RECOVERY HOUSING BEST PRACTICES

HOW TO USE LOW INCOME HOUSING TAX CREDITS

HELPFUL TIPS FROM THE FLETCHER GROUP RCOE

Low-Income Housing Tax Credits (LIHTC) is a potential source of construction/renovation funding for larger residential recovery facilities sponsored by well-financed organizations with expertise in project management.

LIHTC subsidizes the acquisition, construction or rehabilitation of affordable rental housing for low- and moderate-income tenants. LIHTC is the nation's largest source of affordable housing financing.

The IRS allocates Low-Income Housing Tax Credits to the states' Housing Finance Agencies (HFA) that make awards on a competitive basis to affordable housing developers (including nonprofits).

The award of LIHTC is made through a process defined in each state's Qualified Assistance Plan (QAP). HFAs must comply with the Department of Housing and Urban Development's affordability standards but can include additional requirements.

In 2024, it is expected that approximately $113M of LIHTC will be available for the entire nation. Each state will receive an estimated allocation of at least $3,185,000 based on population.

LIHTC has assisted more than three million affordable housing units

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WHAT PROJECTS MAY QUALIFY FOR LIHTC?

Larger Recovery Houses (with more than 30 units of housing - apartments, single-family dwellings, townhouses, or duplexes) that propose to serve low-income populations may qualify for LIHTC through one of the following ways:

- At least 20% of the project’s housing units will be occupied by tenants with incomes at or below 50% of area median income (AMI).
- At least 40% of the housing units will be occupied by tenants with incomes at or below 60% of AMI.
- At least 40% of the housing units will be occupied by tenants whose incomes average 60% or less of AMI, with no units being occupied by tenants with incomes exceeding 80% of AMI.

Rents cannot exceed 30% of income. A LIHTC developer can restrict up to 100% of housing units to tenants with qualifying incomes. Credits are awarded only for the portion of the building occupied by low-income tenants.

The project must comply with income levels and rent limitations during an initial compliance period of at least 15 years. An additional 15 years of required affordability for low-income residents may be stipulated in an “extended use agreement” per each state or other funding source requirements.

ADDITIONAL FUNDING WILL BE NEEDED

LIHTC is not likely to provide enough equity to finance the entire project. Additional sources (for example, grants such as the Community Development Block Grant or the Federal Home Loan Bank Affordable Housing Program) may have to be secured for a debt free project. All of these funding sources come with their own rules and compliance requirements. Smaller projects (fewer than 30 housing units) will likely not be competitive for LIHTC.

Developers (or their syndicators) sell the tax credits to investors. This sale allows the developer to receive equity (funds) to complete the project. Since most of the equity from the sale is not paid until the project is fully occupied, interim financing (such as a construction loan) is often needed. As these transactions may have tax implications and can impact the nonprofit developer’s financial standing, it is important to involve the guidance of an account or consultant who is knowledgeable about LIHTC.

A nonprofit organization must have adequate personnel, finances, and large-scale project management experience to successfully compete for LIHTC. Likewise, the nonprofit must be able to secure a source of guaranteed rental income, for example Section 8, to support the housing program's ongoing operating costs. (More information about nonprofit involvement in LIHTC partnerships is provided on the last page of this document.)

Example of how Equity from LIHTC is Determined

Total Construction Budget (all hard costs such as labor and materials plus soft costs including architecture, engineering, inspections, accounting, permits, taxes and legal fees)	$10,000,000
Total Construction Budget minus ineligible costs (such as land, interest on construction loan, and insurance)	$500,000
"Applicable fraction" (percent of units reserved for low-income tenants)	100%
Resulting “qualified basis” (eligible basis [$9,500,000] multiplied by applicable fraction [of low-income tenants)	$9,500,000
Appropriate Percentages Under Internal Revenue Code Section 42(b)(1) for August 2022 (the % changes periodically, check IRC Section 42(b)(1) for the current rate)	7.75%
Annual Credit Amount (Qualified basis [$9,500,000] multiplied by appropriate percentage [7,75%] = $736,250 multiplied by 10 years	$7,362,500
Tax Credit Factor (Cost per $ of credits sold - this rate varies - .91 is an example)	.91
Total Equity available for the creation of affordable housing (Total Credit Amount multiplied by Tax Credit Factor [selling price of credits])	$ 6,699,875
NOTE: In this example approximately 67% of the project is financed by LIHTC. If this project was located in a Qualified Census Tract (QCT), it could qualify for a High-Cost Adjustment Boost (additional 30%) and LIHTC could cover 87% ($8,709,837) of the project (if credits were sold at .91). Learn more about QTC’s here: https://www.huduser.gov/portal/datasets/qct.html	

RHOAR

RECOVERY
HOPE
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RESILIENCE

LIHTC IN ACTION - Transforming a Rural Dream into a Reality

The Cumberland River RHOAR Center, projected to open in 2023 in Middlesboro, Kentucky (Bell County, population 23,858), will provide living spaces, medication assisted treatment, mental health counseling, and vocational/workforce training for women recovering from substance use disorder.

The RHOAR Center, developed and operated by Cumberland River Behavioral Health, will serve 112 women in 52 living units including efficiencies, shared dorms, and apartments designated for family reunification.

Funding for the $14-million project came from multiple sources. More than $900,000 in Low-Income Housing Tax Credits (which sold for nearly $9M) was awarded by Kentucky Housing Corporation. Additional construction funding was secured from the National Housing Trust Fund ($4M) and the Federal Home Loan Bank of Cincinnati Affordable Housing Program ($1M). Other funding partners include the Bell County Economic Development Foundation and the Ohio Capital Corporation for Housing.

Technical assistance for the RHOAR Center was provided by the Fletcher Group, Inc. with support from HRSA (Health Resources and Services Administration) and the Appalachian Regional Commission.

Cumberland River RHOAR Groundbreaking, October 12, 2022

LIHTC PARTNERSHIPS INVOLVING NON-PROFIT ORGANIZATIONS

A partnership structure (such as a Limited Liability Corporation or Limited Liability Limited Partnership) is formed between the Limited Partner (investor) and the nonprofit organization (General Partner).

The General Partner manages the partnership's day-to-day operations, and the Limited Partner primarily provides an investment to the project and controls terms of the partnership agreement.

Participating in a partnership structure presents benefits and risks to the nonprofit General Partner.

Among the benefits are:

- Substantial amount of equity available for project development. Without this funding the nonprofit may not otherwise be able to develop affordable housing units.
- The nonprofit stands to be paid developer fees, property management and/or other fees
- Opportunity to own the project at the end of the 15-year compliance period

Risks to the nonprofit include:

- Market conditions can influence the pricing that is paid to the nonprofit for the credits
- Changes in economic conditions could impact financial viability and lead to lost credits
- Uncontrollable delays in opening the project as projected could result in the loss of credits
- Credits could also be lost or recaptured if the rate of low-income tenancy changes

IMPORTANT NOTE: Nonprofits must be aware that sizeable upfront costs are required to apply for tax credits. This includes application fees, architecture, market study, environmental reviews, consultants, etc. These costs are paid even if the project is not selected to receive LIHTC.

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