

# Low-Income Housing Tax Credit Compliance Manual

Revised 4/2010



## *Preface*

This manual is a training and reference guide developed to assist owner/agents in administering the Low-Income Housing Tax Credit (LIHTC) Program in the State of Idaho. The manual is designed to furnish guidance pursuant to Section 42 of the Internal Revenue Service (IRS) code, the Revised October 2009 8823 guide, HUD Handbook 4350.3 REV1, Chg. 3 regulations and all subsequent IRS rulings, notices and announcements. Owner/agents must also be familiar with additional Idaho Housing & Finance Association (IHFA) requirements which are set forth in the Regulatory Agreement as well as in the Qualified Allocation Plan (QAP).

It is important to note that this manual is to be used as a supplement to existing laws and rules. It is not intended to be an all-inclusive and comprehensive guide to the LIHTC program. Therefore, LIHTC compliance is solely the owner's responsibility. Please note, however, that as the designated Compliance Monitoring Agency for the LIHTC Program in Idaho, IHFA has been provided with the regulatory authority to implement requirements that are in addition to those published by the IRS. The Association has incorporated several provisions into this version of the manual that are in addition to current IRS guidance. However, those requirements were implemented only in those areas where existing program-related information resulted in ambiguities, or areas that appeared to be in need of clarification. Every effort has been made to keep those additional requirements at a minimum. They have been incorporated into this Compliance Manual in order to help ensure that scarce low-income housing opportunities are afforded to those households truly in need.

Owners are responsible for compliance with all applicable federal and state rules and regulations that govern their particular developments. The determination of compliance is the sole responsibility the owner. IHFA will not assume liability for tax consequences as a result of noncompliance and/or IRS audits. All errors made will be the responsibility of the owner.

Future IRS or HUD rulings more stringent than IHFA requirements must be adhered to based upon their effective date(s). IHFA will make every effort to provide technical assistance and appropriate interpretations where it is able to do so, but will not unilaterally defer or alter effective / implementation dates by so doing. Compliance with all applicable rules and regulations is solely the responsibility of the owner.

The manual is not meant to be all inclusive guidance and does not guarantee the financial viability of any development. As a result, IHFA recommends all tax credit recipients consult with their tax accountant, attorney or other advisors regarding specific requirements of the LIHTC Program.

The manual can be found in its entirety, including updates, on the IHFA website at [www.ihfa.org](http://www.ihfa.org). The manual not only contains guidelines for compliance but source documents and forms to assist Owner/Agents in understanding Tax Credit compliance.

***NOTE.** Please reference the Revised October 2009 IRS 8823 Reporting Guide for detailed information and guidance in addition to the information presented in this manual. Reference HUD Handbook 4350.3 REV-1 Chg. 3 for additional information pertaining to income qualifications and verifications that are applicable to applicants/tenants seeking housing opportunities under the LIHTC Program.*

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## ***Part 1: Introduction***

### **LIHTC History**

Congress enacted the Low Income Housing Tax Credit Program under the Tax Reform Act of 1986. The Treasury Department is responsible for the administration of the program nationwide. State agencies like IHFA are delegated the responsibility and authority to allocate tax credits for the purpose of providing low-income housing at the state level.

The LIHTC program is a dollar-for-dollar reduction in an owner's tax liability for those who construct or rehabilitate low-income rental housing units. The amount of credit allocated is directly linked to the number of qualified low-income units that meet federal rent and income targeting requirements.

The Omnibus Budget Reconciliation Act of 1990 amended the IRS Tax Credit Code to require state tax credit allocating agencies like IHFA to provide procedures for monitoring developments for non-compliance in accordance with Section 42(m) (1)(B) of the Code and for notifying the IRS of such noncompliance. Guidelines and rules outlined in this manual are reflective of that amendment and the associated monitoring requirements contained herein.

## **Compliance Period & Extended Use Period**

According to Section 42 of the Code, all buildings that received allocations of credit after December 31, 1989 must comply with additional eligibility requirements in effect beginning January 1, 1990. Such developments have committed to an extended use period as stated in their individual Regulatory Agreement. After developments are placed in-service, they must comply with eligibility requirements for at least an additional fifteen (15) years beyond the initial fifteen (15) year federal compliance period, for a total of at least thirty (30) years.

Many developers have committed to even longer extended use periods. Previous IHFA Qualified Allocation Plans (QAP) have granted preference points to those developers who were willing to expand the extended use period beyond the fifteen (15) year requirement. Thus, several Owners have forty year extended use agreements. Such commitments bind Owner/Agents to maintain specific occupancy and affordability requirements for the development. Owner/Agents, therefore, must be aware of their development's compliance commitment.

An additional factor impacting management of Tax Credit developments is the fact that these developments are often coupled with subsidy programs (both project-based and tenant-based) that involve other government housing regulations. There are times when conflicts between programs arise, Therefore, Owner/Agents must be aware of the expiration dates attached to each compliance period and extended use periods noted in all regulatory agreements governing their developments.

*Note. Care must be exercised to ensure that the most restrictive of these competing program requirements are met.*

## **Responsibilities**

For the purposes of clarification, the responsibilities of various parties involved in the LIHTC process are outlined below.

### **IHFA Compliance Department Responsibilities**

Once the tax credits are allocated and a development is placed in-service, the IRS code requires that IHFA monitor program compliance during the compliance and extended use periods.

IHFA's Monitoring Duties Include:

1. Providing an on-line LIHTC Compliance Manual and additional pertinent information.
2. Providing technical assistance regarding compliance as needed.
3. Providing required compliance training.
4. Reviewing Annual submissions, which include Certificates of Continuing Compliance, Annual Occupancy Reports and any additional documents required under the Regulatory Agreement.
5. Auditing each low-income housing development at least once every (3) years. IHFA performs inspections by sampling twenty percent (20%) of household units and the associated low-income tenant files. Audits are scheduled in a manner that provides Owner/Agents enough advance notice to ensure arrangements are made for representatives to attend the audit, and that proper notice is given to tenants.

*Note. If the development has HOME units and/or ICRC financing, audits may be conducted on a more frequent basis, depending on the number of units in the development.*

The areas reviewed by IHFA's Compliance Department may include, but are not limited to the following:

- Determining, on a building-by-building basis, whether the initial minimum set-aside has been met within prescribed timeframes and assuring the minimum set-aside is maintained.
- Tenant qualifications, income calculations and appropriate supporting documentation.
- Gross rent calculations including utility allowance processes.
- Rental and social service requirements set forth in the development's Regulatory Agreement. Therefore, owners should have knowledge of their developments additional regulatory requirements.
- Physical Inspections specifically include a review of twenty percent (20%) of tenant units, all common areas, development grounds, building systems, building exteriors and maintenance facilities. IHFA utilizes standards



contained in HUD's Uniform Physical Conditions Standards (UPCS) requirements and State and Local code requirements.

6. Notifying Owner/Agents within thirty (30) days after an inspection when developments are out of compliance with IRS Code or IHFA requirements. Owner/Agents are typically given thirty (30) days to correct the non compliance issues and to respond to IHFA with either the corrected actions or with a corrective action plan. However, extensions may be granted under certain circumstances. Extensions must be requested in writing and submitted to IHFA prior to the original reporting deadline. Extension terms are on a case-by-case basis and are determined by IHFA.
7. Performing follow-up reviews of any building or development if deemed necessary. A follow-up review may include a physical inspection and/or tenant file reviews. Such reviews are subject to additional monitoring fees. Please refer to the Monitoring Fees section in Part Three (3) of this manual for further guidance.)
8. Reporting Owner/Agent non compliance and/or corrected findings are reported to the IRS via an IRS form 8823. Per the 8823 Reporting Guide, a copy of all 8823s sent to the IRS must also be sent to the Owner(s) listed on the IRS Form 8609.

Under IRS regulations, IHFA findings of non compliance, whether corrected or not, may be considered binding.

*Note. IHFA is the only entity that can make final determinations of non compliance; and only the IRS can determine what effect noncompliance will have on the development's Owners and/or investors. The IRS stipulates that findings of noncompliance are a State Agency issue and must be resolved at the state level.*

### **Owners' Responsibilities**

Owners who have chosen to participate in the LIHTC Program have done so in order to take advantage of the tax benefits the program provides. In exchange for the tax benefits, owners must meet requirements, which will benefit low-income tenants. In accordance with Section 42 of the IRS Code, Owners receiving tax credit allocations are required, by acceptance of the allocation, to perform the following:

1. Owners must meet all requirements agreed to in the Placed- in-Service Application, Regulatory Agreement, and Extended Use Agreement. Such requirements include minimum set aside elections, appropriate income and rental rate requirements, and annual certification processes. Further, in the application rounds, if Owner/Agents receive preference points to provide social services or additional rental restrictions, Owner/Agents must ensure that they are complying with these commitments. Noncompliance with social service commitments will not result in an 8823 filing, however it will be

considered a finding on the IHFA audit report and may result in a default of the regulatory agreement.

2. Owners are required to keep tenant records for each qualified low-income building in the development.
3. Throughout all phases of a development, owners are required to submit the following items:
  - Occupancy Reports at Initial Lease-up: Owner/Agents are required to submit an IHFA Occupancy Report during the initial move-in process. As soon as a development is fully leased, Owner/Agents have sixty 60-days in which to provide the report listing all first-year tenants. **Exhibit 1**
  - Certificate of Continuing Compliance: The IRS Code requires owners to certify that they have complied with all terms and provisions of the Section 42 requirements.. Owners must submit a completed certificate including owner signatures on an annual basis.

*Note. The annual due date of the Certificate is the last day of February. Owners have thirty (30) days to submit the form. Failure to submit a Certificate of Continuing Compliance is sufficient cause to file an 8823 with the IRS. Exhibit 1*
  - Annual Occupancy Reports: In conjunction with the Certificate of Continuing Compliance, the annual IHFA Occupancy Report must be submitted. The report is a listing of all the tenants that have occupied a development in the past year. The report allows IHFA Compliance Department staff to ensure Owner/Agents are following the Next Available Unit Rules and other pertinent Section 42 Code requirements. The Annual Occupancy Reports are due annually no later than the last day of February. Exhibit 1
  - IRS Forms 8609 and 8609A: The IRS Form 8609 form must be filed for each building in a development for the first year, showing the development's owner, minimum set-aside designation and verifying the year and the amount of Tax Credits claimed. The 8609A is completed and filed by the owner annually during the fifteen (15)-year compliance period. Owners' are responsible for submitting both IRS forms to the IHFA Compliance Department while filing annual tax returns with the IRS.
4. Any change in the management agent subsequent to reservation and throughout the extended use period...must be approved in writing by the Association. Failure to secure such approval must result in forfeiture of the tax credit.
5. Owners must fulfill this requirement and alert the IHFA Compliance Department prior to all agent changes. Additionally, if an owner changes management agents,

the owner must submit documentation for pre-approval to the IHFA Compliance Department. Agents of developments with Tax Credit allocations granted under Section 4.8.3 of the 2009 QAP and future QAPs are required to be managed by an agent with previous Section 42 Tax Credit experience or who can demonstrate proficiency in the program in order to receive the IRS Form 8609 from IHFA. According to the QAP, “an on-site manager who has received or will receive training within ninety (90) days, adequate program-specific training from experts, recognized in the industry is required for all developments that have twenty (20) or more units. IHFA reserves the right to accept any alternative system of controls and procedures that will provide a reasonable assurance relative to management capacity.” Agents will have to present a certificate before the 8609s will be provided.

6. Owners are responsible to correct incidents of noncompliance when discovered by themselves or their agent. Additionally, owners are responsible for correcting incidents of noncompliance discovered by IHFA within required time frames.
7. In accordance with Section 42 of the Code, the owner’s record-keeping requirements for low-income buildings include, but are not limited to the following:
  - The total number of rental units in the building, including the number of bedroom sizes in each building.
  - The percentage of units in the building that are low-income units meeting the election of 20/50 or 40/60 minimum set-aside test.
  - The rent charged on each unit in the building including the basis for determining the utility allowance.
  - A record reflective of vacancies in low-income units within each building, and when the next available units were rented.
  - Low-income move-in certifications, annual certifications of each low-income tenant as well as documentation to support those certifications. This documentation **must** be available during reviews.
  - The eligible basis and qualified basis of the building at the end of the first year of the credit period.
  - A record of the character and use of nonresidential portions of a building included in the building’s eligible basis under Section 42 (d). For example, 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 development.
  - The IRS requires Owner/Agents to retain tenant records for at least six (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 the entire compliance period plus six (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. Therefore, the IRS mandates that first year records be maintained for twenty-one (21) years.

8. It is solely the owner's responsibility to monitor a development's compliance status, overall well-being and for meeting all LIHTC and IHFA requirements, even when the owner contracts out rental management functions to a third party. Regardless of whether the owner hires a professional Property Management Agent, the owner is held accountable for compliance. Additionally, owners must hold their asset and professional agents accountable for compliance, must monitor their performance, and take corrective actions if problems arise.

***NOTE.** In selecting an agent, an owner should ensure that the agent and all on-site personnel are knowledgeable of the provisions and requirements of the Tax Credit Program and have adequate experience in managing a tax credit development.*

9. Agents/staff that are authorized to lease units to tenants should be thoroughly familiar with all federal laws, rules and regulations governing certifications and leasing procedures. Agents must also provide information, as needed, to IHFA and submit all required reports and documentation in a timely manner.
10. Agents may sign documents on behalf of the Owner only with appropriate signature authority.
11. Agents must ensure that the development is in compliance with all LIHTC and IHFA Program requirements. In cases of tenant fraud and casualty loss, agents must notify IHFA immediately and outline the steps to be taken to correct the non-compliance. Please refer to Section "Tenant Misrepresentation or Fraud" and "Casualty Loss" in Part 2 and 1 respectively within this manual for more guidance.
12. Owners must ensure their agents secure tenant occupancy information and it is contained in a confidential manner. However per IHFA Regulatory Agreements, all documentation must be accessible to authorized representatives of IHFA and/or the IRS.
13. Owners must provide adequate confidential space on-site for IHFA staff to properly perform compliance reviews.

## **Compliance Issues**

The key to the entire Tax Credit Program, as well as an owner's ability to claim the full amount of tax credits allocated to the development, is continuous compliance with federal and state LIHTC rules and regulations throughout the compliance and extended use periods.

The following discussion elaborates on several Code provisions directly affecting project compliance.

*Note. The following is not presented as a complete, all-inclusive listing of compliance regulations. Owners are responsible for overall compliance, and must be thoroughly familiar with all pertinent aspects of the LIHTC Program.*

## **Rent Restrictions**

The two fundamental components of compliance are as follows:

- Tax Credit units must be rented to tenants that are income eligible at move-in.
- Rent must be restricted according to the maximum limits imposed by using the appropriate formula and income limits.

Units set aside as low-income must be rent restricted as required by Section 42 (g)(2) of the Code. A unit is rent restricted if the "gross rent" does not exceed thirty percent (30%) of the applicable income limitation.

Each year, HUD publishes the Section 8 Area Median Gross income Limits for all states. IHFA annually publishes Income and Rent Limit Tables on the IHFA website, [www.ihfa.org](http://www.ihfa.org). The IRS requires these income limits, adjusted for family size, to be used when determining eligibility of LIHTC applicants/tenants at move-in and at recertification.

*Note. Please download the most current Income and Rent Limits for your county or area from the IHFA website, and implement the new limits no later than 60 days after the effective date. Also be aware that any fluctuations up or down in the income limits will have a corresponding impact on maximum gross rent amounts.*

## **Gross Rents**

The Code defines "gross rent" as the sum of unit rent, and utility allowances used to cover any utilities a tenant is required to pay other than telephone and any other charges routinely imposed on tenants that are not considered to be optional. (See the following Utility Allowance section for further guidance) If low-income tenants are charged more than the allowable rent, the unit is in non compliance and recapture of credits may result. The gross rent cannot exceed the applicable maximum rent as listed on the current applicable Income and Rent Limit Tables provided by IHFA. Certain exclusions and inclusions must be considered when determining gross rents.

Gross Rent does not include:

- Any payment under Section 8 of the United States Housing Act of 1937 or any comparable rental assistance program.
- Any fee for Supportive Service, paid to the owner of the unit (or the basis of the low-income status of the tenant of the unit) by any governmental program of assistance or by a tax-exempt organization if such program or organization provides assistance for rent and the amount of assistance provided for rent is not separable from the amount of assistance provided for supportive services.

“Supportive Service” is defined as any service provided under a planned program of services designed to enable tenants of a rental property to remain independent and avoid placement in a hospital, nursing home or intermediate care facility for the mentally or physically handicapped. In the case of single room occupancy or transitional housing for the homeless, such term includes any service provided to assist tenants in locating and retaining permanent housing.

Any rental payment to the owner of the unit to the extent such owner pays an equivalent amount to Rural Development (RD) under Section 515 of the Housing Act of 1949.

Gross Rent does include:

- A Utility Allowance for any tenant-paid utilities other than telephone, cable and internet.

### **Additional Fees**

Fees for facilities or services that are non-optional, and that are charged to tenants, are included within gross rent. Non-optional services such as a washer/dryer hook-up fee and built-in/on storage sheds must always be included within gross rent.

An “optional service” is defined as a service that is not a condition of occupancy and where there is a reasonable alternative available.

No separate fees should be charged for tenant facilities such as pools, parking and recreational facilities if the costs of the facilities are included in the eligible basis. For example: If an owner offers washers and dryers in the units for an additional fee, the cost of the washers and dryers must not be included in the eligible basis and an alternative such as laundry facilities in the building must be provided to the tenants. Please refer to your development’s Placed in-Service Applications for fee exclusion information.

***Note.** Refundable deposits are acceptable for the rental of development facilities such as a common area club house and pool.*

***Note.** Monthly fees charged in addition to gross rent for month-to-month leases are not allowed.*

## Utility Allowances

As stated in the previous section, the gross rent includes any utilities other than telephone cable and internet that a tenant is required to pay. If any utilities are paid directly by the tenant, the Code requires these utility costs to be included within the gross rent. The sum of both the utilities and the tenant rent must not exceed the applicable maximum rent. The type of utility allowance used depends upon the type of building the unit is located in or type of subsidy the unit has in the unit.

- HUD Assisted Buildings: If a development receives assistance from HUD, the utility allowance used must be the HUD approved utility allowance.
- Section 515-RD Assisted Buildings: If a development receives assistance under Section 515, the utility allowance used must be RD utility allowances.
- HUD and Section 515 Assisted Buildings: If a development receives assistance from both HUD and Section 515, the RD utility allowances must be used.
- Buildings without HUD or Section 515 Assistance: If a building is neither RD-assisted nor a HUD assisted building, and no tenant receives RD or HUD Section 8 assistance, building owners may use one of the following options to calculate utility allowances.
  1. **Public Housing Authority (PHA) Utility Allowance**: Owner/Agents may obtain utility allowances from their local PHA in their county, city or region.
  2. **Local Utility Allowance Estimate**: Owner/Agents may obtain utility allowance estimates for each unit in the building from the local utility company. The calculation is based on an energy, water, and sewage consumption analysis model. Specific factors must be taken into account including, but not limited to: unit size, building orientation, design and materials, mechanical systems, appliances, and characteristics of the building location.

The data must include the following:

Submission of applicable tenant paid utilities consumption data covering preceding twelve (12) month period.

The utility allowance data must contain only units which contain households who have resided in their units for a full twelve (12) month period. Therefore, do not include units that have experienced unit turnover in the last twelve (12) months.

### Calculating the Utility Allowance and Submission Requirements:

- Owner/Agents must average the utility costs for each unit type and divide by twelve (12) to ascertain a monthly utility allowance.
- Remove the units with the highest and lowest usage amounts for each bedroom size from your calculations. If the number of units with valid data is small, this step can be omitted.
- Once completed, the Owner/Agent utility allowance analysis and utility consumption print-outs from the utility company must be submitted to IHFA Compliance Department for approval.

*Note. Owner/Agents must remit a non-refundable utility consumption analysis fee of \$3 per unit or a minimum of \$100, whichever is greater, with all documentation regardless of approval.*

IHFA will review the submission and determine the acceptability of the analysis. An IHFA approved utility allowance is effective for one (1) year and must be renewed at the same time every year at the Owner/Agent's request.

3. **HUD Utility Schedule Model:** Owner/Agents may calculate a utility allowance using the "HUD Utility Schedule Model" that can be found on the IHFA website at <http://www.huduser.org/datasets/lihtc.html>. **Utility rates used for the HUD Utility Schedule Model** must be no older than the rates in place sixty (60) days prior to the beginning of ninety (90) days after the change (90 day period)

The utility allowance is considered "obtained" based on the date entered as the "form date" on the "location" spreadsheet of the HUD Utility Schedule Model. The date begins the ninety (90) day period after which the new utility allowance must be used to compute gross rents.

4. **Engineering Consumption Model:** Owner/Agents may calculate utility estimates by using an engineering consumption model. The engineering Consumption Model must take into consideration factors such as, unit size, building orientation, design, and materials, mechanical systems, appliances, and characteristics of the building location.

The date used to compute the estimate must be limited to the building's consumption data for a 12-month period ending no earlier than 60-days prior to the date the utility allowance will change. For new construction or renovated buildings with less than twelve (12) months of consumption data, use consumption data for the twelve (12) month period for similarly sized and constructed units in the geographical area in which the building is located.



The utility consumption estimates must be calculated by either a licensed engineer or a qualified professional approved by IHFA, The qualified professional and Owner/Agent must not have a conflict of interest.

*Note. Owner/Agents must remit a non-refundable engineering consumption data analysis fee of \$3 per unit or a minimum of \$100, whichever is greater, with all documentation regardless of approval.*

Utility allowances must be updated annually or whenever changes are made by the source. Regardless of the utility consumption method used, owner/agents must clearly identify, on all source documentation, which utility allowance is being utilized for the development. Written documentation should be obtained from the source each year of the compliance and extended use periods indicating whether or not there has been a change in the utility allowance or rates. This documentation must be kept on file for audit purposes and maintained in accordance with the Record Retention Requirements of the Code.

#### **Utility Review during Rent-Up**

According to the Revised 8823 Guide, a utility allowance review is not necessary until a building has achieved ninety percent (90%) occupancy for a period of ninety (90) consecutive days, or by the end of the first year of the credit period, whichever is earlier.

If the review is conducted at the end of the first year, the consumption rates for the first year of occupancy must be determined as of December 31<sup>st</sup>. The ninety (90) day period will begin no later than March 1 of the year before the first year of the credit period.

#### **Notification Requirement:**

If the owner obtains a utility allowance from a utility company using the HUD Utility Schedule Model or calculated using the Engineering Consumption Model, the owner must submit copies of the utility allowance estimates to (1) IHFA and (2) make the utility allowance estimate available to all tenants in the building at the beginning of the ninety (90) day period. IHFA may require additional information from the owner during the ninety (90) day period.

*Note. If an Owner/Agent decides to calculate allowances through the utility company one year, they CAN, decide the next year to obtain allowance information from their local PHA or pursue the other previously mentioned utility allowance consumption models. However, Owner/Agents must decide prior to the rent-up process which avenue to take to obtain the first year credit utility allowances.*

Under Treas. Reg. 1.42-10 (c) (2), a building owner *must* review the basis on which utility allowances have been established at least once during each calendar year and *must* update the allowance if required. Building owners may choose to calculate new utility allowances more frequently than once during a calendar year, provided the owner

complies with the requirement of Treas. Reg. 1.42-10, including the requirement to notify IHFA and your tenants.

If utility allowances change, Owner/Agents may need to adjust rents accordingly to remain in compliance with the Code's rent restriction requirement. A unit is in non compliance when tenant rent charged exceeds the maximum rent limits. **If an Owner/Agent does not follow the utility allowance process correctly, IRS Form 8823s will be filed.**

### **Overcharging Rent**

A unit is considered out of compliance when tenant rent exceeds maximum rent limits. Since tax credit development owners pay taxes on a calendar year basis, non compliance is determined on a tax year basis. Please see the following examples.

#### ***In Compliance:***

The maximum 2007 fifty percent (50%) rent limit for a two-bedroom unit in Boise is \$658 monthly. When the 2008 limits are released in March, Owner/Agents have sixty (60) days in which to establish the new rents. The 2-bedroom rents increase to \$777. If Owner/Agents correctly adjust the rents within appropriate timeframes, the development will be in compliance.

#### ***Out of Compliance:***

In January of 2008 the maximum rent for a 2-bedroom unit in Boise is \$800 a month. The Owner/Agent charges \$750 with a PHA utility allowance of \$50 per month paid by the tenant. In March of 2008, the 2-bedroom rent limit increased to \$850, and the utility allowance increased to \$51. The Owner/ Agent increased rent to an even \$800, however, with the utility allowance increase they failed to decrease rent by \$1. Therefore, the monthly rent exceeded gross rent by \$1.

Apartment Development "A" has a policy that charges applicants a one-time optional fee of \$125 to clean their future apartment before move-in. An applicant has the choice to either pay the non-refundable cleaning fee or move into the unit as is. The applicant pays the \$125 cleaning fee and moves into the unit on April 12, 2008.

According to the Revised 8823 Guide, it is not permissible for Owner/Agents to charge applicants a fee for maintaining low-income units in a condition suitable for occupancy under IRC 42(i)(3). Compliance with Section 42 is the responsibility of the Owner and that includes keeping all units in rent ready status. The unit is out of compliance as of April 12, 2008 and will not be back into compliance until January of 2009.

The units illustrated above are out of compliance and cease to be low-income units for the remainder of the owner's tax year. According to the Revised 8823 Guide, "the unit is back into compliance on the first day of the owner's next tax year if the rent charged on a monthly basis does not exceed the limit." Owner/Agents must also refund the overcharged rent and cleaning fee in the examples above, but this action does not avert an IRS Form 8823.

According to the Revised 8823 Guide, overcharging tenants for rent in the first year of the compliance period can disqualify the owner from claiming credits. For example, an owner of a one hundred percent (100%) tax credit building overcharges rent to all units, and as a result, fails to meet the minimum set-aside for the first year of the credit period. Therefore, the building does not qualify for credits.

*Note. It is very important for Owner/Agents to establish rents with the knowledge of applicable utility allowances and current rent limits. The IRS views overcharging tenants in the first year of compliance as an incurable offense. For more guidance please see Chapter 11 in the Revised 8823 Guide.*

### **Household Size**

A household is defined as all occupants who reside in a unit and may or may not be directly related. All household members are considered in determining the family size in a LIHTC unit. Owner/Agents must know this number in order to determine the income limit for the combined household.

There are several categories of people that are not counted as household members when determining household size. Please see the Revised 8823 Guide for additional information.

- Live-in Attendants
- Visitors or Guests
- Foster Children
- Foster Adults

When determining family size for income limits, the owner must include the following household members even though they are not living in the unit:

- Children temporarily absent due to placement in a foster home;
- Children in joint custody arrangements who are present in the household fifty percent (50%) or more of the time;
- Children who are away at school but who live with the family during school recesses;
- Children who are in the process of being adopted.
- Unborn children of pregnant women (as self-certified by the pregnant woman);
- Temporarily absent family members who are still considered family members approved to live in the unit. For example, a family member in the military deployed overseas who is not the head, spouse or co-head of the household;
- Family members in the hospital, or in a rehabilitation facility, for periods of limited or fixed duration. These household members are considered temporarily absent;
- Persons permanently confined to a hospital or a nursing home. The family decides if such persons are included when determining family size for income limits. If the

family chooses to include the permanently confined person as a member of the household, the owner must include income of the confined person when calculating family income.

*Note. Please refer to “Adding Additional Household Members” Section in Part 2 of this Manual for more guidance.*

## **Qualified Basis & Low Income Occupancy**

The amount of tax credits an Owner can claim depends on the number of rent-restricted, qualified LIHTC units in each building of the development. The percentage of tax credit units (applicable fraction) in the building multiplied by the allowable development costs (eligible basis) establishes the building’s Qualified Basis.

In a taxable credit year in a qualified, low-income building, the qualified basis is considered the amount equal to the applicable fraction. The applicable fraction is the smaller of the following:

- The number of low-income units as a percentage of all residential units; or
- The total floor space of low-income units as a percentage of the total floor space of all residential units.

Qualified Basis is determined on a building-by-building manner and not on a development level. For tax credit developments that are not one hundred percent (100%), the Qualified Basis can change annually if there is a change in the number of low-income units in any given building.

Owners have until the end of the initial or first year credit period to establish the development’s original low-income occupancy or applicable fraction for each building. The low-income occupancy achieved by the end of the initial credit period establishes the development’s original Qualified Basis. Once the basis has been initially established and credits claimed, the Qualified Basis is locked in, and must be maintained for the entire fifteen (15)-year compliance period. Only low-income units in the original qualified basis are eligible to receive the full tax credit value during the accelerated ten (10)-year credit period. The Qualified Basis of a building may be increased subsequent to the initial determination only by reason of an increase in the number of low-income units or in the floor space of the low-income units. Credits claimed on such additional Qualified Basis are determined using two-thirds (2/3rds) of the value of the credit which is now “de-accelerated” through year fifteen (15).

A decrease in a development’s applicable fraction reduces its Qualified Basis. If a development’s Qualified Basis for a given tax year decreases from the previous year, this results in non compliance and potential credit recapture of some or the entire accelerated portion of the development’s credits claimed in prior years.

*Note. Issues may occur in establishing or maintaining the Qualified Basis due to rent-up problems, admittance of non-qualified tenants into tax credit units, or misuse of common areas. Owners should be vigilant when renting units to qualified households during the initial first year leasing period as IHFA can and will monitor for potential noncompliance that could affect the livelihood of the tax credits.*

The Qualified Basis multiplied by the development's particular tax credit percentage (9% or 4%) determines the amount of credit an owner can claim each year for the accelerated ten (10)-year credit period. The allocation of credit dollars is based on a Federal Economic formula that is linked to the type of financing involved. The Federal Economic formula sets forth nine percent (9%) credits and four percent (4%) credits. A nine percent (9%) tax credit development is related to conventional financing. A four percent (4%) tax credit development is related to acquisition funding. Please see the Revised 8823 guide, Page 9 for additional guidance.

### **Eligible Basis**

Eligible Basis consists of the following:

- The cost of new construction; or
- The cost of rehabilitation; and/or
- The cost of acquisition of existing buildings acquired by purchase.

Eligible Basis includes the low-income units, facilities for use by the tenants (i.e. common areas, elevators, corridors and roofs) and facilities reasonably acquired by the development. The allowable costs of tenant facilities such as swimming pools, other recreational facilities and parking areas may be included, provided there is no separate fee for the use of these facilities and they are made available on a comparable basis to all tenants in the development. Costs of the low-income rental units in a building may be included in Eligible Basis only if such units are not above the average quality standard of the low-income units. Rehabilitation costs may not be included in Eligible Basis if such expenditures improve any unit beyond comparability with the low-income units.

*Note. Eligible Basis does not include commercial space. The cost of land is also not included in the adjusted basis as well.*

Any change in the Eligible Basis that results in a decrease in the Qualified Basis of the project is non compliance that must be reported by IHFA to the IRS via IRS Form 8823.

### **Minimum Set-Aside Requirements**

At the time of application, owners must choose one (1) of two (2) Minimum Set-Aside (MSA) requirements. The election, once stated in the Regulatory Agreement and elected on the IRS Form 8609, is irrevocable. If managing agents are unaware of which set-aside

requirement is designated for their development, they must contact the owner of their development.

The set-aside is the minimum number of units that must be rent restricted and reserved for low-income tenants in a building to qualify a building as low income. Pursuant to the Code, the set-aside options are:

- At least twenty percent (20%) of the available rental units in a development must be rent restricted and occupied by tenants whose income is fifty percent (50%) or less of Area Median Gross Income (AMGI) as adjusted for family size; or
- At least forty percent (40%) of the available rental units in a development must be rent restricted and occupied by tenants whose income is sixty percent (60%) or less of Area Median Gross Income (AMGI) as adjusted for family size.

These elections are the minimum requirements dictated by IRS Code. An owner must determine if the Minimum Set-Aside (MSA) will be met building-by-building or across the development. Such determination is specified by owners on IRS Form 8609. A building is eligible to receive tax credits during the ten (10)-year accelerated credit period only if it meets the elected MSA no later than the close of the first year of the credit period. The development must maintain this set-aside continually during the initial fifteen (15)-year compliance period or otherwise stated in the extended use agreement in order to remain in compliance.

*Note. Meeting the MSA may not qualify the owner for the full amount of annual credits allocated to a development. An owner must also meet IRS requirements and follow IRS regulations during initial lease up of the development to ensure full credits are awarded.*

For developments receiving credits in 1991 and thereafter, the MSA must be met by December 31 of the year the development is placed in service, if owners want to claim credits for that same year. If the credit start period is deferred until the second year, the MSA must be met by December 31 of the second year. Once the MSA is met, it must be maintained for the entire compliance period as noted above.

### **Other Set-Aside Requirements**

In addition to the MSA election requirement discussed above, developments have additional set-asides. Owners earn extra preference points in the allocation process by establishing additional set-asides. For example, an owner may decide to house tenants at deep skewed income and rent levels of thirty percent (30%) AMI. This set-aside not only gives owners points in the competitive allocation process, but also allows for tenants with a dire need of housing and limited resources.

Additional set-aside requirements are set forth in the IHFA Regulatory Agreement, and are a result of owner Regulatory Agreement commitments or additional loan requirements. Owners must carefully review their Regulatory Agreement for requirements, which may designate units or buildings specifically for the additional set-

aside. States may impose set-asides that require certain units to be rented to the elderly or to large families, or may impose lower income limits than the LIHTC code requires.

*Note. Owners must first establish the MSA, and then determine other set-aside requirements.*

IHFA has allocated credit based upon a specified number of low-income units, and in accordance with the Regulatory Agreement, and will expect compliance with the actual set-aside pledged by the owner after the first year of the credit period. IHFA suggests all Owners implement a tracking system for all set-asides to ensure compliance with all requirements. Follow the most restrictive set-aside so that the development will remain in compliance with all set-asides under commitment.

## **Unit Status**

The following is terminology defining unit status that should be considered when leasing units in a tax credit building.

- Vacant Unit: Tax credit unit, which a qualified tenant has vacated.
- Empty Unit: Tax credit unit that has NEVER been rented.
- Market Unit: Unit without tax credit, occupied or not.
- Occupied Unit: Tax credit unit that is currently rented.

## **Vacant Unit**

Under IRS Code, Owner/Agents cannot count a Vacant unit as a tax credit unit if the unit did not qualify as a tax credit unit prior to being vacated. Therefore, to be considered a tax credit unit, an eligible tenant must occupy or have occupied the unit. A Vacant unit cannot be counted as a tax credit unit simply because it is being held for a qualified tenant.

*Note. The Vacant unit does count towards the set-aside and the Qualified Basis.*

The IRS Code has established that if a low-income tenant moves out, the Owner/Agent may continue to count the unit as a qualified low-income unit as long as a reasonable attempt is made to rent the unit to an eligible household, and no available unit of comparable or smaller size is rented to an ineligible tenant. This provision of the IRS Code allows Owner/Agents to replace eligible tenants without losing Qualified Basis. The Vacant unit also continues to be counted as part of the Minimum Set-Aside.

“Reasonable Attempts” can be defined as Owner/Agents efforts toward marketing and renting a unit that is ready for occupancy. Under no circumstances can an owner claim credits on units if the rule is violated. For example, if an owner/agent has three (3) vacant units and violates this rule by renting to a non-eligible applicant, credit on all three (3)

vacant units will be lost and the units cannot be counted toward the development's Minimum Set-Aside.

### **Empty Unit**

Units that have never been occupied are referred to as Empty units rather than vacant units. Empty units cannot be counted as low-income units. However, they must be included in the building's total unit count for purposes of calculating the applicable fraction.

According to the definitions above, it may be a best-practice suggestion to rent empty units first before renting Vacant units. Empty units are not eligible for tax credits, until an initial, income-qualified tenant rents the unit. Therefore, the initial tenant gives the unit tax credit status.

### **Next Available Unit Rule**

The Next Available Unit Rule (NAUR) amends the regulations under Section 42 (g) (2)(D) of the Code. It applies to all leases entered into or renewed on and after September 26, 1997. Generally, the rule allowed for previously tax credit eligible tenants to move to a new unit within the same building. Thus, when a current tenant moves into a different unit within a building, a newly occupied unit adopts the status of the vacated unit.

Specifically, the Next Available Unit Rule dictates that if a tenant's income increases up to one hundred and forty percent (140%) of the applicable income limit, the unit continues to be treated as a low-income unit if the tenant's income initially met the applicable income limitation, and the unit continues to be rent restricted.

Increases beyond one hundred and forty percent (140%) of the applicable income limitations in a tenant's household income are deemed to result in an "over-income unit." The unit may continue to be counted as a low-income unit as long as the following two (2) conditions are met.

- The unit must continue to be rent restricted.
- The next comparable size unit in the building must be rented to a qualified low-income tenant.

The Owner of a low-income building must rent to qualified tenants all comparable units that are available or that subsequently become available in the same building until the applicable fraction (excluding the over-income units) is restored to the percentage on which the credit is based.

According to the Revised 8823 Guide, a development is considered in compliance when the Owner/Agent makes reasonable efforts to rent vacant low-income units (comparably sized or smaller than the vacated unit) to tenants having a qualifying income before units are rented to non-qualifying tenants. Reasonable effort is defined as advertising, contact with waiting list applicants, banner and signage stating vacancies on the development grounds, and other marketing practices.



If reasonable effort is made to rent to low-income tenants, but no one qualifies by way of the Resident Selection Policy, Owner/Agents may rent a vacant market unit of comparable size or smaller before a low-income unit. The rule only applies as long as none of the current low-income units are over income. The Owner/Agent must make every possible effort to attract low-income tenants to the development before a market unit can be rented.

IHFA may assess whether Owner/Agents made reasonable efforts to rent to low-income tenants by reviewing the Owner/Agent's advertising practices. Ensure that all advertising documentation since initial lease up and through the extended use period is made available during scheduled audits.

### **Comparable Unit Defined**

The Rule defines a "comparable unit" as a unit that is comparably sized or smaller than an over-income unit (or, for deep rent skewed projects, any low-income unit). The Rule further states that a comparable unit must be measured by the same method (unit fraction or floor space fraction) the taxpayer (Owner) used to determine Qualified Basis for the credit year in which the comparable unit became available.

### **Transfers vs. Unit Designation Swapping**

#### *Transfers within the Same Building*

Any low-income tenant may transfer within the same Building Identification Number (BIN). If a BIN contains both market and low-income units, a tenant who is currently living in a market unit cannot transfer to a low-income unit without qualifying for the low-income unit first.

#### *Transfers to a Different Building with Market Units*

When a tenant, whose income is no greater than 140% of the current income limit, moves to a low-income unit in a **different** building within the development, the vacated unit assumes the status of the newly occupied unit. Therefore, the tenant remains qualified.

If a tenant income **exceeds** 140% of the current income limit at the last certification and wishes to move to a different building, the newly occupied unit will be treated as a non-qualifying unit and Owners would be required to decrease the tax credit amount for that building until the non-qualified unit is rented to a qualified tenant and is brought back into compliance.

*Note. In a transfer, units need not be of a "comparable" nature as long as the household is not over 140% of the current income limit.*

The tenant's income status is determined from the most recent recertification. If a tenant's most recent recertification is more than twelve (12) months prior to the transfer, then a recertification must be completed as soon as possible. In addition, for those developments that are exempt from performing annual recertification requirements, owners must conduct an income recertification prior to the unit transfer to assess whether the tenant income exceeds the 140% income limit stipulation.

A new certification is not required when a tenant moves to another unit because the tenant's current income recertification, as well as the lease, moves with them. When a tenant moves within a building, the recertification documentation moves with the tenant to the new unit's file folder.

As indicated above, it is now permissible for those tenants whose incomes are less than 140% of the income limitations to transfer between buildings in a development. However, the IRS Code excludes tenants who earn more than 140% of the income limitations from transferring between buildings within the same development.

### ***Transfers Within 100% LIHTC Developments***

Tenants may transfer from building to building in developments that are 100% LIHTC.

### ***Unit Percentage Swapping***

Unit swapping may occur when a unit is over the income limit of a particular unit percentage. Swapping unit percentages can only occur with "comparable" units but may occur throughout the development.

For example: A tenant moves into Unit #101, a 30% 1 bedroom unit in Building A, on December 1, 2008. At recertification, the agent finds that the tenant is over the 30% income limit. Unit #303, a 50% 1 bedroom unit is vacant in Building B during this time. An owner may swap unit designations so that Unit #101 becomes the 50% unit and the unit in Building B assumes the 30% set aside. The tenant does not physically move out of Unit #101, however, the percentage designation changes.

***Note.** Unit Percentage Swapping may occur within a building and/or throughout a development. However, market units **cannot be swapped** throughout a development. A market unit may only be swapped with a unit of the same size or smaller in the BIN that the market unit has been designated.*

### **Non compliance with the Next Available Unit Rule**

If any comparable unit that is available or that subsequently becomes available is rented to a nonqualified tenant before the original fraction is restored, all over-income units for which the available unit was a comparable unit within the same building lose their status as low-income units and are deemed to be in non compliance. Therefore, violating this rule puts Owners at risk for losing credits on all 140% units. These units would no longer count toward the minimum set-aside. It is also critical in the initial credit period that Owner/Agents do not relocate existing tenants for purposes of qualifying more than one tax credit unit to count toward the minimum set-aside and applicable fraction. Under NO circumstance can one household be used to initially qualify more than one tax credit unit in the development.

### **Next Available Unit Rule in 100% Developments**

A one hundred percent (100%) affordable development may or may not be affected by the NAUR rule, as the next unit should always be rented to a low-income tenant. However, if an owner fails to rent a unit to an income- qualified tenant AND cannot

demonstrate due diligence when making that determination, the NAUR is violated and all units in the building will be considered in non compliance and tax credit recapture could ensue.

According to the IRS, “in cases of egregious non compliance, the Owner disregarded the Available Unit Rule and that the building’s basis is to be zero; i.e., the building is not part of a qualified low-income project at all times during the 15-year compliance period under IRC 42 (c)(2). No credit is allowable until such time as the owner can establish compliance with the Available Unit Rule.”

### **Staff Units**

Under IRS Code, owners may count a unit occupied by a full-time staff member as either a qualified low-income tax credit unit or part of a development’s “common area.”

- Counted as a Low-income Unit: If a staff unit is considered a rental unit and included in the building’s Qualified Basis (as a low-income unit in the building), then the staff member must be income-eligible, certified accordingly, and must sign a lease. The staff member must be treated the same as any low-income tenant. In this case, if a staff member receives free rent or a rental discount, the imputed value of the rent or discount must be included as income.
- Counted as Common Area: Revenue Ruling 92-61, Section 13, effective September 9, 1997 allows a unit for a staff member to be considered part of a development’s “common area.” Such units are not classified as residential units and thus are not included in the applicable fraction under section 42c(1)(B) for purposes of determining the building’s qualified basis. If the unit is not a residential rental unit and is used as common area by full-time staff, then the staff member does not have to be income-eligible, certified, leased or considered a tenant.

The Owner’s LIHTC application and the allocation documentation should stipulate the number of “common area” units set aside for staff members. Staff units must be a fixed unit size as dictated in the Placed-In-Service Application. The designated unit size therefore can’t float and must remain in the building it was originally designated.

The IRS revenue ruling on employee units does not apply to any building placed-in-service prior to September 9, 1992, or to any building receiving an allocation of credit prior to that date unless the Owner filed a tax return that is consistent with this ruling.

The Revised 8823 Guide clarifies the IRS Code, by stating that Owners who charge rent for a staff person’s “common area” unit may take away the exempt status of the unit. If Owners are charging rent for staff member units, the IRS has determined that the designated manager’s unit is not required to be occupied as a condition of employment. If living on-site were a mandatory condition of employment, a portion of a staff person’s salary would be taken out before taxes were remitted. In order for this case to occur, the Placed-In-Service Application and Regulatory Agreement must both state this employment contingency. If not, owners cannot charge for common area staff units.

- Rented as a Low-income Unit. Staff units may be rented as low-income units at the development's minimum set aside rent limit (20/50 or 40/60) to the general public if the unit is not being used by a staff person. Owner/Agents must first check their Regulatory Agreements for additional staff unit requirements.
- Compensation. IHFA does not provide guidance on staff compensation.

### **Commercial Space**

Any space included in eligible basis of a development cannot be used or considered for commercial space. The IRS, however, does allow for commercial use in a LIHTC development. The Code states, "Residential rental property may qualify for the credit even though a portion of the building in which the residential rental units are located is used for commercial use."

*Note. Owner/Agents cannot take LIHTC eligible common areas and convert them to commercial space after they have claimed tax credits. A recapture of credits may occur in this case. For example: If garages are considered part of the eligible basis and a tenant decided to use his garage as a mechanics shop, the garage space (eligible common area) has now become commercial space. This situation may result in tax credit recapture.*

### **Non-Transient Occupancy**

A unit shall be considered a tax credit low-income unit when it is suitable for occupancy and utilized for purposes other than on a "Transient Basis." The IRS Code defines "Suitable Occupancy" as: "occupancy determined under regulations prescribed by the IRS taking into account local health, safety and building codes." The Code defines occupancy on a Transient Basis as: "Any unit that is under a lease term less than six (6) months." Therefore, in order for units to be IRS Code compliant, all initial tenant leases must be for a term of six (6) months or greater. Thereafter, a lease term may revert to month-to-month.

*Note. As per IRC 42 (i)(3)(B)(iii) and (iv) regulations, two exceptions to this rule apply: One, Housing for the Homeless (Section 103 of the Stewart B McKinney Homeless Assistance Act) and two, Single Room Occupancy (SRO) developments.*

### **Available to the General Public**

The IRS also requires tax credit developments be available to the "General Public." Under Treasury Reg. 1.42-9 (b), "If a residential unit is provided 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." Further, any rental unit that is part of a hospital, nursing home, sanitarium, life-care facility, dormitory, trailer park, retirement home providing significant services other than housing, 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. However, owners providing housing for elderly, homeless, disabled or handicapped will not violate the general use requirement.

The General Public Use Rule, clarified July 30, 2008, and stipulated in the Revised 8823 Guide in Chapter 12, allows occupancy restrictions or preferences that favor the following tenants:

- Tenants with Special Needs;
- Tenants who are members of a specified group under a federal or state program or policy that supports housing for such a specified group;
- Tenants who are involved in artistic or literary activities

### **Marketing**

Owners must make reasonable attempts to make vacant low-income units available to the public for rent. As per the Revised 8823 Guide, Chapter 12, Owners should advertise the availability of their vacant units using advertising methods designed to be accessible to all prospective tenants. Please see the guide for more marketing guidance.

### **Federal Regulations for Developments Available to the General Public**

According to the Revised 8823 Guide, “LIHTC properties are subject to Title VIII of the Civil Rights Act of 1968, which makes it unlawful to discriminate in any aspect relating to the sale or rental of dwellings, in the availability of transactions related to residential real estate, or in the provision of services and facilities in connection therewith because of race, color, religion, sex, disability, familial status or national origin.”

Under the Title VIII of the Civil Rights Act of 1968, if auditors become aware of issues during compliance audits, IHFA has the obligation to report violations to HUD Regional offices or other fair housing enforcement agencies as appropriate.

IRS Form 8823 will be filed with the IRS when the civil action is completed. HUD or the Department of Justice (DOJ) will notify IHFA of the resolution of the alleged violation. Documentation that the Owner/Agent has complied with the court order and/or HUD’s requirements that the violation has been corrected must be submitted to IHFA.

HUD or the Department of Justice may also notify IHFA of a violation. On such occasions, IHFA must immediately file IRS Form 8823 noting the potential violation and notifying the owner in writing. IHFA is NOT responsible for determining whether the Owner is in non compliance. The IRS is responsible for determining whether the Owner is in non compliance based on court proceedings. Please see Chapter 13 in the Revised 8823 Guide for more assistance.

*Note. IHFA strongly recommends Owner/Agents attend Fair Housing training at least annually.*

### **Section 8 Requirements**

Under IRS rules, LIHTC Owner/Agents are prohibited from refusing to lease a unit to a Section 8 voucher holder solely because the person has been issued a voucher. Simply put, Section 8 voucher holders cannot be denied housing on the basis of their Section 8

status. However, Section 8 participants may not automatically meet Section 42 requirements. The following issues relative to recipients of Section 8 assistance should be considered.

- A Section 8 participant may have income that exceeds LIHTC income limits.
- Fair Market Rent (FMR) and voucher payment standards, may be less than LIHTC rent preventing voucher holders from tenancy. For example, if the FMR is \$500 and the development rent is \$525, the Section 8 participant may not be able to rent the unit.
- Poor credit rating, criminal background and/or poor rental history, and not meeting other Owner established Resident Selection Plan criteria.
- Tax Credit development may have 100% Section 8 subsidy.

Owner/Agents denying tenancy to participants of the Section 8 program must document the reason that occupancy was denied. Failure to document that Section 8 voucher holder applying for LIHTC units was rejected for acceptable reasons, can result in a finding of non compliance.

### **Students**

As determined under IRS Code Section 151(c)(4) a unit is NOT considered low-income when occupied by all full-time students. Therefore, households consisting of all full-time students are not eligible to reside in units receiving tax credits. The Code defines student as “an individual who during each of five (5) calendar months during the calendar year is a full-time student” at an “educational institution.” The five (5) calendar months need not be consecutive months.

This may present an interesting dilemma for future applicants. For instance, if a student graduates high school on June 1<sup>st</sup> and was a full-time student from January to May 31<sup>st</sup>, the applicant is not tax credit eligible until January of the following calendar year since they attended school five months of the calendar year. If the same student graduates high school in April, and will not be attending a university in the fall, the applicant would be eligible under the five (5) calendar month rule. The student issue only comes into play when ALL tenants in a unit are full-time students. Some additional considerations relative to students follow:

- Part-time Students are NOT “Students” under LIHTC program rules.
- Recent high school and college graduates cannot rent a tax credit unit until the beginning of the next calendar year. For example, an applicant has just graduated in May from high school. The applicant is not eligible to rent a tax credit unit until the following January when the taxable year begins again.
- Educational Institutions alone define full-time student status.
- Full-time student status may include enrollment in grades K-12, depending on the standards of the individual educational institution.

- Individuals pursuing a full-time course in institutional farm training, under the supervision of an accredited agency, are deemed to be full-time students.
- Part-time attendance at multiple institutions with a cumulative of fifteen (15) or more credits is a violation of the full-time student rule.
- Further, full-time students who are employed full-time are still considered full-time students regardless of their employment status.
- The student rule does not contain a grandfather clause. Therefore, a qualified tenant may become a non-qualified tenant after move-in if the tenant decides to become a full-time student. For example, if a household contains a working adult and a full-time student, the student rule does not apply. When the working adult starts school, however, the household would not be eligible since the program does not allow grandfathering. For this reason, student status must be re-verified at annual re-certification to confirm continuing eligibility of the household.

### **Exemptions Available Under the Student Rule**

At no time during the lease, or any extension thereof, may the unit be occupied entirely by full-time students unless the household meets one or more of the following student rule exemptions, contained in Section 42 (i)(3)(D). Units occupying full-time students who meet the following exemptions continue to meet low-income tax credit provisions and are in compliance with IRS Code:

- A student receiving assistance under Title IV of the Social Security Act, i.e. AFDC / TANF; or
- Enrolled in a job training program receiving assistance under the job Training Partnership Act or under other similar Federal, State or Local laws; or
- Married and able to file a joint tax return;

*Note. According to the Revised 8823 Guide, a married couple that is entitled to file a joint tax return but has not filed one still satisfies the exception to the full-time student rule. For example, a recently married full-time student couple is looking for housing. The couple is income qualified, but they have not yet filed their first tax return. Even if the couple does not file a joint tax return, they are still entitled or able to file a joint return, and thus qualify for the exemption.*

- A household consisting of a single parent and school age child(ren), all of whom are not dependents of another individual, except the child(ren)'s other parent (not living in the unit) are considered full-time students. A copy of the current year's tax return must be included in the tenant file to support student eligibility
- If a household is composed entirely of income qualified full-time students and one of those students was previously or is currently under the care of a state foster care program, the household remains qualified for the tax credit unit. Owner/Agents must

obtain written third-party verification from the state foster care administrative entity that the student was previously or is currently in a foster care program.

### **Suitability of Units and Casualty Loss**

In order for Owners to claim tax credits, a development and its units must be suitable for occupancy in accordance with state or local codes. If a unit is not habitable, no tax credits can be claimed. The IRS states in Chapter 6 of the Revised 8823 Guide that if a unit is destroyed (i.e., fire, flood or any other casualty loss disaster), credits cannot be claimed while the unit is being restored. If the unit is restored within a reasonable time, credits can again be claimed and no recapture ramifications.

According to the Revised 8823 guide, casualty loss is defined as, “the damage, destruction, or loss of property resulting from an identifiable event that is sudden, unexpected, or unusual.” Casualty loss ranges from car accidents, fires, government demolitions, hurricanes, mine cave-ins, sonic booms, storms, tornados, vandalism, etc. Property damage is not considered a casualty loss if the damage occurred during normal use, the owner willfully caused the damage or was willfully negligent, or a progressive deterioration, as in the case of damage caused by termites.

The physical damage due to the casualty loss must be reported to IHFA as noncompliance with UPCS Code or local standards as follows:

- As soon as the damage occurs, Owner/Agents must report the damage to IHFA in writing within 10 business days from the incident.
- IHFA is required to file an IRS Form 8823, taking the unit or building off line.
- Owner/Agents must notify IHFA in writing again when repairs are completed. IHFA will then file an IRS Form 8823 form putting the unit or building back into compliance.
- The IRS states that credits will be protected if a unit/building is restored within a reasonable period of time and each unit is occupied by qualified tenants by December 31<sup>st</sup> of the year the casualty occurred. If reasonable time takes an owner into January to get units back into service, credits will be disallowed for the affected units for the year of casualty loss.

*Note. There is no relief for those Owners who experience a casualty loss on December 15<sup>th</sup> and units come back online on January 10<sup>th</sup>. An Owner's credits are essentially lost for the year.*

Tax credit units that are vacant during the course of unit turn must be made rent ready as soon as possible. Otherwise, they may not be considered suitable for occupancy and may be subject to an IRS Form 8823 filing.

According to the Revised 8823 guide, if an Owner has a high vacancy rate with a large number of empty units not suitable for occupancy, they are considered in non-



compliance. “Not Suitable for Occupancy” can be defined as not rent ready within thirty (30) days.

For example, a tenant moved out of a Unit #201 on March 1, 2009. IHFA Compliance Auditors discover during their annual inspection on August 1, 2009 that Unit #201 is not rent ready or suitable for occupancy, i.e. the unit is still under rehabilitation ( missing carpet, appliances are not in place, painting has not been started). Because of the long vacancy, an IRS Form 8823 would be filed and the unit considered in non compliance until the Owner/Agent can return the unit to rent ready status.

## ***Part 2: Development Operations***

### **Procedures in Qualifying Tenants**

Due to the scarcity of affordable housing resources, and the need to allocate those resources to needy households, Owner/Agents must ensure that they take the steps necessary to provide housing only to those who are truly low-income. Owner/Agents must ensure that they adhere to appropriate steps within the application process in order to assure an effective allocation of housing resources.

### **Application Process**

Owner/Agents must be diligent in obtaining complete and accurate tenant information when collecting tenant applications. The application form is the first step in determining tenant eligibility. Therefore, the application should request complete and comprehensive information regarding income, assets, student status, and previous rental and employment history.

Owner/Agents should also demonstrate due diligence in determining applicant eligibility by asking applicants a *minimum* of these questions: Full name; date of birth; student status; household status; current employer; previous employer; current address; previous address for the last 2 years; if the household receives rental assistance; and if there are any anticipated changes to the household in the next 12 months. In addition to this information, an income and asset declaration form should be completed detailing all sources of an individual's income and assets. Owner/Agent's due diligence in determining applicant eligibility must be verifiable. IHFA strongly suggests that Owner/Agents alter or add proper verbiage to Income/Asset Declarations to ensure applicants are asked anticipated income questions. Move-in questions such as these help to ensure compliance and may protect Owner/Agents against tenant misrepresentation when anticipating income.

IHFA strongly suggests that all future adult household members complete a separate application to ensure all documentation is covered and Owner/Agents have performed due diligence when determining move-in eligibility.

*Note. Please refer to Example 7 “Insufficient Documentation of Initial Eligibility” on page 4-35 in the Revised 8823 Guide for additional information.*

IHFA also strongly suggests that Owner/Agents adopt a Resident Selection Policy that provides for credit/criminal background screening and landlord references for every potential tenant. Screening criteria when properly and consistently employed may decrease the likelihood of problems going forward.

*Note. Tax Credit developments that have HOME units are required to have Resident Selection Policies per HOME regulations. Owner/Agents must have the policies available for review during IHFA audits.*

## **Income and Asset Determination**

The IRS Code states: “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) and not in accordance with the determination of gross income for federal income tax liability.” Additionally, household income is defined as the gross annual income (with no adjustments or deductions) the household anticipates it will receive in the 12-month period following the effective date of the household’s certification of income. According to the Revised 8823 Guide, if a household’s income cannot be based on current information because the tenant reports little or zero income or income fluctuates, income may be determined on actual income received or earned within the last twelve (12) months before the certification.

*Note. As stated In Chapter 4 in the Revised 8823 Guide, “Income includes, but is not limited to, earned and unearned income from all household members age 18 and older (adults, including foster adults), unearned income of minor children and foster children under the age of 18, and income from assets.”*

The HUD Handbook 4350.3 REV1, CHG. 3 Chapter 5, provides a discussion of how to correctly calculate gross income. Further, Exhibit 5-1 and 5-2 of the HUD Handbook both list income and asset inclusions and exclusions. Since a variety of eligibility situations arise during certification processing, IHFA encourages tax credit development Owner/Agents to be familiar with income-qualification requirements and protocols. The list of suggestions below, while not all-inclusive, is provided to assist in the qualification and certification process.

### **Gross Annual Income**

Considerations when determining gross annual income include:

- Gross income should always be annualized even if the period of time is less. For example, a teacher may only work for nine months but their income must be annualized. The only time their income is not annualized is if they have a second job during their break and both incomes would be calculated by using 9 months for the teaching job and 3 months for the other. Please see Chapter 4, Page 4-9 in the Revised 8823 Guide for an example of this type of income calculation.
- Owner/Agents must calculate gross income by both the traditional way (hours, rate of pay and weeks) and by the Year-to-Date earnings (YTD). The highest calculated amount must be used as the tenant’s anticipated gross employment income.
- If third-party verification states a range of hours worked, i.e. 7-10, Owner/Agents should use the average to calculate anticipated number of hours worked. However, if it is Owner/Agent policy to use the highest number in the range, IHFA auditors will accept the calculation, with the stipulation that Owner/Agents are aware that they may prevent someone from qualifying for a tax credit unit by calculating the higher hours worked.
- Military employment- The following is updated guidance for military income per the Revised 8823 Guide:

1. A temporarily absent individual on active duty must be removed from the household and his/her income must *not* be included in the computation of household income, unless (1) that person is the head of the family, spouse or co-head or (2) the spouse or a dependent of the person on active military duty resides in the unit.
2. Military Basic Housing Allowances are included as income unless the low-income building is situated in any county or adjacent county in which a qualified military installation is located. Please see pages 4-10-4-11 of the Revised 8823 Guide for more information on qualified military installations.
3. Deployment of a military tenant to active duty does not mean the household must break their lease and move. Owners may allow households to stay in units and remain in compliance. Please see Page 4-11 of the Revised 8823 Guide for guidance.

Per the HUD Handbook 4350.3 REV.1 Chg. 3, GI Bill military income is not counted as student aid, as the money is sent directly to the tenant. The entire amount is counted as gross income.

Per the HUD Student Rule, and noted in the Revised 8823 Guide, “The treatment of a student’s income is dependent on the age of the student, type of income and the status of the student within the household.” The rule does not distinguish whether the student is living in the household or away at school.

1. If the full-time student is 18-years old or older and is the head of household, spouse or co-head, all income is included. ( See Exclusions Below)
2. If the full-time student is 18 years of age or older and a dependent, only the lesser of actual earned income or \$480 is included, along with gross income and income from assets.
3. If the full-time student is a minor, then only unearned income and income from assets is included. No income from employment is included.

The Revised 8823 Guide now distinguishes financial aid income calculations: Effective October 2009, income calculation from educational scholarships and grants applies only to tenants who receive Section 8 Assistance.

If a Tax Credit household receives a Section 8 tenant based voucher assistance, or if the household lives in Section 8 project based development that has a layering of tax credits, HUD Handbook 4350.3 REV1 Chg. 3 student financial aid calculation rules apply. Annual grants and scholarships must be subtracted from the annual tuition amount **and** the remaining amount is included as income.

*Note. Financial assistance does not include loan proceeds.*

Financial assistance in excess of tuition is not includable in income in two instances. The following are two applicable exemptions:

1. The student is over the age of 23 with dependent children and/or,
2. The student is living in a unit with his or her parents who are applying for or receiving Section 8 assistance.

If a household is **NOT** receiving Section 8 assistance, all forms of financial aid are **excluded** from gross income. It doesn't matter whether the financial assistance is paid directly to the tenant or the educational institution; the income is excluded from gross income.

*Note. Per the HUD Handbook 4350.3 REV.1 Chg. 3, GI Bill military income is not counted as student aid, as the money is sent directly to the tenant. The entire amount is counted as gross income.*

- Per HUD's Rental Housing Integrity Improvement Program (RHIIP) and the HUD Handbook 4350.3 REV1 CHG 3, irregular, nonrecurring monetary gifts or contributions to tenant are **not** included in gross income.
- Income from a Sole Proprietorship can be estimated, per the Revised 8823 Guide, by reviewing an individual's prior year tax returns and Schedule C. If necessary, the Owner/Agent may ask the tenant/applicant to provide a signed Form 8821, which allows Owner/Agents to verify tax information with the IRS.

*Note. A tax return must be filed for ALL self-employed individuals who operate sole-proprietorship businesses or otherwise report income on Schedule C, regardless of whether the taxpayer is reporting a profit or a loss.*

- **Businesses in the Home:** According to the Revised 8823 Guide, "A low-income tenant may use a portion of a low-income unit exclusively and on a regular basis as a principle place of business, and claim the associated expenses as tax deductions, as long as the unit is the tenant's primary residence." IHFA encourages Owner/Agents to establish policies for home-based businesses to maintain control over how your development is used without restricting your tenants' ability to make a living.

Owner/Agents may consider adding the following policies to house rules and leases:

- Prohibiting tenants from starting home-based businesses without first getting Owner/Agent approval.
- Prohibiting businesses that may cause heavy traffic and as a result, violate local zoning laws. Prohibiting businesses that may create parking issues at your development or may disrupt other tenants with frequent UPS or FEDEX deliveries, Prohibiting businesses that may create heavy foot traffic, thus

increasing the wear and tear of common area flooring. Prohibiting businesses that may increase noise levels, which may bother tenants.

- Requiring tenants who run home-based businesses to carry liability insurance to ensure that the owner is protected if a tenant's customers or employees are injured on the property. IHFA also recommends that tenants name the Owner as an "additional insured" on their policies.
- Obtaining copies of licenses from those tenants who are required to be a licensed business, such as a day care.
- Outlining specific requirements for home-based business in a lease addendum.

### **Asset Income**

Special considerations relative to counting income derived from assets are:

- Assets should always be included on the Tenant Income Certification (TIC) whether or not the asset yields actual income.
- Owner/Agents should never assume that because a household has little income, that they have no assets.
- There is no limit on the amount of assets a household may hold and they are not required to convert an asset to cash in order to live in a tax credit unit.
- If an applicant/tenant declares a combined total asset value of less than \$5,000, third-party verification is not necessary. However, any actual income the applicant/tenant receives from the asset must be added to regular income. An Under \$5,000 Certification may be used to self-certify total assets under \$5,000 in lieu of a third-party verification.
- If total assets exceed \$5,000, third-party verifications must be sent to all appropriate asset holders to verify the accounts and pertinent balances. The asset income included in household gross income will be the greater of: (a) the actual asset income, or (b) the imputed income from assets, which is the net family assets multiplied by the passbook rate specified by HUD. Please check with your auditor to determine the current HUD passbook rate.

*Note. Owner/Agents who have HOME units must verify all assets through the third-party verification process, in accordance with HOME regulations.*

- When determining asset income, Owner/Agents must calculate the cash value of an asset. Cash value is defined as the market value of an asset minus any reasonable costs that would occur if the asset were converted into cash unless it is already in cash form. Costs may include brokerage/legal fees when selling an asset, penalties on an investment like an IRA for early withdrawal and costs for real estate transactions.

- At each certification and annual recertification, applicants and tenants must declare whether or not an asset has been disposed of for less than fair market value during the two years preceding the date of application or the effective date of the recertification. An asset is considered disposed of for less than fair market value if the cash value of the asset disposed of exceeds the gross amount the tenant received by more than \$1,000.00. If it does exceed this amount, for two years Owners must include in the total household assets the difference between the cash value of the asset and the amount received.

## **Verifications**

All regular sources of income, including asset income must be verified. In order of their acceptability under LIHTC and HUD guidelines, verifications should be accomplished in the following order: (1) Through a third-party via direct written communications; (2) Through second-party activities such as check stubs, W-2's, bank statements, and divorce decrees that are supplied by tenants/applicants; or, (3) Through tenant/applicant self-certifications. Methods other than third-party verifications should be used only when third-party verification methods have been attempted for a minimum of two weeks (efforts must be documented), and are deemed to be either impossible or impractical. Third-party verification activities must be conducted independent of tenant involvement – i.e., tenants may not be allowed access to verification documentation such as through hand-carrying forms or documents to, or returning forms from third parties.

Verifications must contain complete and detailed information and must, at a minimum, include direct written information from all sources of regular income. The required employment verification must be thoroughly completed by the employer. If any mandatory information is not provided, Owner/Agents must follow-up with a phone clarification to obtain the information that was omitted in the original verification. Clarifications must be documented in the tenant file. Complete verifications and/or phone clarifications are a key program requirement and thus are subject to in-depth review during compliance audits.

*Note. An Owner/Agents failure to obtain complete and detailed information from employers will be determined by IHFA to be deficient in owner due diligence.*

According to the HUD Handbook 4350.3 REV1 CHG 3, Page 5-52 & 5-59, if third-party verifications are not received within two (2) weeks of the request, Owner/Agents may attempt to verify income and assets via second-party verification such as pay-stubs. However, before second-party verifications are pursued, Owner/Agents must document their attempts at obtaining third-party verifications. Such documentation may include fax cover sheets or written notes indicating follow-up efforts to obtain the third-party verification. The follow-up evidence and documentation must be placed in the tenant file.

*Note. Third-party verifications must never be altered.*

Owner/Agents must never write on the verification themselves. Writing in calculation information, or filling in incomplete areas on the verification itself will invalidate that verification. Additionally, “whiteout” must never be used, as this will call the validity of the original information into question. If there is a need to clarify information, a phone clarification document should be used to obtain and record any additional information not appearing on the third-party verification. Clarification documents must have the name and signature of the party completing the clarification document, the date and time performed, and the source of the additional information, including the name and title.

Phone clarifications must never be used in place of third-party verification. The phone clarifications should only be used when third-party verification is not clear or complete and/or there is conflicting information. Clarifications will not supersede any information originally obtained through third-party verification. The third-party information must be used to qualify applicants/tenants.

Third-party verifications are valid 120 days prior to the effective date of move-in.

***Note.** Verifications must be received by Owner/Agent prior to the execution of the TIC and the actual move-in date. They may not be obtained after the actual move-in date, as this is considered non compliance.*

### **Forms of Verification**

The following briefly describe acceptable forms of verification:

- Employment Income: The IHFA required verification form must be completed by the employer and include the anticipated income for the following 12 months, as well as current year to-date earnings. If employer verification is not possible, then current check stubs from the employer showing gross income per pay period and frequency of pay should be collected. As a last resort, a copy of the most recent income tax return signed by the applicant/tenant or copies of Form W-2 providing the amount of income, including income from tips and other gratuities, supported by current check stubs from the employer could be used.
- Self-Employment Income: Self-employed applicants/tenants must provide sufficient documentation to prove they are income qualified. A tenant statement, whether notarized or not, is not sufficient documentation to verify income. In this case, when obtaining written third-party verification is impossible, Owner/Agents must obtain the following tenant-supplied documentation in support of tenant eligibility:
  1. An independent accountant’s statement or attorney’s statement of net income,
  2. IRS Form 1040 with Schedule C (business income) for the past year. This form is only valid if the tenant was self-employed, in the same profession, throughout the previous year.
  3. An audited or unaudited financial statement of the business, as well as a self-certified statement signed by the applicant/tenant stating the anticipated income for the 12 months following certification.



Social Security, Pensions, Supplemental Security Income (SSI) Income: A benefit verification form completed by the agency providing the benefits, or an award letter or benefit letter, or other printout prepared by the authorizing agency.

*Note. Since income calculations are based upon anticipated income figures for the following 12 months, Owner/Agents must include the published Cost of Living Adjustment (COLA) in the calculation of gross income. The COLA can be found on the Social Security Administrations web site.*

Unemployment Compensation: A verification form completed by the unemployment compensation agency, or records from the unemployment office stating payment dates and amounts.

*Note. Unemployment compensation benefits must be annualized regardless of the number of weeks noted on the third-party verification. However, if you are aware that the tenant will be obtaining employment, calculate the employment as well as the remaining weeks of the unemployment compensation. Please see Example 3 on Page 4-9 of the Revised 8823 Guide for further assistance.*

Alimony & Child Support Payments: A copy of a separation or settlement agreement or a divorce decree stating the amount and type of support and payment schedule, a printout or statement from the Support Enforcement Agency, a signed statement from the person paying support (i.e. a former spouse not currently residing in the household), or a signed self-certification by an applicant/tenant indicating that they are not receiving child support payments, and have taken all legal steps to enforce collection.

If a signed non-receipt of support self-certification is accepted, that statement should indicate whether the tenant will be seeking or expects to receive child support payments within the next 12 months. The self-certification must be accompanied by a print out from the Child Support Enforcement Agency listing no open case(s). If the tenant has a child support agreement, but is not presently receiving child support payments, the applicant/tenant should include an explanation and all supporting documentation; i.e. divorce decree or court documents. The self-certification, according to the Revised 8823 Guide, should also indicate the tenant will notify the owner of any future changes in the status of child support payments.

*Note. You must include the amount specified in a divorce settlement, separation agreement or other legally binding document as income unless the applicant/tenant certifies: (1) the income is not being provided, and (2) he/she has made reasonable effort to collect the amounts due, including filing with courts or agencies responsible for enforcing payments.*

Recurring Contributions and Gifts: Self-certified statement or affidavit signed by the person providing the gift and indicating the frequency and value of the gift, a verification letter from the bank, attorney or a trustee administering the gift, or a notarized statement

from the receiver of the gift stating the frequency and value of the gift and copies of the checks.

*Note. A recurring contribution or gift may be nonmonetary in nature. Regular nonmonetary contributions to the household by those not living in the unit are considered income. For instance, if an applicant has their bills paid by an outside third party, the amount paid is counted as income. Such bills may include utility bills, car bills and cell phone bills. Groceries however, even if provided by someone outside the household on a regular basis, are not included as income. Please refer to Chapter 4 of the Revised 8823 Guide.*

Public Housing Authority/Section 8 Voucher Holders: If an applicant/tenant is receiving a Section 8 Voucher housing assistance payment, Owner/Agents do not have to obtain written third-party verifications and are no longer required to obtain the 50058 from Public Housing Authorities. According to the Revised 8823 Guide, Owner/Agents may accept and rely upon a statement from the Public Housing Authority (PHA) that certifies the voucher holder does not exceed the applicable LIHTC income limits. The Statement form, found at **Exhibit 2**, is the mandatory document required for Section 8 voucher holder information in lieu of obtaining a 50058 from the PHA, or third-party verifications. If Owner/Agents are unable to obtain the Statement from the PHA, they must then follow third-party verification procedures necessary to income-qualify the applicant/tenant. Owner/Agents do not have to use the PHA Statement. However, if you elect not to use the statement, you must third-party verify all documentation. IHFA will not accept the 50058 as sufficient documentation for Section 8 voucher holder tenants.

*Note. The gross income, as noted on the new PHA-supplied Statement, must be reflected on the TIC. IHFA will accept the PHA Statement for recertifications only. Owner/Agents must third-party verify all documentation for applicants at initial qualification.*

Unemployed/Zero Income Household Members: The income of unemployed applicants/tenants with regular income from any other sources, such as Social Security, pension, recurring gifts, etc., must be verified as specified in the HUD Handbook 4350.3 REV CHG 3, Ch. 5.

When determining household eligibility for the LIHTC program a comprehensive look at the household's income viability must be considered. According to the Revised 8823 Guide: "If the household's income cannot be determined based on *current* information because the household reports little to zero income, or income fluctuates, income may be determined based on actual income received or earned within the last twelve months before the determination." IHFA requires that any applicant that has been previously employed within the last twelve months to anticipate income based on their previous work history or prove why not. If an Owner/Agent does not anticipate income for an applicant that has been previously employed, and that applicant becomes employed prior to the first year re-certification, the household could be deemed in non compliance from move in.

**Example:**

Jim and Joyce are both in their early 20s and are looking to move into a 60%, 2 bedroom unit with a rent of \$500 a month. Jim is currently working at the Quick Stop making \$7.25 an hour, 25 hours a week. Joyce currently is unemployed and has completed a zero income self affidavit.

If Joyce's application states that she had been previously employed in the last 12 months should she actually claim zero income?

Since Joyce had been previously employed the diligent action would be to anticipate income for her based on her 12 month work history. If the Owner/Agent chooses to accept the zero income self affidavit from Joyce and she obtains employment prior to the first year re-certification that puts the household over income, the household is in non compliance from move in.

Student Status: Owner/Agents must include student status questions on applications and/or questionnaires to determine if an applicant or tenant has been a student for any portion of five calendar months within the current calendar year. This question will allow Owner/Agents to demonstrate due diligence in determining student status prior to move-in and/or annual recertification. Full-time and part-time student status must be verified for eligibility purposes.

Owner/Agents must verify full-time student status for all adult household members, by sending third-party verifications to appropriate educational institutions.

## **Tenant Income Certification**

Once all sources of income and assets have been properly obtained, Owner/Agents must calculate and record annual gross income using a Tenant Income Certification (TIC) **Exhibit 1** to document formally that the applicant/tenant qualifies for LIHTC housing. The TIC must remain in the tenant file.

### **TIC Effective Dates**

The effective date of an applicant/tenant's TIC is the date the tenant actually moves into the unit. All adult members of the household must sign the certification at the time of move-in. Per the Revised 8823 Guide, if the certification is more than 120 days old, the applicant/tenant must provide a new certification.

Income recertifications performed annually must be based on the anniversary of the move-in effective date.

If for whatever reason an Owner/Agent is late in completing an annual recertification, the TIC effective date will be the tenant signature date. The next annual recertification, if performed in a timely manner, will again be the anniversary date of the original move-in. All recertification documentation must be obtained and the TIC generated before tenants sign the late recertification paperwork. Backdating TICs is an event of noncompliance.

### **TIC Signatures**

Pursuant to the Revised 8823 Guide, all adult household members must sign all documents and forms, either before the effective date of a recertification, or the day they move-in to the unit in order to be in compliance with LIHTC guidelines. This stipulation includes the lease and the TIC. However, there will be situations where obtaining signatures will be impractical. In these circumstances, Owner/Agents should document the reason for the delay in the tenant's file and secure the signature as soon as possible.

Owner/Agents must ensure that TICs are thoroughly and accurately completed, and that all required signatures have been obtained. Incomplete or inaccurate TICs will represent an event of non-compliance. Common errors include the following: incorrect effective and move-in dates, incomplete Section 8 rental assistance information, HOME program units are not complete, incorrect income and rent limits and BIN number inaccuracies.

### **Adding Additional Household Members after Move-in**

According to the Revised IRS 8823 Guide, if an income qualified person moves into a unit and "soon thereafter", a second tenant joins the household putting the household above the income limits, the unit is out of compliance as of the original tenant's move-in date. The IRS has not, to date, defined "soon thereafter." In order to remove the ambiguity this provision created, IHFA has made the determination that a change in household composition that occurs within the first six (6) months of tenancy will be deemed to have occurred "soon thereafter." (IHFA's adoption of this definition is consistent with accepted industry practice in this area as it has evolved since the release of the 8823 Guide.) The new/changed household must re-qualify for the unit as of the date of original move-in. If the original move-in occurred prior to new published income limits, and the new tenant moves in after the new income limits, the household must re-

qualify at the old income limit rates. In other words, the new/changed household must qualify under the income limits that were in place at the date of original move-in.

If a new household member moves into a household after the original six (6) months have passed, the household will not have to re-qualify since the event did not occur “soon thereafter.” The new household member must sign a lease and Owner/Agents must prepare a new TIC to reflect the new household composition of the unit. Only at annual recertification will the new household member’s income be included in gross income.

### **Recertification**

Owner/Agents are required to recertify each low-income household at least annually and may begin 120 days prior to the anniversary date of move-in. The recertification process is identical to the initial certification in terms of documenting household composition, income and income from assets. The annual recertification process also assists Owner/Agents in identifying changes in household attributes such as student status, household composition changes, and provides for compliance with the next available unit rule.

Owner/Agents are in compliance if the recertification process is completed within 120 days before anniversary date of move-in. If an Owner/Agent has sent timely recertification notices to a tenant, but the household does not respond because they are vacating the unit, the vacated unit will not be considered out of compliance with the recertification requirements. Owner/Agents must always document the attempts made to recertify the household by placing copies of the 120, 90, 60 and 30 day notification of annual recertification in the tenant file. IHFA may determine whether it is the fault of Owner/Agents or the tenant if a recertification is late whether or not notification letters were sent to the tenant in a timely manner or at all.

Prior to the Revised IRS 8823 Guide, it was common practice to accept an interim/annual certification date as a starting date for the next annual recertification in LIHTC developments with Rural Development (RD) subsidy and project-based Section 8 developments respectively. As of January 2007 and the advent of the 8823 Guide, this practice is no longer deemed to be acceptable. All RD as well as project-based Section 8 developments must recertify tenants on the anniversary date of the original move-in under the LIHTC program – regardless of when the last interim/annual recertification in any layered program may have taken place.

### **100% Low-Income Developments and the Annual Recertification Waiver**

As part of the Housing and Economic Recovery Act (HERA) legislation passed in 2008, the tax code was amended to read as follows:

“...the determination of whether the income of a resident of a unit in a project exceeds the applicable income limit shall be made at least annually on the basis of the current income of the resident. The preceding sentence shall not apply with respect to any project for any year if during such year no residential unit in the project is occupied by a new resident whose income exceeds the applicable income limit.”

As a result of the new legislation, Owners of 100% low-income developments can immediately stop completing the annual tenant income recertifications.

In response to the legislation, IHFA has adopted a policy that all 100% tax credit households must be re-certified once. After the first year recertification, the household may self-certify. The required self-certification packet is located at [www.ihfa.org](http://www.ihfa.org). When Owner/Agents utilize the packet, a Tenant Income Certification (TIC) must be included to certify a household's eligibility.

*Note. The requirement to verify student status was not waived with the passage of HERA. Therefore, student status must continue to be self-certified and when a household state they are students within the self-certification packet, Owner/Agents must third-party verify student status with appropriate educational institutions.*

### **Non-Compliance at Recertification**

A LIHTC unit is considered to be noncompliant and subject to an 8823 submission if the annual recertification is not performed or the annual recertification was performed *late and/or after notification of* an IHFA compliance review. If non-compliance is determined by the Owner/Agent and corrected prior to notification of an IHFA review, the unit is not considered to be in non compliance and an 8823 will not be submitted to the IRS.

If during an IHFA review potential recertification non compliance is discovered, Owner/Agents must comply with all procedures including IRS protocol. According to the Revised 8823 Guide, there are two methods Owner/Agents may use to correct noncompliance. With both methods, Owner/Agents must submit copies to IHFA of all documents that demonstrate the issue has been rectified.

1. A recertification can be performed using current income and asset sources and current income limits. If there is no resulting noncompliance such as a violation of the Next Available Unit Rule, the unit would be in non compliance on the date of the recertification was due and back in compliance on the date the tenant signed the recertification paperwork.
2. A retroactive recertification can be performed which clearly documents all sources of income and assets that were in place at the time the recertification should have been completed and applies income limits that were in effect on that date. If there is no resulting non compliance such as a violation of the Next Available Unit Rule, the unit would be in non compliance on the date the recertification was due and back in compliance on the date the tenant signs the certification.

Even though the certification is performed retroactively, the recertification documents should be dated with the current date. All adult members of the household should sign the TIC and all appropriate documents with the current date. **Backdated documents are not acceptable and are considered to be an event of noncompliance.**

In both methods the effective date on the TIC will be the anniversary of the actual move-in date.

### **Changed Income after Move-In**

The LIHTC program exists to provide affordable housing resources to those that are truly in need of such assistance. Changes in individuals' incomes can and do occur with a fair degree of regularity. IHFA acknowledges this situation and is supportive of individuals' efforts to better their life circumstances. However, due to the potential for misrepresentation by applicants in this area, IHFA has determined that a defined timeframe is appropriate in order to address ambiguity surrounding this issue and in order to assist Owner/Agents with compliance in this area.

Thus, an increase in income within the first 60-days of tenancy that puts a household over the initial income limits will be considered a misrepresentation of eligibility unless the Owner/Agent can demonstrate through due diligence, and to a reasonable degree of certainty, that the changes were unintended and unanticipated as of the date of move-in. If this level of assurance cannot be demonstrated, the household will be deemed ineligible, and the unit deemed to be in non compliance as of the move-in date. To reiterate, Owner/Agents must be able to demonstrate that the changes were unintended to a reasonable degree of certainty, in order to avoid an event of non-compliance.

*Note. It is the Owner/Agents responsibility to demonstrate due diligence through comprehensive applications and documentation. IHFA considers Owner/Agent move-in documentation and how much due diligence was performed to prevent tenant fraud at move-in. Please reference the Revised 8823 Guide Pages 4-33 and 4-25 for further guidance.*

In order to illustrate this requirement, consider the following example: An applicant states on the application that they are not working and do not intend to work in the next 12 months. They also have no prior employment history. Further, the applicant completes a Statement of No Income, wherein they further state they are currently not working and do not intend to seek employment in the next twelve months. After move-in, the tenant decides within the first sixty (60) days of tenancy to seek employment. Therefore, the household may be considered over-income and the unit may be in non compliance if income from these changed circumstances places the household's income over the current income limits.

When the Owner/Agent discovers this circumstance at the tenant's first annual recertification, they must perform due diligence and re-qualify the household at the point where income changed in order to ensure the household was not over the income limits in effect at the time of original move-in. If the household is over-income as a result of the re-qualification process, the Owner/Agent must either perform the necessary due diligence required to effectively demonstrate that the change was neither anticipated nor intended at the time of move-in; or the Owner/Agent must recognize a non compliance condition, and proceed with the appropriate corrective actions necessary to bring the unit back into compliance.

## **Acquisition and Rehabilitation**

The trend today in low-income housing is for developers to acquire aging developments and update properties with the assistance of Low-Income Tax Credits as well as other funding sources. Most often, tenants continue to reside in the units when Owners purchase the development and conduct the rehabilitation. The IRS has developed protocol on how to income qualify in-house tenants. The protocol depends on whether the credit period has started or whether the acquisition is prior to the credit period. Please reference the Revised 8823 Guide Chapter 4 for more information on the differences in protocol.

## **Tenant Misrepresentation or Fraud**

Owner/Agents must be able to demonstrate due diligence in their efforts to prevent tenant fraud. According to the Revised 8823 Guide, "...fraud includes **deliberate** misrepresentation of fact in order to induce someone else to part with something of value or surrender a legal right. The outcome of deliberate misrepresentation by a tenant can result in the development's owner/agent renting a unit to an ineligible tenant at below market rate..."

If misrepresentation is suspected, Owner/Agents must take the necessary steps to verify the accuracy of the information provided by the tenant. If necessary, Owner/Agents may ask the tenant to complete IRS Form 8821, Tax Information Authorization, which will provide confirmation to the Owner of the accuracy of the tenant's IRS tax return.

*Note. Consult Chapter 25 of the Revised 8823 Guide for additional details relative to fraud-related program requirements, and Owner/Agent responsibilities in this area.*

## **Other Issues Impacting Development Operations**

### **Leases**

All tenants occupying tax credit units must be qualified low-income tenants, and must have executed a lease no later than the date the tenant takes possession of the unit. All adult members of the household, including dependents that are 18, must sign the lease agreement. The lease start date and the move-in date must be the same date and be reflected as such on the TIC.

IHFA does not specify a model lease for LIHTC developments as long as the lease contains information sufficient to satisfy the following minimum requirements:

- Legal name of the parties to the agreement and all additional occupants.
- Unit number.
- Date the lease is effective.
  
- Term of the lease (minimum of 6 months per IRS, regulations unless the housing is Single Room Occupancy [SRO], where 30-day lease terms are appropriate).



- The amount of rent tenant must pay for the duration of the lease.
- The rights and obligations under the lease, such as the obligation to recertify income annually.
- Signature pages including dates.

*Note. Project Based Section 8/Tax Credit developments may use the HUD Model lease.*

*Note. Owner/Agents must ensure that they enter into leases under the LIHTC program with all Section 8 Voucher holders.*

### **LIHTC Developments Combined with Other Assistance Programs**

Properties that combine LIHTC with HOME or other federal programs have a unique set of rules that must be observed in order to maintain compliance with program regulations. It is imperative that applicants are Tax Credit eligible before any additional regulatory requirements are met. In other words, the LIHTC program is the primary program and all requirements associated with it must be satisfied before additional requirements related to other programs are observed. The following is a list of the types of programs that may be associated with the LIHTC program:

1. HOME: If HOME funds are included in a LIHTC development, at least twenty percent (20%) of the total units must be reserved for households with incomes at or below fifty percent (50%) of the Area Median Income and eighty percent (80%) of the HOME funded units be rented to households at sixty percent (60%) or less of Area Median Income.

For HOME units to qualify as low-income units, rents and income cannot exceed either program limit. Low HOME rents are subject to fifty percent (50%) HOME income and rent limits. High HOME rents are subject to sixty-five percent (65%) of AMI or FMR, whichever is less. Further, high HOME income limits are at sixty percent (60%) of AMI. HOME units can be deep skewed at the thirty percent (30%) or forty percent (40%) income and rent limits. Owner/Agents must be aware that both deep skewed unit types have HOME income limits, however rent limits are not stated on the HOME rent limit charts. Therefore, Owner/Agents must use the Tax Credit rent charts to obtain thirty percent (30%) and forty percent (40%) rent limits. If a unit is being counted under both programs, the stricter rent income and rent limit applies.

*Note. Owner/Agents may have to obtain both Tax Credit and HOME income and rent limits to determine household eligibility.*

When tenants receive additional subsidy through rental assistance such as Project-Based Section 8 or Rural Development (RD), the rents may be raised to the rental assistance program limit only if the following HOME requirements are met:

- The tenant is paying no more than thirty percent (30%) of their adjusted income.

- The subsidy is project-based (affects the entire development, not just a single unit).
- The tenant's income is less than fifty percent (50%) of the Area Median Income.

*Note. The Tax Credit rule of allowing the tenant's rent to be raised to the higher Project Based Section 8 rent limit as long as the tenant pays no more than thirty percent (30%) of their adjusted monthly income does not apply when a unit is combined with HOME funds. According to the Revised 8823 Guide, the "portion of the rent paid by Section 8 tenants can exceed the LIHTC rent ceiling as long as the owner receives a Section 8 assistance payment on behalf of the tenant." This does not apply to HOME units.*

Unless the subsidy is project-based (not tenant-based), the total HOME rent is the maximum amount from all sources that the Owner/Agent may receive for HOME assisted units. Therefore, a tenant's rent, utility allowance, and rental subsidy amount CANNOT equal more than the applicable HOME rent limit.

In addition to obtaining the HOME income and rent limits, Owner/agents must follow three HOME Program requirements.

- Owner/Agents must complete Affirmative Housing Marketing Plans and have them available during IHFA audits.
- Tenants, who live in HOME designated units, must sign a one-year initial lease.
- The HOME program also dictates that all leases include a HOME Lease Addendum. Addendum can be located at [www.ihfa.org](http://www.ihfa.org). The Lease Addendum must be included with every new lease signed by a HOME unit tenant.

HOME regulation requires third-party verification of all assets, whereas the Tax Credit program rules require third-party verification of assets only if the household's combined assets are greater than \$5,000. For units that combine both HOME and LIHTC units, the stricter HOME rules apply and all assets must be third-party verified.

For those Owner/Agents who must adhere to both program requirements in one development, IHFA ensures compliance through annual monitoring. Under the Tax Credit program, the affordability period is generally 30 years, unless developments agree to longer extended use periods. Developments with HOME monies may have affordability periods of 5-20 years depending upon the type of development and the amount of HOME dollars invested. As a result, developments with combined HOME and LIHTC units may be subject to two sets of affordability periods and will be monitored according to each specific program requirement.

*Note. You may find the affordability period in the Regulatory Agreement documents of your development.*

*Note. Failure to establish and maintain compliance with HOME regulations could result in an event of default under the HOME Note, Deed of Trust and Regulatory Agreements, which would be noted as a Program Violation.*

For additional HOME information please see the HOME Compliance Manual at [www.ihfa.org](http://www.ihfa.org).

2. Rural Development (RD): Rural Development subsidy may be included in LIHTC developments. Owner/Agents must not only certify through the subsidy process that the tenant is receiving rental subsidy, but is also qualified to live in a LIHTC unit. A Tenant Income Certification must be completed for these units as well.
3. Deep Skewed Units: In addition to an election of the minimum set-aside, Owner/Agents may elect to provide housing to households with incomes of forty percent (40%) or less of the Area Median Income. The election of the deep skewed units is a means for developers to gain additional points in the qualified allocation process. By agreeing to allocate units at a thirty percent (30%) or forty percent (40%) Area Median Income, Owner/Agents agree to rent units to those households whose income is extremely low.

According to the Revised 8823 Guide, under deep-rent skewing”, set-asides at least fifteen percent (15%) of the low-income units in the development must be occupied by households with incomes at forty percent (40%) or less depending on the percentage designation of the development. Gross rent must not exceed the maximum gross rent applicable for the deep-skewed percentage elected.

Once made, the minimum set-aside and deep-skewed elections are irrevocable. Therefore, the applicable minimum set-aside and deep-skewed designations are set for the duration of the initial 15-year compliance period as well as the extended use period.

For developments with thirty percent (30%) and forty percent (40%) Area Median Income unit restrictions, Owner/Agents must apply the one-hundred and forty percent (140%) or Next Available Unit Rule at annual recertification. Based on the assumption that the tenant was a qualified thirty percent (30%) or forty percent (40%) Area Median Income tenant at move-in, the tenant or household continues to be a qualified tenant provided the tenant’s income does not increase above one hundred and forty percent (140%) of the applicable thirty percent (30%) or forty percent (40%) gross Area Median Income limit.

If the tenant’s income increases above one hundred and forty percent (140%) of the thirty percent (30%) or forty percent (40%) gross Area Median Income limit, then the next available unit of equal size or smaller (subject to the established square footage applicable fraction) must be rented to a qualified thirty percent (30%) or forty percent (40%) Area Median Income tenant. The rent of the “over-income” tenant will remain at the thirty percent (30%) or forty percent (40%) level until such time as the next available unit is rented to a qualified tenant. Once the next available unit is rented to a qualified

tenant, the rent of the “over-income” tenant can be converted to the next applicable Area Median Income level, depending upon the minimum set-aside.

*Note. LIHTC regulations only require a minimum set-aside of 20/50 or 40/60. However, the Revised 8823 Guide does state that a development is in compliance when the elected minimum set-aside and the elected deep-skewed requirements (fifteen percent (15%) of the deep-skewed units) are met by the end of the first year of the Owner/Agent’s credit and compliance period and continues to be met each year throughout the compliance period. Owner/Agents must be aware of the minimum set-aside and deep-skewed designations for their own developments. The Placed-in Service Application and Regulatory Agreement should be available to those who are responsible for adhering to these requirements.*

4. Project-Based Section 8/Tax Credit Developments: Project-based Section 8 developments may include Tax Credit allocations. Such allocations come with separate compliance regulations. See IHFA QAP for step by step information on acquisition rehab or rehab requirements.

During a compliance audit, however, all EIV, Enterprise Information Verification information used in verifying Project-Based Section 8 income, must not be in the same file as the tax credit documentation. IHFA Tax Credit and HOME auditors must not have access to EIV information. If so, IHFA auditors have the obligation to inform the IHFA Housing Compliance Manager. Owner/Agents may have their EIV privileges revoked by HUD if they are in violation of this rule.

### **Extended-Use Agreement**

For all buildings allocated tax credits after 1989, IRS regulations dictate that Owner/Agents enter into an extended use agreement. Extended use periods are typically reflected in paragraph 6 of the IHFA LIHTC Regulatory Agreement. Building Owners must agree to a long-term commitment on the first day of the 15-year compliance period and ending on the later of (1) the date specified by IHFA in the Regulatory Agreement or (2) the date, which is 15 years after the close of the 15-year compliance period. In other words, the Owner/Agent commits to maintain the development as a low-income housing project for at least 30 years. Owner/Agents may receive allocation points for electing for a longer extended use agreement.

### **Termination of Participation in the Program during the Compliance Period**

The IRS stipulates that there are several ways regulatory agencies can terminate tax credit participation. According to Treasury Regulation 1.42-14(d)(2)(iv), a State Agency such as IHFA may recapture the entire amount of credits allocated to Owner/Agents due to the following:

- A building is not placed in service within the required time period.
- A building fails to meet set-aside requirements.

- The building does not comply with the terms of its credit allocation.
- The Owner and IHFA mutually agree to cancel an allocation of credit.
- Tax credits allocated to a development are not necessary for the financial feasibility of the development.
- Egregious noncompliance.
- Voluntary withdrawal from the LIHTC program.
- Failure to respond to repeated notices of compliance reviews, annual reporting and owner certifications.

When tax credits have been recaptured or upon foreclosure, a building or development is no longer participating in the LIHTC program and the Extended Use Period is terminated. Owner/Agents must note that the termination of participation in the program and of the Extended Use Agreement does not mean tenant rights under the LIHTC program are forgone.

Tenant Rights must be protected subsequent to termination per the following:

- Eviction or Termination (other than for Good Cause) of a current tenant before the close of the 3-year period following the termination of the extended use period is prohibited; and
- A gross rent increase of any unit occupied by an existing tenant before the close of the 3-year period following the termination of the extended use agreement is prohibited. Therefore, income-qualified tenants continue to be rent restricted for three years or until the tenants vacate the unit, whichever comes first.

### **Changes in Ownership and/or Management**

If at any time ownership entities and management agent changes occur, the IHFA Compliance Department must provide prior written approval of such change.

All property management agents must be Qualified Management Agents. In order to be considered a Qualified Management Agent, the following documentation must be submitted:

- IHFA Management Agent Questionnaire
- IHFA Previous Management Experience Questionnaire
- Property Management Agreement
- Management Plan
- Affirmative Fair Housing Marketing Plan or similar document

IHFA reserves the right to request reference from other States in which the property management agent has done business. IHFA will not approve property management agents who have a history of non-compliance with IHFA or any other State.

## **Changes in Management Agent**

### ***Prior to Placed-In-Service:***

Changes in management prior to placed-in-service, is generally approved by IHFA's Multi-Family Finance Department. The Compliance Department will provide a recommendation for approval or non-approval.

Only qualified management agents will be approved. If a change in management occurs prior to the placed-in-service date, the following information must be submitted to IHFA:

- Property Management Agreement
- Management Plan
- Affirmative Fair Housing Marketing Plan or similar document
- Written consent from the syndicator/LP and all lenders

### ***After Placed in Service:***

Changes in management agent after the placed-in-service date must be approved by IHFA's Compliance Department. Only qualified management agents will be approved. If a change in management occurs after the placed-in-service date, the following information must be submitted to IHFA:

- Property Management Agreement
- Management Plan
- Affirmative Fair Housing Marketing Plan or similar document
- Written consent from the syndicator/LP and all lenders

### **Changes in Ownership:**

Changes in ownership must be approved, in advance, by IHFA's Compliance Department. If a change in ownership is anticipated, please contact the Housing Compliance Manager as soon as possible to discuss the necessary documentation.

## ***Part 3 – Compliance***

### **Compliance with Program Requirements**

IHFA is responsible for establishing compliance monitoring procedures based on LIHTC program requirements; utilizing the requirements contained in the IHFA Regulatory Agreement, IRS code, the Revised 8823 Reporting Guide, and HUD Handbook 4350.3 REV1, CHG3 and any other applicable regulations. IHFA conducts periodic inspections to assess the degree to which Owner/Agents are following the guidelines referenced above. Compliance with the applicable regulations is ultimately the responsibility of the Owner, who is liable for consequences resulting from non compliance. It is vitally important that Owner/Agents understand fundamental program requirements, IHFA monitoring procedures, how on-going compliance can impact tax credits, and participation in the program.

### **Regulatory Agreement**

Developments receiving an allocation of tax credits after December 31, 1989 must execute, and are subject to a Regulatory Agreement. The agreements are signed between Owner entities and IHFA, and are recorded in the county where the development is located.

A Regulatory Agreement contains covenants that govern the development throughout the compliance period. Such covenants include, but are not limited to the following:

- Amount of annual credit.
- Number of low-income units.
- Area Median Gross Income Targeting- 50% or 60%.
- Extended Use Term.
- Very Low-Income Targeting.
- Additional commitments pledged during the application / allocation process such as social service programs as noted in the Regulatory Agreement.

It is not only the responsibility of the Owner, but of the management agent as well, to understand the contents of the Regulatory Agreement. Both parties should acquaint themselves with all aspects of the development's commitments, and with provisions contained in the governing documents.

### **Additional Tax Credit Commitments**

Owner entities will often make additional commitments to receive preference points during the tax credit application and allocation process. These additional commitments are typically recorded in paragraph 10 of the IHFA Regulatory Agreement. Owners are expected to fulfill those commitments during both the compliance period, and the entire extended use period.

Such commitments often include:

- Targeting households with lower income levels than the IRS minimum set-aside requirements.
- Restricting unit rent levels.
- Providing amenities and supportive services.
- Extending affordability periods.
- Reducing developer and contractor fees.
- Developing housing that serves populations with special needs such as persons with physical or developmental disabilities, the homeless or the elderly.

IHFA will monitor compliance with any such commitments contained within the Regulatory Agreements. Owner/Agents should ensure that they are meeting all agreed-upon commitments. If not, noncompliance will be noted in the IHFA audit report.

### **Tax Credit Allocation Period and Initial Credit Period**

Once a development's tax credit allocation has been finalized, the tax credits can be claimed annually on a building-by-building basis over a 10- year period. This 10- year period begins during either the taxable year in which the building is placed-in-service or at the election of the Owner, the succeeding taxable year. The development's Owner entity must elect the initial credit period on each building's IRS Form 8609. Once made, this election is irrevocable.

It is important for Management Agents to know when the credits were or will be claimed for the first time because the compliance period starts the first year the credits are claimed. No credits may be taken if the building does not comply with IRS regulations for meeting initial compliance.

### **Tax Credit Compliance Period**

Section 42 regulations require an initial 15 years of continuous compliance – also known as the “federal compliance period.” However, with the advent of extended-use periods, Owner entities are required to extend the low-income housing commitment period by a minimum of an additional 15 years beyond the initial 15-year federal compliance period.

State allocating agencies have been granted the authority to impose additional requirements over and above the federal standards to better address local housing needs, including extending the period of affordability. IHFA grants preference points to developments that extend the period of affordability beyond the 30- year commitment. Therefore, Owner entities are committed to a longer period of compliance than the original compliance period.

A complicating factor exists when tax credit developments are coupled with other subsidy programs such as HOME. There are times when conflicts between programs may arise. Care must be exercised to ensure that the most restrictive of these competing program requirements is met.



### **Placed-In-Service Date**

All auditing and compliance is on a building-by-building basis. The date an Owner can formally qualify tax credit units and initiate the start of the compliance period for a building is called the “Placed-in-Service Date”. This date is the day the Owner/Agent receives a building’s certificate of occupancy.

Each building has only one placed-in-service date. It is possible to have the same or different dates for different buildings in a tax credit development. For New Construction, the placed-in-service date corresponds with the date of the certificate of occupancy. The occupancy date 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 and/or local law.” This is the date when the first unit in a building could be occupied, not when it was occupied.

For acquisition and rehabilitation developments, the Owner entities must select a placed-in-service date, which may be any date within a 24-month period corresponding with the period between the date the building was acquired and the date the rehabilitation work is completed.

All projects must be placed-in-service by the end of the second calendar year from the date of the allocation of Tax Credits. Owners must document the date by completing an IRS form 8609 for each building in the development.

### **IHFA Compliance Monitoring Procedures**

Generally, the IHFA Compliance Department will begin inspection of LIHTC developments within two years of the Placed-in-Service date. As soon as IRS Form (s) 8609 is/are completed and filed, developments will be added to IHFA’s inspection regime. Owner/Agent compliance responsibilities commence shortly after placed-in-service occurs. IHFA may, however, begin inspections of LIHTC developments before the IRS Form 8609 forms are completed and filed if IHFA believes that, after performing a risk analysis, the development requires an immediate inspection. The Risk Analysis Process may include the following:

- Marketing difficulties
- First-year rent-up difficulties
- Vacancies due to set asides

### **Owner/Agent issues**

Once the lease up period is completed, Owner/Agents must provide IHFA with an IHFA Occupancy Report **Exhibit 1** that includes all first year household information. Owner/Agents have sixty (60) days from the completion of lease-up in which to submit the required occupancy report.

The Compliance Department performs an on-site inspection and file audit at least once every three years.. If a development has HOME, Bond or ICRC funding, compliance reviews will typically be conducted on an annual basis depending on the individual

Regulatory Agreement. Generally, Owner/Agents will be notified of the site visit within 30-days. The time frame may be less under certain circumstances. IHFA will make every effort to accommodate emergency situations and re-scheduling requests, but audit dates are not always negotiable due to travel schedules and the added costs associated with last-minute changes to pre-arranged travel. Schedules are tight, and on-site visits must be geographically coordinated in order to mitigate travel costs.

*Note. If IHFA auditors have to conduct additional on-site visits, extra charges may be associated with inspections at the Owner/Agents expense.*

### **IHFA-Required Program Forms**

In an attempt to ease the burden associated with both compliance and oversight, IHFA requires the use of a very limited number of forms. The required forms are found in **Exhibit 1 and 2**. Forms used by Owners Agents must replicate these forms as to both content and format. Deviations from these formats will not be considered acceptable. The following list represents the forms that are considered mandatory:

- Owner’s Certificate of Continuing Program Compliance
- Annual Occupancy Report
- Tenant Income Certification (TIC)—An original certificate, signed by all adult members of the household and Owner/Agents, which demonstrates household members are qualified to live in the low-income unit
- Employment Verification
- Annual Recertification Packet (AR) with Tenant Income Certification (TIC).
- HOME Addendum

An additional array of forms is included in **Exhibit 2**. These forms are included for Owner/Agent use on a recommended basis only. They are not required, but IHFA recommends that their use be strongly considered since they will facilitate the gathering of information necessary for compliance. The following is a list of recommended forms for Owner/Agent use:

- Eligibility Verifications
- Unearned Income/Assets Verifications
- PHA Statement of Income –Qualification of Tenant/Applicant

### **IHFA Audit/Inspection Procedures**

Following are the basic procedures IHFA will adhere to when planning and conducting LIHTC compliance monitoring reviews:

- Contact the Owner/Agent via notification letter, and request pre-audit documentation such as occupancy reports. Documentation will be requested to be sent no later than ten (10) days prior to date of inspection.
- Only original tenant file documentation will be reviewed. File reviews will be conducted at the physical address of the development.

- On-site visitations include an audit and inspection of at least 20% of tenant files and occupied units, all common areas and vacant units if appropriate.
- Only if findings/issues are determined to exist, a formalized Compliance Report will be generated and sent to the Owner/Agent within 30-days of the on-site review. Owner/Agents will have 30-days to respond. If owner/agents are late with a response without an explanation or an approved extension, they will be in noncompliance. A formal ten (10) day notice will be sent giving the Owner/Agent ten days to respond. If no response or an inadequate response ensues, an IRS Form 8823 will be filed reflecting noncompliance.
- If the audit resulted in no findings or comments, Owner/Agents will receive a letter from the IHFA Compliance Department that results in no response necessary.
- IHFA will approve extensions if Owner/Agents need the time to rectify findings and issues on-site. Owner/Agents must ask for an extension in writing and must abide by the deadlines they set for themselves or those set by IHFA.
- Owner/Agent responses to audits will then be reviewed and appropriate notifications will be sent informing them of their compliance status. Auditors may need additional documentation for a particular finding or the Owner/Agent response may be sufficient to close a review.

Auditors at this stage will send appropriate correspondence to Owner/Agents. If an Owner has remedied an IRS reportable finding, an IRS Form 8823 will be filed reflecting the fact that issues of non-compliance have been corrected. If an Owner has not adequately addressed or resolved a reportable finding, a formal ten day (10) day notice will be sent giving the Owner/Agent 10 days to respond. If no response or an inadequate response ensues, an IRS Form 8823 will be filed reflecting a continuing noncompliance condition. IHFA will also send the Owner a copy of the IRS Form(s) 8823 concurrent to filing the form(s) with the IRS.

## **IHFA Review, Inspection, and Reporting Standards**

IHFA auditors perform both file reviews and on-site inspections. Both monitoring tasks include specific documentation and condition standards that must be followed in order for developments to be successful in their compliance efforts. IHFA auditors will request occupancy reports and other supporting documentation such as resident selection plans and affirmative housing marketing plans if applicable. As soon as the occupancy report is received from the Owner/Agent, auditors determine which of the units to inspect, and which files to review by selecting a sample. Auditors make every effort where possible to choose from those of the development's units that were not inspected in the previous year. Program guidelines require that a 20% sampling of files and units be used as the foundation for the audit.

### **The Tenant File Review Procedures**

As indicated earlier, in each case, IHFA requires review of original documentation only. The following original documents will form the basis for a file review:

- Tenant Rental Application
- Tenant Lease and Addendums, if applicable
- Tenant Income and Asset Disclosure
- Tenant Income Certifications (TIC)
- Third-party verifications of income and unearned income
- Under \$5,000 Asset Certification\*
- Document action supporting tenant eligibility, i.e. credit, criminal checks.
- Move-in Unit Inspection Report

\*All assets must be verified for HOME/Section 8 and RD units. The \$5,000 limitation applies only to tax credit files.

An event of non compliance may occur due to the following issues. (The listing is not all inclusive)

- Tenants are not qualified under the LIHTC program.
- Qualified low-income tenants are charged improper or unrestricted rents.
- Owner/Agents failed to maintain properly executed certification or failed to re-certify tenants prior to move-in anniversary date.
- Owner/Agent failed to perform a recertification prior to the IHFA correspondence date of audit, otherwise known as the "Bright Line" date. Please see Page 3-2 in the Revised 8823 Guide for more information.
- Owner/Agents failed to document tenant income eligibility and identify full-time students.

- Tenant records such as applications, leases, third-party verifications and TICs are insufficient, inaccurate and/or incomplete; or they show evidence of additional deficiencies that would impair their validity.
- Owner/Agent lease does not have minimum LIHTC standards such as a 6-month lease term or the lease is not properly executed.
- Owner/Agents fail to gather and implement utility allowance changes annually or within ninety (90) days of a changing the utility allowance consumption rate.
- Rents, including other regularly assessed charges, exceed annual published limits.
- Owner/Agents failed to comply with IRS record-keeping requirements.
- Other issues that evidence a departure from LIHTC program rules or requirements.

### **Physical Inspection Procedures**

Owner/Agents are not only responsible for ensuring tenant files are maintained in a compliant fashion, but that the development is structurally sound, functionally adequate, in good repair, and free of health and safety hazards.

IHFA compliance auditors require Owner/Agents or their designated representatives to accompany them on all physical inspections. If the auditor is unable to gain access to a unit during a physical inspection, a replacement unit may be chosen at the discretion of the auditor and an IRS Reportable Finding may ensue.

Pursuant to program guidelines, IHFA utilizes the *Uniform Physical Condition Standards (UPCS)/REAC Standards* promulgated by HUD to assess the physical condition of the LIHTC developments. For specific physical inspection information, please refer to HUD's UPCS/REAC protocol, found at 24 CFR 5.703. That guidance, as well as additional REAC documents and guidance, can be accessed at [www.hud.gov/offices/reac](http://www.hud.gov/offices/reac). The UPCS/REAC standards require developments to be in "decent, safe and sanitary condition and in good repair" and require IHFA to inspect the following major areas:

- **Site:** Site components include, but are not limited to, fencing, retaining walls, grounds, lighting, project signs, parking lots and driveways, play areas and equipment, refuse disposal equipment, roads, storm drainage, and walkways. All items must be free of health and safety hazards and in good repair / working order, as applicable.
- **Building Exterior:** Each building on-site must be structurally sound, secure, habitable, and in good repair. Each building's door, fire escapes, foundations, lighting, roofs, walls and windows must be free of health and safety hazards, operable and in good repair / working order, as applicable.
- **Building Systems:** Each building's domestic water, electric systems, elevators, emergency power, fire protection, HVAC, and sanitary system must be free from health and safety hazards, functionally adequate, operable and in good repair / working order, as applicable.

- Dwelling Units: Each dwelling unit within a building must be structurally sound, habitable and in good repair. The unit must be free from health and safety hazards, functionally adequate, operable and in good repair / working order, as applicable. This includes all areas and aspects of the unit, i.e., bathroom call for aid and fixtures, ceilings, doors, electrical systems, floors, hot water heaters, HVAC, kitchen, lighting, outlet/switches, patio/porch/balcony, smoke detectors, stairs, walls and windows.  
  
Each living unit also must include at least one (1) battery operated or hard-wired smoke detector in proper working condition on each level of the unit.
- Common Areas: Common areas also must be structurally sound, secure and functionally adequate for the purposes intended. The basement, garage/carport, restrooms, closets, utility, mechanical, community rooms, day care, halls and corridors, stairs, kitchens, laundry rooms, office, porch/patio/balcony and trash collection areas, if applicable, must be free from health and safety hazards, operable and in good repair / working order, as applicable.
- Health and Safety Concerns: All areas and components of the development must be free of health and safety hazards. These areas include, but are not limited to, air quality, electrical hazards, elevators, emergency/fire exits, flammable materials, garbage and debris, handrail hazards, infestation and lead based paint.

Please refer to the “Dictionary of Definitions” within the REAC program documentation for further information and examples. According to the REAC protocol, violations in each of the inspection areas listed above may be present at any of three levels, one being the least severe, and three being the most severe. According to the Revised 8823 Guide all violation levels are considered to be IRS Reportable items. Please see Page 6-4 of the Revised 8823 Guide for further explanation of this standard.

### **Compliance Concerns Related to Physical Condition**

A unit, building, or development may be in non compliance and an IRS Form 8823 will be filed due to the following:

- The Owner/Agent incorrectly certifies that the buildings and units in the tax credit development were suitable for occupancy. For example, if an Owner/Agent certifies that a unit has been turned and is rent ready for a new tenant, but an inspection discovers the unit is still under rehabilitation, the unit is considered in non compliance and will be noted as an IRS Reportable finding on the report. Per the Revised 8823 Guide, all vacant tax credit units that are not suitable for occupancy are in non compliance and are subject to an IRS Form 8823 submission. Accordingly, vacant units are subject to inspection in order to ensure compliance.
- The development evidenced conditions that failed to meet UPCS standards. For example, the development may have findings that include parking lot potholes and exterior paint peeling problems.

- Owner/Agent fails to comply with the requirements of the REAC protocol at any time. Noncompliance in this case may mean the Owner/Agent is not living up to their agreement to maintain affordable housing in a decent, safe and sanitary state.
- Non compliance of REAC protocol will be identified and noted in a compliance report during a development's extended use agreement.
- Casualty loss to a unit, building or any part thereof at any time during the compliance period may lead to recapture of credits.

### **Exit Interview**

Shortly after the physical inspection, IHFA auditors will perform an exit interview to discuss all inspection findings and/or comments. This meeting provides Owner/Agents with the opportunity to ask questions, confirm observations, and/or refute findings. Auditors will ask development staff to sign an Exit Interview Acknowledgement to ensure Owner/Agents feel their concerns have been addressed.

### **Audit Reports / Responses**

IHFA will provide Owner/Agents with a written report of findings within 30 days of the date a review is conducted, and requires that the Owner/Agent provide an adequate response within thirty (30) days of the date of the report. The report/response phase of the examination process provides the Owner/Agent with an opportunity to review the issues, and take corrective actions as necessary and appropriate. This period also provides Owner/Agents with an opportunity to refute the findings that, upon further investigation, may be without merit. If the Owner's documentation clearly refutes a report finding, the noted condition will not be reported on IRS Form 8823.

Once the report/response phase is completed, IHFA will file IRS Form 8823 forms as required. The IRS Form 8823 will reflect the status of any reportable conditions of non compliance noted during the review. A development is back in compliance when reportable/reported findings are corrected. Owner/Agents must confirm all IRS reportable findings have been corrected by supplying IHFA with works orders, invoices or other pertinent documentation with their response to the review. IHFA, on occasion, may determine that visual inspection is needed to determine the Owner/Agent is back in compliance. If so, IHFA will notify the Owner/Agent, and will schedule a follow-up visit. IHFA reserves the right to bill Owner/Agent for the costs to travel to developments to perform additional audits due to egregious non compliance.

IHFA's reports may also include observation or recommendation items in the report. These items are for Owner/Agent information only, and are not required to be addressed via the response process. Observation and Recommended items may not need a response; however they do represent issues IHFA believes Owners should consider for possible corrective action, or for procedural change.

### **IHFA Compliance Auditing Protocols—Extended-Use Period**

IHFA has established a separate monitoring protocol that will be followed for developments that have completed their federal compliance period (the first 15 years),

and are entering the required extended use period. During the extended use period, audits will be conducted as follows:

- Frequency: Monitoring will occur at three (3) year intervals, or more frequently as IHFA deems necessary.
- Scope: The number of tenant files and living units will be reduced. Ten percent (10%) of the files and units will be audited.
- Monitoring Fees: Monitoring fees will be reduced to two-thirds (2/3) of the standard annual fees that are payable during the federal compliance period (the initial 15 year affordability period).
- Monitoring Protocol: All other auditing protocols such as scheduling, notice, file reviews, reporting, etc... will remain the same.

### **Monitoring Provisions**

- The Next Available Unit Rule is not applicable and no longer enforced during the extended use period,
- Because the NAUR is not in effect, the 140% Rule is no longer applicable as well.
- Annual Recertifications is not applicable in mixed-use developments after the first year recertification. All households may self-certify the third year of residency.

### **Penalties under Extended Use**

- IHFA may find the Development in default under the Regulatory Agreement.
- If agents have a non-compliant history of violations with previous developments currently under LIHTC Regulatory Agreements, IHFA may prevent Agents from participating in future Tax Credit/HOME allocation rounds.

## **Ongoing Compliance Activities**

### **Owner Reporting**

Owners are responsible for completing a “Certificate of Continuing Program Compliance” each year. IHFA normally sends out a notice relative to this requirement during the month of January. The Certificate is due to the IHFA Compliance office by February 28<sup>th</sup> of each year. For example, the report for 2009 is due February 28, 2010.

Owners are also responsible for completing and submitting an Annual Occupancy Report. The report, which must be submitted with the “Certificate of Continuing Compliance”, must show all tenants that have lived in the development in the last year. Compliance auditors will use the year-end report to ensure compliance with the next available unit rule and reasonable vacancy time-periods. Both reports can be found at **Exhibit 1** in the Appendix of this manual.



## **Monitoring Fees**

In order to support the monitoring efforts of designated Compliance Monitoring Agencies, Tax Credit developments are required to pay a modest monitoring fee on a per-door basis each year. To account for changes in operating costs, these fees are indexed in Idaho. After the initial base monitoring fee of \$30.00 per living unit was established, IHFA utilized the annual change in the Consumer Price Index (CPI) published each January to annually adjust the monitoring fees. Thus, fees will only be increased at a rate that is consistent with the overall rise in prices in the general economy.

Additional fees may be required in specific circumstances. If non-compliance is discovered and IHFA determines that an additional or out-of-pattern follow-up review is necessary, an additional charge based on the current monitoring fee then in effect will be charged for every file and / or unit inspected. For example, if IHFA auditors have to perform a follow-up 100% file review on a 40 unit development, and the current year's monitoring fee was \$31, the additional fees due and payable as a result of the review would be calculated as follows: 40 files x \$31.00 = \$1,240.00.

Monitoring fee invoices will be sent to Owners during the Month of January each year. Monitoring fees are due February 28<sup>th</sup> of each year.

## **Conclusion**

It is vitally important Owners/Agents remember that the responsibility for maintaining compliance in an LIHTC development rests solely with the Owner. Due to the complexity of the program, and the risks and exposures involved, IHFA encourages the Owner to ensure that management and staff involved in both initial leasing activities, and in on-going operations are adequately trained and versed in the tax credit program so that compliance can be maintained. IHFA is available to provide technical assistance wherever needed, but, as the designated Compliance Monitoring Agency, bears no responsibility for on-going compliance at LIHTC developments. To reiterate, IHFA is responsible for monitoring compliance on an on-going basis and for reporting on conditions of non compliance – Owners are responsible for maintaining compliance with all applicable program requirements.

Owner/Agents are invited to contact IHFA Compliance Staff in order to discuss LIHTC questions and concerns in order to arrive at acceptable solutions. We can be reached at (208) 331-4707 and [compliance@ihfa.org](mailto:compliance@ihfa.org).