685-8470.

## D. Owner-Created Verification Forms

1. Owners must create verification forms for specific verification needs and must include the language required by HUD as shown in Figure 5-5. **Appendix **6**** contains instructions, a sample verification consent, and guidance about the types of information to request when verifying income and eligibility.

2. It is important that the applicant or tenant know whom owners will ask to provide information and to whom the completed form will be returned. Therefore, verification forms must clearly state in a prominent location that the applicant or tenant may not sign the consent if the form does not clearly indicate who will provide the requested information and who will receive the information. When sending a request for verification to a third party, owners send the verification form with the applicant's or tenant's original signature to the third-party source. Owners must retain a copy of the verification form and provide a copy to the applicant or tenant upon request.

**Figure 5-5: Language Required in all Consent Forms**

The following statement must appear on all consent forms developed by owners:

"Title 18, Section 1001 of the U.S. Code states that a person is guilty of a felony for knowingly and willingly making false or fraudulent statements to any department of the United States Government. HUD and any owner (or any employee of HUD or the owner) may be subject to penalties for unauthorized disclosures or improper use of information collected based on the consent form. Use of the information collected based on this verification form is restricted to the purposes cited above. Any person who knowingly or willingly requests, obtains or discloses any information under false pretenses concerning an applicant or participant may be subject to a misdemeanor and fined not more than $5,000. Any applicant or participant affected by negligent disclosure of information may bring civil action for damages, and seek other relief, as may be appropriate, against the officer or employee of HUD or the owner responsible for the unauthorized disclosure or improper use. Penalty provisions for misusing the social security number are contained in the **Social Security Act at 208 (a) (6), (7) and (8). Violation of these provisions are cited as violations of 42 U.S.C. 408 (a) (6), (7) and (8).**

## 5-16 Social Security and Supplemental Security Income Data Match

A. Owners verify social security income and supplemental security income electronically through TRACS. If there is a discrepancy between income reported by the tenant or applicant and income provided by the Social Security Administration (SSA), TRACS will automatically generate a message that is sent to the owner. The owner must attempt to contact the applicant or tenant to disclose the discrepancy. **

B. Additional information is available on HUD's website page describing the tenant assessment system (for tenant income verification) (TASS):

www.hud.gov/offices/reac/products/prodtass.cfm

TASS is a computer-based tool to assist owners in verifying tenant incomes by comparing tenant-reported information to information in other HUD systems from the Social Security Administration and the Internal Revenue Service.

## 5-17 Effective Term of Verifications

Signed verification and consent forms must be used within a reasonable time after the applicant or tenant has signed if the tenant's signature is to represent a valid and current authorization by the family. Therefore, HUD has set specific limits on the duration of verification consents. In addition, verified information must be used in a timely manner since family circumstances are subject to change. HUD places several other limits on the information that may be requested and when and how it may be used.

A. **Duration of Verification Authorization**

Owner-created verification forms and the forms HUD 9887 and 9887-A expire 15 months after they are signed. Owners must ensure that the forms HUD 9887 and 9887-A have not expired when processing verifications. However, there are differences between the duration of form HUD-9887 and that of the individual verification forms.

1. The form HUD 9887-A and individual verification forms can be used during the 120 days before the certification period. During the certification period, however, these forms may be used only in cases where the owner receives information indicating that the information the tenant has provided may be incorrect. Other uses are prohibited.

2. Owners may verify anticipated income using individual verification forms to gather prospective information when necessary (e.g., verifying seasonal employment). Historical information that owners may request using individual verification forms is restricted as follows:

   a. Information requested by individual verification forms is restricted to data that is no more than 12 months old.

   b. However, if the owner receives inconsistent information and has reason to believe that the information the applicant or tenant has supplied is incorrect, the owner may obtain information from any time in the last five years when the individual was receiving assistance, as provided by the form HUD 9887-A.

3. The form HUD-9887 may be used at any time during the entire 15 month period. The information covered by the form HUD-9887 is restricted as follows:

   a. State Wage Information Collection Agency (SWICA). Information received from SWICA is limited to wages and unemployment compensation the applicant or tenant received during the last five years she/he received housing assistance.

   b. Internal Revenue Service and Social Security Administration. form HUD-9887 authorizes release by IRS and SSA of data from only the current income tax return and IRS W-2 form.

      If the IRS or SSA matches reveal that the tenant may have supplied inconsistent information, HUD may request that the tenant consent to the owner acquiring information on the last five years during the periods in which the tenant was receiving assistance.

B. **Effective Term of Verifications**

1. Verifications are valid for **120** days from the date of receipt by the owner.

**

2. If verifications are more than 120 days old, the owner must obtain new verifications.

3. Time limits do not apply to information that does not need to be reverified, such as:

   a. Age;

   b. Disability status;

   c. Family membership; or

   d. Citizenship status.

4. Time limits also do not apply to the verification of social security numbers; however, at each recertification any family member who has previously reported having never received a social security number, must be asked:

   a. To supply verification of a social security number if one has been received; or

   b. To certify, again, that he/she has never received a social security number.

## 5-18 Inconsistent Information Obtained Through Verifications

An owner may not take any action to reduce, suspend, deny, or terminate assistance based on inconsistent information received during the verification process until the owner has independently investigated the information. The owner should follow procedures for addressing errors and fraud and for terminating assistance in accordance with Chapter 8.

## 5-19 Documenting Verifications

### A. Key Requirement

Owners must include verification documentation in the tenant file.

### B. Documenting Third-Party Verification

Third-party verification received through the mail or by facsimile transmission must be put in the tenant file.

### C. Documenting Telephone Verification

When verifying information by phone, the owner must record and include in the tenant's file the following information:

1. Third-party's name, position, and contact information;

2. Information reported by the third party;

3. Name of the person who conducted the telephone interview; and

4. Date and time of the telephone call.

### D. Recording Inspection of Original Documents

Original documents should be photocopied, and the photocopy should be placed in the tenant file. If the original document cannot be copied, a clear note to the file must describe the type of document, the information contained in the document, the name of the person who reviewed the document, and the date of that review.

**NOTE:** It is not mandatory that social security cards be copied. See **Appendix 3** for alternate methods.

### E. Documenting Why Third-Party Verification Is Not Available

When third-party verification is not available, owners must document in the file efforts made to obtain the required verification and the reason the verification was not obtained. The owner must include the following documents in the applicant's or tenant's file:

1. A written note to the file explaining why third-party verification is not possible; or

2. A copy of the date-stamped original request that was sent to the third party;

3. Written notes or documentation indicating follow-up efforts to reach the third party to obtain verification; and

4. A written note to the file indicating that the request has been outstanding without a response from the third party.

### F. Reasonable Accommodation

If an applicant or tenant cannot read or sign a consent form because of a disability, the owner must provide a reasonable accommodation. See Chapter 2, Section 3, Subsection 4 for a description of the requirements regarding reasonable accommodations.

**Examples – Reasonable Accommodation**

- Provide forms in large print.
- Provide readers for persons with visual disabilities.
- Allow the use of a designated signatory.

# Exhibit 5-1: Income Inclusions and Exclusions

## 24 CFR 5.609(b) and (c)

Examples included in parentheses have been added to the regulatory language for clarification.

### INCOME INCLUSIONS

(1) The full amount, before any payroll deductions, of wages and salaries, overtime pay, commissions, fees, tips and bonuses, and other compensation for personal services;

(2) The net income from operation of a business or profession. Expenditures for business expansion or amortization of capital indebtedness shall not be used as deductions in determining net income. An allowance for depreciation of assets used in a business or profession may be deducted, based on straight line depreciation, as provided in Internal Revenue Service regulations. Any withdrawal of cash or assets from the operation of a business or profession will be included in income, except to the extent the withdrawal is reimbursement of cash or assets invested in the operation by the family;

(3) Interest, dividends, and other net income of any kind from real or personal property. Expenditures for amortization of capital indebtedness shall not be used as deductions in determining net income. An allowance for depreciation is permitted only as authorized in paragraph (2) above. Any withdrawal of cash or assets from an investment will be included in income, except to the extent the withdrawal is reimbursement of cash or assets invested by the family. Where the family has net family assets in excess of $5,000, annual income shall include the greater of the actual income derived from all net family assets or a percentage of the value of such assets based on the current passbook savings rate, as determined by HUD;

(4) The full amount of periodic amounts received from social security, annuities, insurance policies, retirement funds, pensions, disability or death benefits, and other similar types of periodic receipts, including a lump-sum amount or prospective monthly amounts for the delayed start of a **periodic amount (e.g., Black Lung Sick benefits, Veterans Disability, Dependent Indemnity Compensation, payments to the widow of a serviceman killed in action). See paragraph (13) under Income Exclusions for an exception to this paragraph;**

(5) Payments in lieu of earnings, such as unemployment, disability compensation, worker's compensation, and severance pay, except as provided in paragraph (3) under Income Exclusions;

(6) Welfare Assistance.

(a) Welfare assistance received by the family.

(b) If the welfare assistance payment includes an amount specifically designated for shelter and utilities that is subject to adjustment by the welfare assistance agency in accordance with the actual cost of shelter and utilities. the amount of welfare assistance income to be included as

income shall consist of:

(c) The amount of the allowance or grant exclusive of the amount specifically designated for shelter or utilities; plus

(d) The maximum amount that the welfare assistance agency could in fact allow the family for shelter and utilities. If the family's welfare assistance is ratably reduced from the standard of need by applying a percentage, the amount calculated under this paragraph shall be the amount resulting from one application of the percentage.

(7) Periodic and determinable allowances, such as alimony and child support payments, and regularr contributions or gifts received from organizations or from persons not residing in the dwelling; and

(8) All regular pay, special pay, and allowances of a member of the Armed Forces, except as provided in paragraph (7) under Income Exclusions.

(9) For Section 8 programs only and as provided in 24 CFR 5.612, any financial assistance, in excess of amounts received for tuition, that an individual receives under the Higher Education Act of 1965 (20 U.S.C. 1001 *et seq.)*, from private sources, or from an institution of higher education (as defined under the Higher Education Act of 1965 (20 U.S.C. 1002)), shall be considered income to that individual, except that financial assistance described in this paragraph is not considered annual income for persons over the age of 23 with dependent children. For purposes of this paragraph "financial assistance" does not include loan proceeds for the purpose of determining income. *(Note: This paragraph also does not apply to a student who is living with his/her parents who are applying for or receiving Section 8 assistance.)*

**INCOME EXLCUSIONS:**

(1) Income from employment of children (including foster children) under the age of 18 years;

(2) Payments received for the care of foster children or foster adults (usually persons with disabilities unrelated to the tenant family, who are unable to live alone);

(3) Lump-sum additions to family assets, such as inheritances, insurance payments (including payments under health and accident insurance and worker's compensation), capital gains, and settlement for personal or property losses, except as provided in paragraph (5) under Income Inclusions;

(4) Amounts received by the family that are specifically for, or in reimbursement of, the cost of medical expenses for any family member;

(5) Income of a live-in aide, as defined in 24 CFR 5.403;

(6) The full amount of student financial assistance paid directly to the student or to the educational institution (see Income Inclusions (9), above, for students receiving Section 8 assistance);

(7) The special pay to a family member serving in the Armed Forces who is exposed to hostile fire (e.g., in the past, special pay included Operation Desert Storm);

(8) (a) Amounts received under training programs funded by HUD (e.g., training received under Section 3);

(b) Amounts received by a person with a disability that are disregarded for a limited time for purposes of supplemental security income eligibility and benefits because they are set-aside for use under a Plan to Attain Self-Sufficiency (PASS);

(c) Amounts received by a participant in other publicly assisted programs that are specifically for or in reimbursement of out-of-pocket expenses incurred (special equipment, clothing, transportation, child care, etc.) and which are made solely to allow participation in a specific program;

(d) Amounts received under a resident service stipend. A resident service stipend is a modest amount (not to exceed $200 per month) received by a resident for performing a service for the owner, on a part-time basis, that enhances the quality of life in the project. Such services may include, but are not limited to, fire patrol, hall monitoring, lawn maintenance, and resident-initiative coordination. No resident may receive more than one such stipend during the same period of time; or

(e) Incremental earnings and benefits resulting to any family member from participation in qualifying state or local employment training programs (including training programs not affiliated with a local government) and training of a family member as a resident management staff person. Amounts excluded by this provision must be received under employment training programs with clearly defined goals and objectives, and are excluded only for the period during which the family member participates in the employment training program.

(9) Temporary, nonrecurring, or sporadic income (including gifts);

(10) Reparation payments paid by a foreign government pursuant to claims filed under the laws of that government by persons who were persecuted during the Nazi era. (Examples include payments by the German and Japanese governments for atrocities committed during the Nazi era);

(11) Earnings in excess of $480 for each full-time student 18 years or older (excluding the head of household and spouse);

(12) Adoption assistance payments in excess of $480 per adopted child;

(13) Deferred periodic amounts from supplemental security income and social security benefits that are received in a lump-sum amount or in prospective monthly amounts;

(14) Amounts received by the family in the form of refunds or rebates under state or local law for property taxes paid on the dwelling unit;

(15) Amounts paid by a state agency to a family with a member who has a developmental disability and is living at home to offset the cost of services and equipment needed to keep the developmentally disabled family member at home; or

(16) Amounts specifically excluded by any other federal statute from consideration as income for purposes of determining eligibility or benefits under a category of assistance programs that includes assistance under any program to which the exclusions set forth in 24 CFR 5.609(c) apply. A notice will be published in the *Federal Register* and distributed to housing owners identifying the benefits that qualify for this exclusion. Updates will be published and distributed when necessary.

The following is a list of income sources that qualify for that exclusion:

(a) The value of the allotment provided to an eligible household under the Food Stamp Act of 1977 (7 U.S.C. 2017 [b]);

(b) Payments to Volunteers under the Domestic Volunteer Services Act of 1973 (42 U.S.C. 5044(g), 5058) (employment through AmeriCorps, Volunteers in Service to America [VISTA], Retired Senior Volunteer Program, Foster Grandparents Program, youthful offender incarceration alternatives, senior companions);

(c) Payments received under the Alaska Native Claims Settlement Act (43 U.S.C. 1626[c])

(d) Income derived from certain submarginal land of the United States that is held in trust for certain Indian tribes (25 U.S.C. 459e);

(e) Payments or allowances made under the Department of Health and Human Services' Low-Income Home Energy Assistance Program (42 U.S.C. 8624[f]);

(f) Payments received under programs funded in whole or in part under the Job Training Partnership Act (29 U.S.C. 1552[b]; (effective July 1, 2000, references to Job Training Partnership Act shall be deemed to refer to the corresponding provision of the Workforce Investment Act of 1998 [29 U.S.C. 2931], e.g., employment and training programs for Native Americans and migrant and seasonal farm workers, Job Corps, veterans employment programs, state job training programs, career intern programs, Americorps);

(g) Income derived from the disposition of funds to the Grand River Band of Ottawa Indians (Pub. L-94-540, 90 Stat. 2503-04);

(h) The first $2,000 of per capita shares received from judgment funds awarded by the Indian Claims Commission or the U. S. Claims Court and the interests of individual Indians in trust or restricted lands, including the first $2,000 per year of income received by individual Indians from funds derived from interests held in such trust or restricted lands (25 U.S.C. 1407-1408);

(i) Amounts of scholarships funded under title IV of the Higher Education Act of 1965, including awards under federal work-study programs or under the Bureau of Indian Affairs student assistance programs (20 U.S.C. 1087uu);

(j) Payments received from programs funded under Title V of the Older Americans Act of 1985 (42 U.S.C. 3056[f]), e.g., Green Thumb, Senior Aides, Older American Community Service Employment Program;

(k) Payments received on or after January 1, 1989, from the Agent Orange Settlement Fund or any other fund established pursuant to the settlement in *In Re Agent*-product liability litigation, M.D.L. No. 381 (E.D.N.Y.);

(l) Payments received under the Maine Indian Claims Settlement Act of 1980 (25 U.S.C. 1721);

(m) The value of any child care provided or arranged (or any amount received as payment for such care or reimbursement for costs incurred for such care) under the Child Care and Development Block Grant Act of 1990 (42 U.S.C. 9858q);

(n) Earned income tax credit (EITC) refund payments received on or after January 1, 1991, including advanced earned income credit payments (26 U.S.C. 32[j]);

(o) Payments by the Indian Claims Commission to the Confederated Tribes and Bands of Yakima Indian Nation or the Apache Tribe of Mescalero Reservation (Pub. L. 95-433);

(p) Allowances, earnings, and payments to AmeriCorps participants under the National and Community Service Act of 1990 (42 U.S.C. 12637[d]);

(q) Any allowance paid under the provisions of 38 U.S.C. 1805 to a child suffering from spina bifida who is the child of a Vietnam veteran (38 U.S.C. 1805);

(r) Any amount of crime victim compensation (under the Victims of Crime Act) received through crime victim assistance (or payment or reimbursement of the cost of such assistance) as determined under the Victims of Crime Act because of the commission of a crime against the applicant under the Victims of Crime Act (42 U.S.C. 10602); and

(s) Allowances, earnings and payments to individuals participating in programs under the Workforce Investment Act of 1998 (29 U.S.C. 2931).

## Exhibit 5-2: Assets

**NOTE:** There is no asset limitation for participation in HUD assisted-housing programs. However, the definition of annual income includes net income from family assets.

A. Net Family Assets include the following:

1. Cash held in savings and checking accounts, safe deposit boxes, homes, etc. For savings accounts, use the current balance. For checking accounts, use the average balance for the last six months. Assets held in foreign countries are considered assets.

2. Revocable trusts. Include the cash value of any revocable trust available to the family. See discussion of trusts in paragraph 5-7 G.1.

3. Equity in rental property or other capital investments. Include the current fair market value less (a) any unpaid balance on any loans secured by the property and (b) reasonable costs that would be incurred in selling the asset (e.g., penalties, broker fees, etc.).

   **NOTE:** If the person's main business is real estate, then count any income as business income under paragraph 5-6 G of the chapter. Do not count it both as an asset and business income.

4. Stocks, bonds, Treasury bills, certificates of deposit, mutual funds, and money market accounts. Interest or dividends earned are counted as income from assets even when the earnings are reinvested. The value of stocks and other assets vary from one day to another. The value of the asset may go up or down the day before or after rent is calculated and multiple times during the year thereafter. The owner may assess the value of these assets at any time after the authorization for the release of information has been received. The tenant may request an interim recertification at any time thereafter that a decrease in stock value may result in a decrease in rent.

5. Individual retirement, 401K, and Keogh accounts. These are included when the holder has access to the funds, even though a penalty may be assessed. If the individual is making occasional withdrawals from the account, determine the amount of the asset by using the average balance for the previous six months. (Do not count withdrawals as income.)

**Example – Withdrawals from a Keogh Account**

Ly Pham has a Keogh account valued at $30,000. When she turns 70 years old, she begins drawing $2,000 a year. Continue to count the account as an asset. Use the guidance in paragraph 5-7 to determine the cash value and imputed income from the asset. Do not count the $2,000 she withdraws as income.

6. Retirement and pension funds.

a. While the person is employed. Include only amounts the family can withdraw without retiring or terminating employment. Count the whole amount less any penalties or transaction costs. Follow paragraph 5-7 G.4 of the chapter on determining the value of assets.

b. At retirement, termination of employment, or withdrawal. Periodic receipts from pension and retirement funds are counted as income. Lump-sum receipts from pension and retirement funds are counted as assets. Count the amount as an asset or as income, as provided below.

(1) If benefits will be received in a lump sum, include the lump-sum receipt in net family assets.

(2) If benefits will be received through periodic payments, include the benefits in annual income. Do not count any remaining amounts in the account as an asset.

(3) If the individual initially receives a lump-sum benefit followed by periodic payments, count the lump-sum benefit as an asset as provided in the example below and treat the periodic payment as income. In subsequent years, count only the periodic payment as income. Do not count the remaining amount as an asset.

**NOTE:** This paragraph and the example below assume that the lump-sum receipt is a one-time receipt and that it does not represent delayed periodic payments. However, in situations in which a lump-sum payment does represent delayed periodic payments, then the amount would be considered as income and not an asset.

**Example – Retirement Benefits as Lump-Sum and Periodic Payments**

Upon retirement, Eleanor Reilly received a lump-sum payment of $15,000. She will also receive periodic pension payments of $350 a month.

The lump-sum amount of $15,000 is generally treated as an asset. In this instance, however, Eleanor spent $5,000 of the lump sum on a trip following her retirement. The remaining $10,000 she placed in her mutual fund with other savings. The entire mutual fund will be counted as an asset.

The owner has verified that Eleanor is now not able to withdraw the balance from her pension. Therefore, the owner will count the $350 monthly pension payment as annual income and will not list the pension account as an asset.

7. Cash value of life insurance policies available to the individual before death (e.g., the surrender value of a whole life policy or a universal life policy). It would not include a value for term insurance, which has no cash value to the individual before death.

8. Personal property held as an investment. Include gems, jewelry, coin collections, or antique cars held as an investment. Personal jewelry is NOT considered an asset.

9. Lump-sum receipts or one-time receipts. (See paragraph 5-6 **P** for additional information on what is counted as a lump-sum receipt and how to treat lump-sum receipts.) These include inheritances, capital gains, one-time lottery winnings, victim's restitution, settlements on insurance claims (including health and accident insurance, worker's compensation, and personal or property losses), and any other amounts that are not intended as periodic payments.

10. A mortgage or deed of trust held by an applicant.

    a. Payments on this type of asset are often received as one combined payment of principal and interest with the interest portion counted as income from the asset.

    b. This combined figure needs to be separated into the principal and interest portions of the payment. (This can be done by referring to an amortization schedule that relates to the specific term and interest rate of the mortgage.)

    c. To count the actual income for this asset, use the interest portion due, based on the amortization schedule, for the 12-month period following the certification.

    d. To count the imputed income for this asset, determine the asset value **as of the effective date of the certification**. Since this amount will continually be reduced by the principal portion paid during the previous year, the owner will have to determine this amount at each annual recertification. See the following example:

**Example – Deed of Trust and Imputed Income**

Computation of imputed income:
An elderly tenant sells her home and holds the mortgage for the buyer. The cash value of the mortgage is $60,000. The combined payment of principal and interest expected to be received for the upcoming year is $5,000. The amortization schedule breaks that payment into $2,000 in principal and $3,000 in interest. In completing the asset income calculation, the cash value of the asset is $60,000, and the projected annual income from that asset is $3,000. **The imputed income would be calculated by multiplying the cash value of $60,000 by the 2% imputed passbook rate.** Each subsequent year, the cash value of the asset should be reduced by the principal portion paid. In this example, it would be reduced to $58,000 in the following year ($60,000 – $2,000 principal payment = $58,000). **When calculating the imputed income for the following year, the owner would multiply the cash value of $58,000 by the 2% passbook savings rate.**

**Regulatory References**

(These references are current as of the date of publication. Readers should refer to the latest edition of the Code of Federal Regulations.)

24 CFR part 5.603 defines net family assets as follows:

Net cash value after deducting reasonable costs that would be incurred in disposing of real property, savings, stocks, bonds, and other forms of capital investment, excluding interests in Indian trust land and the equity accounts in HUD homeownership programs. The value of necessary items of personal property such as furniture and automobiles shall be excluded. . . . . In determining net family assets, owners shall include the value of any business or family assets disposed of by an applicant or tenant for less than fair market value (including a disposition in trust, but not in a foreclosure or bankruptcy sale) during the two years preceding the date of application for the program or recertification, as applicable, in excess of the consideration received therefor. In the case of a disposition as part of a separation or divorce settlement, the disposition will not be considered to be for less than fair market value if the applicant or tenant receives important consideration not measurable in dollar terms.

B. Net family assets **DO NOT** include the following:

**IMPORTANT:** The owner does not compute income from any assets in this paragraph.

1. Personal property (clothing, furniture, cars, wedding ring, other jewelry that is not held as an investment, vehicles specially equipped for persons with disabilities).

2. Interests in Indian trust land.

3. Term life insurance policies (i.e., where there is no cash value).

4. Equity in the cooperative unit in which the family lives.

5. Assets that are part of an active business. "Business" does NOT include rental of properties that are held as investments unless such properties are the applicant's or tenant's main occupation.

**Example -- Assets that are Part of an Active Business**

- Laura and Lester Hines own a copier and courier service. None of the equipment that they use in their business is counted as an asset (e.g., the copiers, the FAX machines, the bicycles).
- Alice Washington rents out the home that she and her husband lived in for 42 years. This home is not an active business asset. Therefore, it is considered an asset and the owner must determine the annual income that Alice receives from it.

6. Assets that are NOT effectively owned by the applicant. Assets are not effectively owned when they are held in an individual's name, but (a) the assets and any income they earn accrue to the benefit of someone else who is not a member of the family, and (b) that other person is responsible for income taxes incurred on income generated by the assets.

   **NOTE:** Nonrevocable trusts (i.e., irrevocable trusts) are not covered by this paragraph. See information on nonrevocable trusts in paragraph 5-7 G.1.

**Example – Assets not Effectively Owned by the Applicant**

Net family assets do not include assets held pursuant to a power of attorney because one party is not competent to manage the assets, or assets held in a joint account solely to facilitate access to assets in the event of an emergency.

**Example:** Alexander Cumbow and his daughter, Emily Bornscheuer, have a bank account with both names on the account. Emily's name is on that account for the convenience of her father in case an emergency arises that would result in Emily handling payments for her father. Emily has not contributed to this asset, does not receive interest income from it, nor does she pay taxes on the interest earned. Therefore, Emily does not own this account. If Emily applies for assisted housing, the owner should not count this account as her asset. This asset belongs to Alexander and would be counted entirely as the father's asset should he apply for assisted housing.

7. Assets that are not accessible to the applicant and provide no income to the applicant. Nonrevocable trusts are not covered under this paragraph. See information on nonrevocable trusts in paragraph 5-7 G.1.

**Example**

A battered spouse owns a house with her husband. Because of the domestic situation, she receives no income from the asset and cannot convert the asset to cash.