

CHAPTER 1 – OVERVIEW OF THE LIHTC PROGRAM

This Chapter provides a generalized overview of the LIHTC Program. Additional information can be obtained from the MSHDA website at www.michigan.gov/mshda.

Note: Individuals whose primary function involves certifying the eligibility of tenants to reside in LIHTC units may desire to read Chapter 3 first.

Section 1A - LIHTC Overview

Part 100 : What is the Low Income Housing Tax Credit (LIHTC)?

The Low Income Housing Tax Credit (LIHTC) is a dollar for dollar reduction in the tax liability of the owner (or investor) of a qualified low-income housing development for the rehabilitation, acquisition, or construction of low-income rental housing units. In exchange for the tax credit, the owner agrees to rent a percentage (or all) of the units in a development to low income persons and restrict rent amounts.

Part 102 : Creation of the LIHTC Program

In 1986, Congress enacted the Tax Reform Act, creating the Low Income Housing Tax Credit Program (the “LIHTC Program”). The LIHTC Program is authorized and governed by the 1986 Tax Reform Act as amended, and codified as Internal Revenue Section 42 of the Internal Revenue Code (the Code) as amended. In August 1993, Congress passed the Omnibus Budget Reconciliation Act of 1993, which permanently extended the LIHTC program. MSHDA is the designated “housing credit agency” to allocate and administer tax credits for the entire state of Michigan.

For additional information regarding responsibilities, see [Chapter 2](#) (Responsibilities). For additional information regarding LIHTC Program legislation and regulations, see [Part 114](#) (Major Regulations and Legislation Impacting LIHTC Compliance Monitoring).

Part 104 : Overview of the LIHTC Program

The purpose of the LIHTC program is to provide incentives for the investment of private equity capital in the development of affordable rental housing for persons of low and moderate incomes. The equity comes into the project from investors who contribute to the legal entity that owns the project (the “owner”). This entity is typically a limited partnership or a limited liability company, all of which are legal entities that allow the benefit of the tax credits to flow through to the investors. The equity funds are used to pay for part of the project development costs. Investors, in turn, use the credit to lower their federal income tax liability. The LIHTC Program reduces the federal tax liability of pro-

ject owners in exchange for the acquisition, rehabilitation, and/or construction of affordable rental housing units that will remain income and rent restricted for at least 15 years. The amount of tax credit allocated is based on the number of qualified low-income units that meet federal rent and income targeting requirements.

Credit can be claimed on an annual basis for ten (10) years. The equity funds, however, are usually contributed during construction or soon after the completion of the project. The price paid for the credit is determined by the timing of the payments into the project as agreed upon by its investors. The balance of the project costs are paid with conventional mortgage financing, private contributions, or other government sources, such as bond financing, HOME funds, and Rural Housing Services loans.

The trade-off for receiving tax credits is that the owner must agree that the housing units receiving credit will be restricted to low-income households for a specific period of time and that the rents for these units be capped, following a fixed formula. Because a large portion of the cost of the project has been paid from equity, a project is designed so that the restricted rents are sufficient to pay the operational costs and mortgage debt on the property.

Part 106 : **Amount of Credit Available for Michigan**

A low-income housing credit is allowable only if the owner of a qualified building receives a housing credit allocation from the state or local housing credit agency. The aggregate credit authority provided annually to each state for the 2011 calendar year was \$2.15 per resident. The amount per person is indexed for inflation for subsequent years. In certain cases, a state may increase its available credit by using unallocated or returned credit from a prior year, or by using credit authority originally allocated to other states that failed to use all their credit authority (called the National Pool Credit).

The tax credits allocated to LIHTC projects that also receive financing with proceeds of tax-exempt bonds issued subject to the private activity bond volume limits are not made (i.e. subtracted) from the state's aggregate credit authority discussed in the previous paragraph.

For information about the amount of credit available to an individual project, see **Part 128** (The Annual Tax Credit Amount).

Part 108 : **Qualified Allocation Plan**

To receive tax credits, an owner must apply to the state-allocating agency (MSHDA) and be awarded a reservation or an allocation of the state's available credit. Each state's Qualified Allocation Plan (QAP) establishes the guidelines and procedures for the acceptance, scoring, and competitive ranking of applications, as well as the rules and procedures for the administration of the LIHTC Program. The Michigan QAP is developed to be relevant to state housing needs and priorities and is approved by the Governor. Portions of the total credit authority are set aside for special or targeted groups of applicants, such as for non-profit sponsors or projects located in rural areas. MSHDA has its own threshold requirements that must be met to submit an application, and its own limitations on the amount of credit a project or owner may receive, as well as limitations on the amount of fees an owner may include in eligible basis.

The latest version of the Michigan Qualified Allocation Plan is available on MSHDA's website, discussed in [Part 202](#). For more information on Michigan's Qualified Allocation Plan, see [Part 220](#) (Michigan's Qualified Allocation Plan).

Part 110 **The LIHTC Allocation Process**

In Michigan, the allocation process is made through periodic application rounds, with allocation criteria points given for project characteristics, such as project location and the income level or special needs of residents. The highest scoring qualified projects receive reservations of tax credit. Most projects receive an allocation of credit called a Carryover Allocation in the year the application was made, prior to the construction or rehabilitation of the project. For additional information regarding the allocation process, see [Section 1B](#) (LIHTC Allocation Basics, which contains [Parts 118 - 156](#)) and the MSHDA website (discussed in [Part 202](#)).

Part 112 **IRS 8609 (Low-Income Housing Credit Allocation Certification)**

An IRS Form 8609 is issued by MSHDA for each building in the project that is awarded an allocation of tax credits. The form is prepared by MSHDA following completion of the new construction or rehabilitation and submission of all required documentation. It identifies the amount of credit assigned to each building, the eligible basis of each building, and the low-income percentage of each building. It also indicates the date the building was placed in service. (Placed in service dates are discussed further in [Part 134](#).)

Part I of the IRS 8609 form is completed by MSHDA and then sent to the owner when the project is placed in service and all required documentation is received by MSHDA. Part II of the IRS 8609 form must be completed by the owner of the LIHTC project for the first taxable year for which the credit is claimed. Before signing and dating Part II of the form, the owner should make sixteen (16) copies of it, one for each of the tax credit compliance years. A completed copy of Part II must be sent to the LIHTC Compliance Section of MSHDA. The original is sent to the IRS with the owner's personal, partnership, or corporate tax returns in the first taxable year in which the credit is claimed and each year thereafter in the compliance period. MSHDA will not issue an IRS Form 8609 for each year of the credit period.

Part II also discloses certain irrevocable elections, which must be made in the first year of the credit period. These irrevocable elections include the following:

- The election to claim the credits in the year after the building is placed in service;
- The minimum set-aside election;
- Whether to treat the buildings as a multiple building project; and
- The election to not treat a large partnership as the tax payer.

IRS 8609 – Dec. 2008 version – Irrevocable Elections

Part II First-Year Certification—Completed by Building Owners with respect to the First Year of the Credit Period

| | | | |
|----|---|--------------------------------|--------------------------------|
| 7 | Eligible basis of building (see instructions) | 7 | |
| 8a | Original qualified basis of the building at close of first year of credit period | 8a | |
| b | Are you treating this building as part of a multiple building project for purposes of section 42 (see instructions)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 9a | If box 6a or box 6d is checked, do you elect to reduce eligible basis under section 42(i)(2)(B)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| b | For market-rate units above the average quality standards of low-income units in the building, do you elect to reduce eligible basis by disproportionate costs of non-low income units under section 42(d)(3)(B)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 10 | Check the appropriate box for each election: Caution: <i>Once made, the following elections are irrevocable.</i> | | |
| a | Elect to begin credit period the first year after the building is placed in service (section 42(f)(1)) | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| b | Elect not to treat large partnership as taxpayer (section 42(j)(5)) | <input type="checkbox"/> Yes | |
| c | Elect minimum set-aside requirement (section 42(g)) (see instructions) | <input type="checkbox"/> 20-50 | <input type="checkbox"/> 40-60 |
| d | Elect deep rent skewed project (section 142(d)(4)(B)) (see instructions) | <input type="checkbox"/> 15-40 | |

Schedule A of Form 8609 is completed by the tax payer and filed annually with the tax payer’s tax return along with Forms 8609 and 8586 for each year during the 10 year credit period. The schedule discloses increases or decreases in eligible basis, modified credit percentage, additions to qualified basis, and other information as it pertains to a particular year.

Owners should consult with their legal and / or tax advisors for advice on completing and filing the IRS tax forms. MSHDA cannot give legal or tax advice on the filing or completion of tax forms.

A sample, blank copy of the IRS 8609 form is available on the IRS website or on the MSHDA website (discussed in **Part 202**).

Multiple Building Project Election

If the owner checked “Yes” on line 8b of the IRS 8609 form, it has opted to treat the buildings as part of a multiple building project. In this situation, certain LIHTC requirements (such as the minimum set-aside, vacant unit, and unit transfers) can be met on a project-wide basis. If the owner checked “No” on line 8b of the 8609 forms (or if that line was left blank by the owner), it chose to treat each building as a separate project. In this situation, these LIHTC rules must be met on a building basis because each building is treated as a separate project. The impact of the Multiple Building Election is discussed in **Part 804** (Overview of LIHTC Rules).

Part 114 Major Regulations and Legislation Impacting LIHTC Compliance Monitoring

- **IRS Section 42: Low Income Housing Credit, Including Effective Dates and Related Provision**
- **General Explanation of the Tax Reform Act of 1986 (The “Blue Book”)** – A copy of this act can be obtained at www.irs.gov.
- **IRS Regulation 1.42-5 (Tax Credit Compliance Monitoring), as amended** – A link to the compliance monitoring regulations is included on the MSHDA website (see **Part 202**).
- **IRS Regulation 1.42-10 (Utility Allowances)**
- **Various IRS Revenue Rulings, Revenue Procedures, and Notices:**

- IRS Revenue Ruling 90-60, Recapture Bonds
- IRS Revenue Ruling 90-89, Minimum Set-Aside Requirements
- IRS Revenue Ruling 91-38, LIHTC Questions and Answers
- IRS Revenue Ruling 92-61, Treatment of Common Area Unit
- IRS Revenue Ruling 92-79, Extended-Use Commitment
- IRS Revenue Ruling 94-57, Changes in Area Median Gross Income
- IRS Revenue Ruling 95-49, Tenant Right of First Refusal
- IRS Revenue Ruling 94-9, Number of Bedroom Method Election
- IRS Revenue Ruling 98-4, Definition for Residential Rental Property for 142(d)(1)
- IRS Revenue Ruling 2002-65, Eligible Basis Reduced By Federal Grants
- IRS Revenue Ruling 2004-82, Answering 12 Questions About Low-Income Housing Tax credits Under I.R.C. Section 42, July 2004

- IRS Revenue Procedure 94-57, Gross Rent Floor
- IRS Revenue Procedure 94-64 Obtaining a Waiver of Annual Income Recertification
- IRS Revenue Procedure 94-65, Annual Income Certification Requirement

- IRS Revenue Bulletin 2008 – 39, Section 42 Utility Allowance Regulations Update

- IRS Notice 88-80, Determination of Income
- IRS Notice 88-91, Building Identification Number
- IRS Notice 88-116, Placement in Service

- **H.R. 3221 “the Housing and Economic Recovery Act of 2008” (HERA)** was issued on July 23, 2008. It contained new regulations and/or modifications to the following subject areas:
 - Community service facility (sec. 3003 of HERA) – discussed in **Part 872**.
 - Treatment of federal grants (sec. 3002 of HERA) – discussed in **Part 120**.
 - Repeal of bond posting requirement (sec. 3004 of HERA) – discussed in **Part 1016**.
 - Treatment of individuals who previously received foster care assistance (sec. 3004 of HERA) – discussed in **Part 520**.
 - Measurement of area median gross income for certain projects located in certain non-metropolitan areas (sec. 3004 of HERA) – discussed in **Part 410**.
 - Clarification of general public use rule (sec. 3004 of HERA) – discussed in **Part 870**.
 - Treatment of basic housing allowances for purposes of income eligibility rules (sec. 3005 of HERA and sec. 42 of the Code) – discussed in **Part 394**.
 - Coordination of certain rules applicable to the low-income housing credit and qualified residential rental project exempt facility bonds (sec. 3008 of HERA and sec. 142 of the Code)
 - Next available unit rule – discussed in **Part 806**.
 - Students – discussed in **Part 508**.
 - Single-room occupancy units – discussed in **Part 868**.
 - Hold harmless for reductions in area median gross income (sec. 3009 of HERA and sec. 42 of the Code) – discussed in **Part 408**.
 - Exception from the annual recertification requirement for projects which are entirely low-income use (sec. 3010 of HERA and sec. 142 of the Code) – discussed in **Part 362**.

- **American Recovery and Reinvestment Act of 2009 (ARRA)**
 - Tax Credit Assistance Program (TCAP) – discussed in **Chapter 11**.
 - Section 1602 Program – discussed in **Chapter 11**.

- **HUD Handbook 4350.3 (Section 8 Guidelines)** – A link to the HUD Handbook 4350.3 is included on the MSHDA website. A copy of the entire handbook and other HUD regulations can be obtained at www.hud.gov or www.huduser.org.

For more information about some of the federal and state laws that impact LIHTC compliance, see **Part 566** (Housing Laws).

Part 116 **Regulations for Various Tax Credit Years**

IRS regulations differ depending on when a development was allocated credit. In some cases, the change in regulations brought forth by a technical correction is minor; in others, it is substantial. It is the credit year that determines which regulations apply, not the year the development is placed in service. Management must not only be aware of the differences in regulations but must also clearly understand which rule governs each particular building and/or development. Currently, there are five specific tax credit regulation periods as follows:

1. **January 1, 1987 – December 31, 1989.**
 - For buildings allocated credit during this period, rent was based on the number of people living in the unit, and was (is) subject to change as family composition changes. Owners of those developments, however, had a one-time opportunity to opt to change to the methodology used by sending a letter to the Internal Revenue Service requesting a conversion. Verification of the option chosen was provided to the MSHDA.
2. **January 1, 1990 and beyond.**
 - Rent for all buildings allocated after January 1, 1990 is based on the number of bedrooms in a particular unit.
 - The compliance period is increased to 30 years minimum.
3. **1991 and January 1, 1992 – June 30, 1992 and beyond**
 - The Farmers Home Administration Overage Rule (not retroactive) was implemented.
4. **July 1, 1992 and/or August 10, 1993 and beyond**
 - Section 8 voucher (cannot refuse to lease to Section 8 tenants) – retroactive.
 - Two student rule changes were implemented.
 - 1987-1989 developments could convert rental rates from number of persons to number of bedrooms.
5. **July 23, 2008 and beyond**
 - H.R. 3221 “The Housing and Economic Recovery Act of 2008” (HERA) was issued. See **Part 114** for information about HERA.

Section 1B - LIHTC Allocation Basics

The following section highlights some of the statutory and regulatory provisions directly affecting project compliance. The following is not meant as an exhaustive listing of compliance regulations and presents only a generalized description of the topics. Owners / managers of LIHTC projects should contact an accountant, attorney, or other professional with expertise in LIHTC program regulations for detailed description of these topics as they apply to their specific project.

Part 118 : Eligible Basis

Eligible basis is tied to the credits that can be claimed. The eligible basis is assigned to a building at the time of final credit allocation (issuance of 8609). It consists of the cost of new construction; the cost of rehabilitation and / or the cost of acquisition of buildings to be converted to low-income housing. It equals all eligible areas of the project inclusive of LIHTC units, common areas, hallways, elevators, doors, windows, rooftops, parking lots, management offices, etc. Only the adjusted basis of the depreciable property may be included in the eligible basis. The cost of land, which is non-depreciable, is not included in adjusted basis. The Michigan Qualified Allocation (discussed in [Part 108](#)) provides additional information about eligible basis, including a list of additional exclusions.

Eligible basis does not include commercial space. Projects in which only a portion of the buildings are used for residential purposes and in which part is commercial space (or other non-eligible space, such as congregate care, dormitory, etc.) are termed “mixed-use” projects. See [Part 878](#) (Commercial Space) for more information about mixed-use projects and commercial space.

Some of the special provisions for determining eligible basis under Section 42(d) are:

- The cost of tenant facilities (e.g. parking, garages, and swimming pools) may be included in eligible basis if there is no separate charge for use of the facilities, and they are made available on a comparable basis to all tenants in the developments;
- Eligible basis is reduced by federal grants, residential rental units that are above the average quality standard of the low-income units, any historic rehabilitation credits, and nonresidential rental property.
- The eligible basis, as of the end of the first year of the credit period, is reported to the IRS on Part II of the form 8609 and does not change from year to year.

For related discussions, see [Part 126](#) (Qualified Basis), [Section 8F](#) (Common Space – Residential and Non-residential), and [Part 432](#) (Additional Fees and Charges in LIHTC Projects).

Part 120 : Federal Grants

The treatment of federal grants received by LIHTC projects after the start of the compliance period differs depending on when the project was placed in service. This Part applies to federally-funded grants only. No reduction in basis is required for private grants or grants from state or local governments.

A. Projects that were placed in service before July 23, 2008

Under IRC §42(d)(5)(A), the eligible basis is reduced if a federal grant is made to fund the cost or operation of a building. This includes federal grants obtained during the allocation process and those obtained or received by the project at any time during the 15 year Compliance Period. A building is out of compliance as of the date the federal grant is made if the eligible basis is not reduced.

Eligible Basis is not reduced if the proceeds of a federal grant are used as a rental assistance payment under section 8 of the United States Housing Act of 1937 or a comparable rental assistance program. Under Revenue Ruling 2002-65, rental assistance payments made to a building owner on behalf or in respect of a tenant under the Rental Supplement Payment program (12 U.S.C. §170) or the Rental Assistance Payments program (12 U.S.C. §1715z-1(f)(2)) are not grants made with respect to a building or its operation under IRC §42(d)(5). Thus, proceeds from these programs do not require a reduction in eligible basis.

All federal grants received, including those to be used as project-based rental assistance, must be reported to the Authority or the project will be deemed to be in noncompliance. For additional information, see **Part 704** (Owner Certification of Continuing Compliance).

For additional information about noncompliance, see **Chapter 10** (Noncompliance).

B. Projects that were placed in service on or after July 23, 2008

H.R. 3221 (which is discussed in **Part 114**) clarified the basis reduction rule to apply to federally-funded grants received before the compliance period. It also provides that no basis reduction is required for federally-funded grants to enable the property to be rented to low-income tenants received during the compliance period if those grants do not otherwise increase the taxpayer's eligible basis in the building.

The provision also directed that section 1.42-16(b) of the Treasury regulations be modified to provide that none of the following shall be considered a grant with respect to a building or its operation for purposes of IRC section 42(d)(5)(A):

- (1) rental assistance under section 521 of the Housing Act of 1949 (42 U.S.C. 1490a);
- (2) assistance under section 538(f)(5) of the Housing Act of 1949 (42 U.S.C. 1490p-2(f)(5));
- (3) interest reduction payments under section 236 of the National Housing Act (12 U.S.C. 1715z-1);
- (4) rental assistance under section 202 of the Housing Act of 1959 (12 U.S.C. 1701q);
- (5) rental assistance under section 811 of the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. 8013);
- (6) modernization, operating, and rental assistance pursuant to section 202 of the Native American Housing Assistance and Self-Determination Act of 1996 (25 U.S.C. 4132);
- (7) assistance under title IV of the Stewart B. McKinney Homeless Assistance Act (42 U.S.C. 11361 et seq.);
- (8) tenant-based rental assistance under section 212 of the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. 12742);
- (9) assistance under the AIDS Housing Opportunity Act (42 U.S.C. 12901 et seq.);
- (10) per diem payments under section 2012 of title 38, United States Code;

- (11) rent supplements under section 101 of the Housing and Urban Development Act of 1965 (12 U.S.C. 1701s);
- (12) assistance under section 542 of the Housing Act of 1949 (42 U.S.C. 1490r);
- (13) any other ongoing payment used to enable the property to be rented to low-income tenants; and
- (14) No basis reduction is required for loans (regardless of interest rate) made to owners of qualified low-income housing projects from the proceeds of federally-funded grants.

Part 122 **Minimum Set-Aside**

IRS Revenue Ruling 90-89

Federal regulations mandate that an owner of a LIHTC project maintain at least the minimum required number of LIHTC units in order for any building in the project to be eligible to claim tax credits. The minimum set-aside, also referred to as the “project set-aside” is the minimum percentage of units an owner commits to reserving for tax credit eligible households paying a restricted rent. By the time credit is allocated, the owner has selected one of the following two minimum set-aside elections on a project basis:

- A. At least 20% of available rental units must be rented to households with incomes not exceeding 50% of area median income adjusted for family size
- or
- B. At least 40% of available rental units must be rented to households with incomes not exceeding 60% of area median income adjusted for family size.

Two examples are as follows:

Michigan Villas is a 75-unit project. If the owner elects the 20% @ 50% minimum set-aside, then at least 15 of the 75 units must be occupied by persons at 50% of median or below.

Great Lakes Apartments is a 75-unit project. If the owner elects the 40% @ 60% set-aside, a minimum of 30 of the 75 units must be occupied by persons at 60% of AMGI (Area Median Gross Income) or below.

Other pertinent information regarding the minimum set-aside is as follows:

- The minimum set-aside must be met on a project-wide basis (26 CRF Part 1, Public Comment). The multiple building project election (discussed in **Part 112** and below) is important in this, determining whether each building is a separate project or if multiple buildings comprise one single project.
- Once the owner has committed to a set-aside (i.e. 20% @ 50% or 40% @ 60%), it is irrevocable. The minimum set-aside is selected at the time of LIHTC allocation and is designated in Part II of the IRS 8609.
- Multiple building project election – If the owner checked “Yes” on line 8b of the IRS 8609 form, it has opted to treat the buildings as part of a multiple building project. In this situation, the minimum set-aside must be met on a project-wide basis. If the owner checked “No” on line 8b of the 8609 forms, it chose to treat each building as a separate project. In

this situation, the minimum set-aside must be met on a building basis because each building is treated as a separate project.

- Minimum set-aside deadline – For projects receiving credits in 1991 and later, the minimum set-aside must be met by December 31 of the year the project is placed in service, if credits are to be claimed for that year. If the start of the credit period is deferred until the second year, the minimum set-aside must be met by December 31 of the second year. Once the minimum set-aside is met, it must be maintained for the entire compliance and extended use period.
- An owner cannot take any tax credits until and unless the property meets the set-aside requirement. For more information on claiming the LIHTC, see [Parts 138, 140, and 142](#) (First Year of the Credit Period) and [Part 146](#) (Claiming the LIHTC Credit in Years Two through Ten).
- The minimum election of 40% @ 60% or 20% @ 50% AMGI affects all low-income units within a project. If the project falls below the minimum set-aside, it is no longer considered a qualified project and is no longer eligible for credit. In addition, there is a possibility of recapture of credit claimed in earlier years, as well as other penalties. Projects that elect the 20% @ 50% minimum set-aside must maintain all LIHTC units at 50% AMGI or lower and are not permitted to claim credits for units that exceed 50% AMGI as LIHTC units. Units at 60% AMGI do not qualify as LIHTC units in projects that elect the 20% @ 50% set-aside.
- The minimum set-aside is always calculated as a percentage of units. It is never based on a percentage of square feet at the property.
- The minimum set-aside is referred to by several different names / terminology. The minimum set-aside election is sometimes called the 40/60 or 20/50 election or test. It is also known as the project set-aside.
- Since tax credits are only available for project costs associated with the low-income units and not for market-rate units, some owners elect to maintain more than the minimum required number of units in the project as low-income. In other words, some projects elect an applicable fraction of greater than the 20% or 40% minimum requirement. See [Part 124](#) (Applicable Fraction) for a discussion of the applicable fraction.

Part 124 : Applicable Fraction

IRC Sec. 42(c)(B), (C) and (D)

The applicable fraction represents the portion (percentage) of the building for which tax credits will be claimed. The applicable fraction is the lesser of the total number of tax credit units divided by the total number of residential units in the project or the total square footage of tax credit units divided by the square footage of total units. For example,

A building in Michigan Villas has 36 residential units, consisting of 25 one-bedroom units and 11 two-bedroom units. Each one-bedroom unit contains 600 square feet and each two-bedroom unit contains 800 square feet. The total square footage of the building is 23,800. Of the 36 residential units, 15 units (consisting of 10 one-bedroom and 5 two-bedroom

units) are reserved for low income households. The percentage of units reserved for low income persons is 41.67% (15 / 36). The percentage of square feet reserved for low income is 42.02% (10,000 / 23,800). The applicable fraction of the building is therefore 41.67%, which is the lesser of the low income unit percentage versus the square footage percentage.

Other pertinent information regarding the applicable fraction is as follows:

- The term “unit fraction” is sometimes used when discussing the ratio of low-income units to total housing units in a building. The term “floor space fraction” is sometimes used when discussing the ratio of the square footage of the low-income units to the square footage of all residential housing units. The applicable fraction of a building is the lesser of the unit fraction or the floor space fraction.
- The applicable fraction must be met on a building-by-building basis (regardless of whether the multiple building project election discussed in [Part 112](#) was made or not). Different buildings within a project can sometimes have different applicable fractions, as determined by the IRS 8609 forms completed by MSHDA and the owner.
- Projects in which all of the units are reserved for low-income persons have a 100% applicable fraction. Projects in which only a portion of the units are reserved for low-income persons (and thus have an applicable fraction of less than 100%) are called “mixed income” projects. See [Part 802](#) (Mixed Income Projects) for more information on mixed income projects. See [Part 832](#) (Overview of Deeper Targeting / Agency Covenants) for a related topic.
- Units that have never been occupied can not be included in the numerator (low-income units), but must be included in the denominator (total units). For additional information, see [Section 820](#) (Overview of Vacant Unit Rule).
- The Next Available Unit Rule potentially impacts the applicable fraction, as discussed in [Part 818](#) (NAUR - Transfers).
- Common area residential units (discussed in [Part 858](#)) and common space (discussed in [Part 862](#)) potentially impact the applicable fraction.

Part 126 **Qualified Basis**

Eligible basis equals all eligible areas of the project inclusive of LIHTC units, common areas, hallways, elevators, doors, windows, rooftops, parking lots, management offices, etc. The **qualified basis** of a qualified low-income building for any taxable year is an amount equal to the applicable fraction (determined as of the close of the taxable year) of the eligible basis of each building.

For a related discussion, see [Part 118](#) (Eligible Basis).

Part 128 **The Annual Tax Credit Amount**

The low-income housing tax credit may be claimed over a 10-year period by owners of certain residential rental property for the cost of rental housing occupied by tenants having incomes and rents below specified levels. The amount of the credit for any taxable year in the 10 year period is the applicable percentage of the qualified basis of each qualified low-income building. (Applicable Credit Percentage describes the technical term for the credit percentage that a qualified low-income housing is eligible for, as discussed in [Part 130](#).) The qualified basis of any qualified low-income building for any taxable year equals the applicable fraction of the eligible basis of the building. In other words, the maximum amount of credit that can be allocated is calculated by multiplying the “eligible basis” by an “applicable fraction” to ascertain the “qualified basis” and then multiplying by the “applicable credit percentage.”

QUALIFIED BASIS = Eligible Basis X Applicable Project Fraction

ANNUAL TAX CREDIT \$\$\$ AMOUNT = Qualified Basis X Applicable Credit Percentage

The applicable credit percentage is determined based on a formula using federal interest rates and present value annuity factors. The applicable credit percentage should not be confused with the applicable fraction. In general*, the annual tax credit dollar amount can be claimed each year for ten years**. For additional information, see [Part 130](#) (Applicable Credit Percentage) and [Part 136](#) (Credit Period).

*Important note: The amount of credit that can be claimed each year may be impacted by other factors as well, including occupancy levels, the placed in service date for each building, and non-compliance with LIHTC regulations such as income limits, rent restrictions, physical condition standards, student status, etc. that are discussed throughout this Compliance Manual.

**The annual tax credit amount and number of years for which credit can be claimed for some LIHTC projects may be impacted by the Two-Thirds (2/3) Rule, which is discussed in [Part 150](#).

Part 130 **Applicable Credit Percentage**

The low-income housing credit may be claimed over a 10-year credit period after each low-income building is placed in service. The amount of the credit for any taxable year in the credit period is the applicable percentage of the qualified basis of each qualified low-income building.

The credit percentage for a low-income building is set for the earlier of:

- (1) the month the building is placed in service; or
- (2) at the election of the taxpayer, (a) the month the taxpayer and the housing credit agency enter into a binding agreement with respect to such building for a credit allocation, or (b) in the case of a tax-exempt bond-financed project for which no credit allocation is required, the month in which the tax-exempt bonds are issued.

These credit percentages (used for the 70-percent credit and 30-percent credit, discussed below) are adjusted monthly by the IRS on a discounted after-tax basis (assuming a 28-percent tax rate) based on the average of the Applicable Federal Rates for mid-term and long-term obligations for the month the building is placed in service. The discounting formula assumes that each credit is

received on the last day of each year and that the present value is computed on the last day of the first year. In a project consisting of two or more buildings placed in service in different months, a separate credit percentage may apply to each building.

A. 4% Annual Credit (the 30% Present Value Credit)

The approximate applicable percentage used to calculate the annual amount of tax credits given for any of the following:

- (1) the cost of a new building with a federal subsidy;
- (2) the cost of substantial rehabilitation built with a federal subsidy; or
- (3) the cost of buying an existing building for which substantial rehabilitation expenditures also are incurred with a federal subsidy.

B. 9% Annual Credit (the 70% Present Value Credit)

The approximate applicable percentage used to calculate the annual amount of tax credits given for either of the following:

- (1) the cost of a new building built without federal subsidy; or
- (2) the cost of substantial rehabilitation built without federal subsidy.

Also note the following:

- The actual applicable percentage is set each month by the Department of Treasury based on current interest rates. This percentage is then multiplied by the qualified basis to determine the actual annual tax credits. In the case of the 4% Annual Credit, the aggregate amount of tax credits would have a present value of 30% of the qualified basis. In the case of the 9% Annual Credit, the aggregate amount of tax credits would have a present value of 70% of the qualified basis.
- Where existing housing is substantially rehabilitated, the existing housing is eligible for the 30-percent credit and the qualified rehabilitation expenses (if not federally subsidized) are eligible for the 70-percent credit.
- H.R. 3221 contains a provision that provides a temporary applicable percentage of 9-percent for newly constructed non-federally subsidized buildings placed in service after the date of enactment (July 23, 2008) and before December 31, 2013. It also contains a modification to the enhanced credit for buildings in high-cost areas and a modification to the substantial rehabilitation requirement. Detailed discussion of these provisions is beyond the scope of this Compliance Manual.
- H.R. 3221 contains other provisions that impact the LIHTC Program. H.R. 3221 is discussed in [Part 114](#).

Part 132 **Year of the Credit (Allocation Year)**

The year of the credit is the year that the tax credits were allocated for the particular project. For most projects, the year of the credit is the date a carryover allocation was issued and is not necessarily the year the IRS 8609 was prepared or filed. [The credit year is significant because it determines the placed in service deadline (discussed in [Part 134](#)) and the funding requirements under the Qualified Allocation Plan (discussed in [Part 108](#)). The first two digits of the building identification number indicate the year of the credit, as discussed further in [Part 154](#) (Project Numbers).

For a similar topic, see [Chapter 11](#) (Projects Receiving New Second Allocations of Credits).

A building's placed in service (PIS) date determines when an owner can formally qualify tax credit units and initiates the start of compliance monitoring for that building. A newly constructed or rehabbed building has only one PIS date. A building that was both acquired and rehabbed as part of the LIHTC project may have two PIS dates, one for acquisition and one for rehabilitation. Further, it is common that different buildings in the same multi-building project have different PIS dates. All projects must be placed in service no later than the end of the second calendar year following the calendar year in which the allocation of tax credits is made. The PIS date is recorded on IRS form 8609 for each building. Owners must have documentation of the PIS date for every building in the project. IRS Notice 88-116 states that the term "placed in service" has two definitions – one for newly constructed buildings and one for rehabilitation expenditures that are treated as a separate new building.

New Construction - For new construction, the PIS date corresponds with the date of the Certificate of Occupancy. The PIS date for a new or existing building is the date on which the building is ready and available for its specifically assigned function, i.e. the date on which the first unit in the building is certified as being suitable for occupancy in accordance with state or local law. This is the date when the first unit in a building could be occupied, whether or not it was occupied. This date may be different for each building in the project.

Rehabilitation - If the owner incurs substantial rehabilitation expenditures that exceed the amount set forth in IRC 42(e)(3), the owner may treat these expenditures as a separate new building. Under IRC 42(e)(4)(A), rehabilitation expenditures are placed in service at the close of any 24 month period over which such expenditures are aggregated. In other words, for acquisition and rehabilitation projects, the owner selects a PIS date, which may be any date within a 24-month period beginning when the building was acquired and ending when the rehabilitation work is completed. If the rehabilitation is completed and the minimum expenditures requirement is met in less than 24 months, the expenditures may be treated as placed in service at the end of that shorter period.

Acquisition – In general, transactions involving the transfer of a building (i.e. acquisition) creates a PIS date for LIHTC purposes based on the date of the transfer, the date the building is occupied or becomes ready for occupancy, whichever is later.

Transfer - Generally, the transfer of a building creates a new PIS date if, on the date of the transfer, the building is occupied or ready for occupancy.

Certificates of Occupancy / Certificate of Substantial Completion - A copy of the Certificate of Occupancy (for new construction or unoccupied rehabilitation projects) or the Certificate of Substantial Completion (for occupied rehabilitation projects) for each building must be submitted to the Authority's Compliance Monitoring Section within five (5) business days of each document becoming available.

For related discussions, see **Part 652** (Soon to Be Placed in Service Projects) and **Part 654** (Newly Placed in Service Projects.)

Once allocated by the housing credit agency, tax credits can be claimed annually over a ten (10) year period. The ten-year period over which an owner may claim tax credits usually begins by the end of the taxable year that a building is placed in service. Alternatively, an owner may elect to defer the beginning of the ten-year credit period to the next taxable year. Deferring the credit period may be advantageous if the owner is going to incur additional costs or if more time is needed to increase occupancy for purposes of calculating the credit. If the first year the credit is begun at a time during which less than 12 months remains in the calendar year, only a portion of the credit otherwise available for that year may be allowed with the balance being allowed in the 11th year. For example:

XYZ project was allocated tax credits in the amount of \$100,000.00. XYZ project is placed in service on October 1 of the year 2010 and the owner of XYZ elects the year 2010 as the first year of the credit period. Since only three months remains in 2010, the owner can take 25% of the \$100,000.00, or \$25,000, in tax credits for the first year of the credit period. The owner can take the full \$100,000 in credit (provided all compliance requirements are met) for each of the years 2011 through 2019. The owner can then claim the \$75,000 in credits not claimed during year 2010 in year 2020 (i.e. the 11th year).

(Note: For illustration purposes, the example above is generalized and may be oversimplified. The amount of credit available during any year may be impacted by several different factors, including occupancy levels and compliance with LIHTC Program requirements.)

Note: The Credit Period differs from the Compliance Period (discussed in **Part 160**). The Credit Period represents the first 10 years (or, in some situations, 11 years) of the Compliance Period.

Part 138 **First Year of the Credit Period – New Construction Projects**

IRS Revenue Ruling 2004-82

A. Claiming Tax Credits in the Initial Year

The credit is claimed annually for ten years and the credit period begins in the year that the building is placed in service unless the owner elects to defer to the next taxable year. During the first year of the credit period, the low-income occupancy percentage is calculated on a monthly basis. The calculation begins with the first month in which the project was placed in service (or the following year if there is an election to defer the credit period) even though the building may not be occupied during that month. Occupancy for each month is determined on the last day of the month.

An IRS Form 8609 is completed for each building in the development receiving tax credits and is filed with the taxpayer's return for the first year of the credit period. Owners can elect to defer the start of the credit period by checking the appropriate box in Part II of the IRS Form 8609. A sample copy of this form and its instructions are located on the MSHDA website.

B. Initial Year Proportion

A project claiming credit in the initial year of occupancy is subject to a special provision limiting the credit to a proportionate amount based on average occupancy during the year. For example:

A project (comprised of one building and a total of 50 low-income residential units) is not available for occupancy (i.e. construction or rehab is not complete) from January 1 through October 31. After completion of construction, the building became available for occupancy on November 1. If the building reached 50% occupancy in November and 100% occupancy in December, the building would be eligible for credit for 1 ½ months of the 12 months calendar year. In other words, the building would be treated as being in service for 12.5% of the year (1 ½ months, based on 50% occupancy in November and 100% occupancy in December). In the 11th year, the disallowed credit of 87.5% (based on the 10 ½ months of the initial year in which the units were unoccupied) could be claimed.

If a qualified low income tenant becomes an ineligible tenant prior to the end of the initial tax credit year, that unit cannot be counted in the first year toward the minimum set-aside for purposes of determining the qualified basis.

Further, per IRS Revenue Ruling 2004-82, during the first year of the credit period, units occupied by qualified households by the last day of a month are included in that month's applicable fraction provided the building was in service a full month.

For additional information about the First Year of the Credit Period, see **Part 854** (Relocating Existing Tenants during the First Year of the Credit Period), which discusses transfers during the first year of the credit period.

Part 140 : First Year of the Credit Period – Acquisition / Rehabilitation Projects

IRS Revenue Ruling 2004-82

Following is a summary of the guidelines for acquisition/rehabilitation (acq/rehab) projects that have been provided in IRS Revenue Rulings and in the IRS 8823 Guide. Owners should consult an accountant, attorney, or other professional with LIHTC Program expertise prior to determining the amount of credit to claim.

Determining the First Credit Year

- The most important issue for an owner to be eligible to start claiming credit is the date resident eligibility is certified.
- Once the rehabilitation threshold is met, the second placed-in-service date is chosen, and the project is able to earn rehabilitation credits.
- Owners may claim credit for both acq/rehab back to the date of acquisition or the first day of their fiscal year, dependent on the rehab placed in service date.
- If an owner is claiming credit back to the date of acquisition, all units that credit is being claimed for must be certified as eligible households as of the purchase date.
- For acq/rehab properties, both the acquisition and rehabilitation credit must be claimed for the same time period. Credit cannot be claimed in years prior to the rehab placed in service year.

- Credit can be claimed back to the date of acquisition only if the rehab was completed in the same fiscal year. If the rehab was completed in a later fiscal year, credit can only be claimed as of the first day of the fiscal year.

Two important considerations

For LIHTC projects involving both acquisition and rehabilitation, there are two important considerations in determining the first credit year:

- I. The earliest possible date from which credit can be claimed (see examples below); and
- II. The date on which existing tenants must be certified as income-eligible (which is discussed in **Part 344**).

Examples of Determining the Earliest Possible Date from Which Credit Can be Claimed

A. Acq Date and Rehab PIS date are in the SAME fiscal year

- All of the examples below assume the owner's fiscal year is the January 1 – December 31 calendar year.
- All of the examples below assume that there is only one unit in each building.

Example #1 {Existing Tenant was certified within 120 days of the Acq Date}

| | |
|--|------------------|
| <i>Acquisition Date</i> | <i>04/13/04</i> |
| <i>Rehab Placed In Service Date</i> | <i>11/29/04</i> |
| <i>Earliest Date from which Credit can be Claimed*</i> | <i>04/13/04*</i> |

**Provided the tenant is certified as LIHTC-eligible within 120 days before or after 4/13/04. Both the acquisition credits and the rehabilitation credits can be claimed from this date.*

Example #2 - {Existing Tenant not certified within 120 days after the Acq Date}

| | |
|---|-------------------|
| <i>Acquisition Date</i> | <i>04/13/04</i> |
| <i>120 days after Acquisition Date</i> | <i>08/11/04</i> |
| <i>Date Existing Tenant was Certified as LIHTC-eligible</i> | <i>08/23/04</i> |
| <i>Rehab Placed in Service Date</i> | <i>11/29/04</i> |
| <i>Earliest Date from which Credit can be Claimed**</i> | <i>08/23/04**</i> |

***Since the tenant was not certified within 120 days of the acquisition date, the earliest date that credit can be claimed from becomes the date the tenant was actually certified. The “earliest date” is not “back-dated” to the acquisition date as in Example #1 for neither the acquisition nor the rehabilitation credits. Both the acquisition and rehabilitation credits can be claimed from 08/23/04, even though the rehab placed in service date is after this date, due to the fact that the rehab placed in service date is in the same fiscal year as the acquisition placed in service date.*

Example #3 – {Existing tenant not certified until after the rehab placed in service date}

| | |
|--|--------------------|
| <i>Acquisition Date</i> | <i>04/13/04</i> |
| <i>Rehab Placed in Service Date</i> | <i>11/29/04</i> |
| <i>Date Tenant Certified as LIHTC-eligible</i> | <i>12/15/04</i> |
| <i>Earliest Date from which Credit can be Claimed***</i> | <i>12/15/04***</i> |

***Since the tenant was not certified before the rehab placed in service date, the earliest date that credit can be claimed is the date the tenant was certified as LIHTC eligible.

B. Acq Date and Rehab PIS date are in DIFFERENT fiscal years

- All of the examples below assume the owner's fiscal year is the January 1 – December 31 calendar year.
- All of the examples below assume that there is only one unit in each building.

Example #4

| | |
|--|--------------|
| Acquisition Date | 04/13/04 |
| Rehab Placed In Service Date | 11/23/05 |
| Earliest Date from which Credit can be Claimed**** | 01/01/05**** |

****Provided the tenant is certified as LIHTC-eligible within 120 days before or after the 01/01/05 date (as discussed in **Part 348**, Item d).

For related discussions, see **Part 348** (Acq/Rehab Projects – Certifying Existing Tenants), **Part 856** (Temporary Relocation), and **Part 854** (Transfers during the First Year of the Credit Period).

Part 142 : First Year of the Credit Period – Multiple Government Programs

All existing tenants in newly placed in service acquisition/rehabilitation projects should be screened to determine LIHTC eligibility as if they were new move-ins. Even if they have previously qualified for a housing program like Section 8, current residents do not automatically qualify to live in a LIHTC development; they must meet LIHTC guidelines as if moving in for the first time.

Resident Recertification Schedule with Multiple Government Programs

Sometimes an existing Rural Development (referred to as RHS or RD), Section 8, or Section 236 project is refinanced as a LIHTC project. In these situations, there may be residents that currently live at the development and who already have a schedule for their annual recertification pursuant to the RHS, Section 8, or Section 236 program requirements. When adding LIHTC to the property, MSHDA does not require a change in the certification schedule or reporting requirements for these other programs. However, to meet the LIHTC initial eligibility certification requirements, the owner/management agent reviews the certification conducted for the other government program and in some situations, must perform a special full certification (including initial LIHTC certification with third party verifications) to ascertain LIHTC-eligibility (as discussed in **Chapter 11**). After an initial eligibility certification for LIHTC purposes is completed, the household's annual certification requirements can remain the same as they were under the RHS, Section 8, or Section 236 program. LIHTC requires only that a household be recertified at least once during every 12 month period. For example:

A project became a Rural Development (RD) in 1998. In 2002, the project is sold and rehabbed as a LIHTC project.

| | |
|--|---------------------|
| Household's Actual Move-in Date | 2/28/98 |
| Regularly Scheduled RD Annual Recertification Date | Feb. 1 of each year |
| Purchase Date (for LIHTC purposes) | 07/23/02 |
| Rehab Placed In Service Date | 12/31/02 |

First Date from Which Credit Will Be Claimed*

07/23/02

**Households must be certified as LIHTC-eligible within 120 days before or after this date. The RD certification conducted on 02/01/2002 can not be used for LIHTC purposes since it was conducted more than 120 days from the required LIHTC eligibility date. Therefore, a separate certification must be conducted in order to determine LIHTC-eligibility.*

Household Initial Certification Date (for LIHTC purposes)

07/23/02

Next scheduled RD Annual Recertification Date**

02/01/03

***This 2/01/03 recertification can be used to satisfy both the RD and LIHTC recertification requirements. LIHTC only requires that tenants be certified at least once per year. The tenant would not have to be recertified on the anniversary date of the LIHTC certification.*

For additional information specific to preservation projects, see [Chapter 11](#) (Preservation Projects – Procedures for Certifying Initial LIHTC Eligibility).

Part 144 **First Year Credit Statement**

As part of the Annual Compliance Certifications (see [Part 704](#)), the owner must complete a First Year Credit Statement form. This form indicates the first year for which the tax credit was claimed and the number of units for which the tax credit was claimed. A sample copy of the First Year Credit Statement form is available on the MSHDA website.

Part 146 **Claiming the LIHTC in Years Two through Ten**

Owners must file an IRS Form 8609 (Low Income Housing Credit) with the Internal Revenue Service for every year of the ten-year period. This form is a certification by the owner that the LIHTC projects have been in continuing compliance and provides the qualified basis of the development for each year of the credit period. IRS Form 8586 must be attached to IRS Form 8609 and Schedule A (IRS Form 8609) and submitted annually with the owner's federal tax return. A sample copy of this form is available on the MSHDA website.

Part 148 **Units that Have Never Been Occupied by Qualified Residents**

Units that have never been occupied cannot be counted as "low-income", but must be included in the "total units" figure for purposes of determining the applicable percentage. Existing tenants can not be transferred to never-occupied units for purposes of meeting the minimum set-aside or applicable fraction in the first credit year of the project. In other words, one tenant household can not be used to qualify more than one unit for LIHTC purposes. For related discussions, see [Part 826](#) (Vacant Unit Rule - Transfers) and [Part 854](#) (Transfers during The First Year of the Credit Period).

Part 150 **The Two-Thirds (2/3) Rule**

If a tax credit unit has not been occupied by the end of the first year of the credit period, tax credits cannot be claimed on that never-occupied unit in that year. Should the unit become occupied after the end of the first year of the credit period, two-thirds of the credit can be claimed each year for the remaining years of the 15-year compliance period. In other words, 14 years of 2/3 of the credit amount allocated for that unit can be claimed. Thus, 1/3 of one year's worth of credit will be permanently lost. A simplistic example is as follows:

A 100-unit project with a 100% applicable fraction has an annual credit allocation of \$500,000. In theory, each of the 100 units is "worth" \$5,000 per year in tax credits, which is \$50,000 total over the ten year credit period. The total amount of credit available for the 100 unit project is \$5,000,000 over a ten year period.

During the first year the building is placed in service, only 99 of the 100 units are leased. Even though the applicable fraction was not met, the owner elects to claim credits for that year for the 99 units. The maximum amount of credit that the owner could take would be \$5,000 for each of 99 units, or \$495,000 total for the 99 units combined.

In the second year, the one remaining unit is occupied by the LIHTC-eligible tenant. As stated previously, the pro-rated amount of credit per unit is \$5,000. Since the owner did not lease the unit during the first year of the credit period, each year he or she would be eligible to claim only 2/3 of the \$5,000 pro-rated allocation, or \$3,333.33. That amount, \$3,333.33 could be claimed each year for 14 years (as opposed to the normal 10 year accelerated period). Over the 14 years, the amount of credit claimed would be \$46,666.67, rather than the \$50,000 that would have been eligible if the 2/3 rule had not been triggered due to failure to lease the unit during the first credit year.

If an owner decides to take the tax credit for a property in the initial year when, for example, only 80% of the units are rented to tax credit eligible tenants, the maximum qualified basis for the entire credit period would be 80% with the remaining 20% eligible for two-thirds credit if later rented to eligible tenants. [Continuing the example above, if the remaining unit wasn't rented until the beginning of third year, that unit would be eligible for 2/3 credits for 13 years (years 3 through 15).]

Part 152 **Definition of a Low-Income Unit**

Tax credits "attach" to each qualified low-income unit, which is usually an apartment unit. However, a unit may be part of a duplex, triplex, single-room occupancy (SRO) building, a rented manufactured home or a rented single-family house. In this manual, the term "project" includes both multifamily housing complexes and scattered site projects, and the rules apply to low-income units in any configuration.

Qualified units rented to or reserved for, eligible tenants:

- Must have substantially the same equipment and amenities (including luxuries such as fireplaces and whirlpool tubs if these amenities are/were included in eligible basis) as other units in the project; and
- Cannot be geographically segregated from other units in the project.

Units intended for eligible tenants must be comparable in size, location, and quality to those rented to other tenants. In the event a residential unit in a project which is not rented to an eligible tenant is above the average quality standards of the units rented to eligible tenants, then the basis in the project which is used to determine the amount of tax credits must be reduced by the portion which is attributable to the excess costs of the above standard units.

Further, in order to be eligible for tax credits, a unit must:

- Be suitable for occupancy, based on the Uniform Physical Condition Standards and all applicable local housing codes;
- Be occupied by a qualified low-income household or last occupied by a qualified household;
- Be currently available for rent;
- Be appropriately rent-restricted;
- Be used on a non-transient basis (except for transitional housing); and
- Be available to the general public.

Part 154 : Project Numbers

MSHDA Number

MSHDA currently uses a four-digit number (the “MSHDA #” and formerly referred to as “The MITAS Number”) to identify each project funded under any of the Direct Loan, LIHTC, HOME, Pass-through, Section 8, Section 236, or other rental housing program administered by MSHDA.

Building Identification Number (BIN)

All LIHTC buildings are assigned a nine character code consisting of two letters followed by a seven-digit number. This number is assigned by MSHDA at the time the building is allocated credit. Each building will have a different BIN number. The two letters denote the State that allocated the tax credits. For example, “MI” indicates Michigan. The first two numeric digits represent the year that the credit was allocated to the project. For example:

Michigan Villas has two buildings, with the BIN#s MI-87-12301 and MI-87-12302. “MI” identifies Michigan as the allocating state. The “87” indicates that the building was allocated credit in the year 1987. The last two digits indicate the building number in the project, either “01” or “02”.

See [Part 132](#) (Year of The Credit) and IRS Notice 88-91 (Building Identification Numbers) for additional information.

Tax Credit Application Number

Each project that submits an application for allocation of tax credits is assigned a six character code consisting of a letter, the first two digits of the year the application was submitted, and three digits to indicate the sequence the application was received by MSHDA. Not all projects that submit an application are approved for an allocation of tax credits. The application number is used only during the application process and is replaced by the MSHDA number and the BIN number discussed above for projects that are approved for an allocation of tax credits. (This tax credit application numbering system is subject to change in the near future.)

LIHTC Project Number

Each building within the project is assigned a building identification number. Each project (which could be comprised of one or more buildings) is assigned a six-digit number. The project number is usually a six-digit derivative of the building identification number(s). For example, a project with the building identification numbers MI-87-12301 and MI-87-12302 would be given the project number “870123”. [Note: The six-digit LIHTC project number is now seldom used. Instead, the MSHDA number discussed above is now the preferred identifier.]

Part 156 : Important Periods for LIHTC Projects

- Credit Period - Tax credits can be claimed each year for a 10-year period. See **Part 136** for more information.
- Year of the Credit (Allocation Year) - The year of the credit is the year that the tax credits were allocated for the particular project. See **Part 132** for more information.
- First Year of the Credit Period – This is either the year a building is placed in service, or, at the owner’s option, the following year. See **Parts 136 – 144** for more information.
- The Compliance Period runs for 15 years, during which time any noncompliance with Section 42 could result in a recapture of a portion or all of the credit. See **Part 160** (The Compliance Period) for more information.
- The Extended Use Period runs 30 years, and can only be terminated earlier under certain circumstances. See **Part 900** (Extended Use Period) for more information about the Extended Use Period. See **Part 902** (Terminating the Extended Use Period) for information about early termination.
- The Three-Year Tenant Protection Period is the three years following the last of any of the above periods, during which time no low-income tenant can be evicted except for good cause and rents must remain at the restricted level. The Three-Year Period is intended to allow a transition of use of the project following the low-income use under the program. The Three-Year Tenant Protection Period is discussed in greater detail in **Part 904**.
- The Additional Low-Income Housing Use Period is a commitment to the Authority to maintain the housing for a specified period of years, which may extend beyond the Extended Low-Income Housing Use Period, with an agreement not to terminate the low-income use or Regulatory Agreement during this period. Many owners make the maximum time commitment in the allocation process. See **Part 220** (Michigan’s Qualified Allocation Plan) for more information.

Section 1C - Compliance Overview for LIHTC Projects

Part 158 : IRC Section 42 Compliance and Monitoring Requirement for LIHTC

The fundamental requirements for LIHTC projects are that the housing units must be rented only to income-qualified households and the rents for those LIHTC units must be restricted. Household income is determined at the time tenancy begins and is based on the actual number of persons in the household at the time of initial occupancy and the appropriate median gross income for the county in which the project is located and/or date the project was placed in service. This is known as the “Area Median Gross Income” or “AMGI”. The rent level is also tied to the AMGI. Additional discussion of household income and how unit rent is determined is included in **Chapter 4** (Income Limits, Rent Limits, and Utility Allowances).

As of January 1, 1992, Section 42 (m)(1)(B)(iii) of the Code requires that each state’s Qualified Allocation Plan provides a procedure that the agency will follow in notifying the Internal Revenue Service (IRS) of any noncompliance with the provisions of Section 42 of which it becomes aware. Final IRS regulations, published in September 1992, outline minimum requirements for owner record-keeping and reporting, state credit agency monitoring and inspecting, and reporting instances of noncompliance to the IRS. LIHTC Compliance Monitoring regulations are listed in IRC Section 1.42–5. A link to the compliance regulations is available on the MSHDA website.

Michigan’s compliance monitoring plan follows the final regulations, as well as the recommendations of the National Council of State Housing Agencies (NCSHA), and is applicable to all owners of all buildings which have ever claimed the low income housing tax credit since the inception of the program in 1987.

Part 160 : The Compliance Period

Internal Revenue Code (IRC) Section 42(j)(1)

Once allocated by the housing credit agency, tax credits can be claimed annually over a ten (10) year period. All projects must, however, remain in compliance for a minimum of fifteen (15) years, with some requirements extending for an additional three years after that. The period of 15 taxable years begins with the first taxable year of a building’s credit period (the “Compliance Period”) per Section 42(i)(1). All requirements of IRC Section 42 including the 1.42-5 monitoring regulations are in effect during the 15-year compliance period. Additionally, owners who agree in their applications to have longer compliance periods will be bound for the length of time specified.

- A. **Projects that received Credit Allocations in 1987, 1988, and 1989 only (Pre-1990)**
{As of the date of this Compliance Manual, all projects that received allocations of credit during 1987, 1988, and 1989 have completed their 15-year compliance period and are no longer in the LIHTC program, with the exception of those which were re-financed or preserved}.

Generally, properties receiving a credit allocation before January 1, 1990 have only a 15-year compliance period. However, any building in such a property that receives an additional allocation of credit after December 31, 1989, must comply with eligibility re-

quirements in effect beginning January 1, 1990 and will be bound by a Restrictive Covenant. Projects that received credit allocations in 1987, 1988, or 1989 have building identification numbers beginning with a “87”, “88”, or “89”.

B. Projects receiving Credit Allocations after December 21, 1989 (Post-1989)

Owners of developments with allocations of 1990 credit and thereafter will have entered into a restrictive covenant with MSHDA at the time of final allocation. The restrictive covenant is a recorded land use agreement and is also sometimes referred to as a Regulatory Agreement. These developments must comply with eligibility requirements for an additional 15 years beyond the initial 15-year compliance period (or a total of 30 years). These developments have Compliance Periods that are a minimum of 30 years long. If a property receives ranking points for income and rent restrictions beyond the initial 15 years, the owner will be bound by this election in the Regulatory Agreement. Early termination of the extended use period is provided for under certain circumstances in the code (as discussed in [Part 902](#)). Projects that received credit allocations after 1989 have building identification numbers that begin with digits other than “87”, “88”, or “89”.

For additional information, see [Part 134](#) (Placing a LIHTC Building in Service), [Part 164](#) (Regulatory Agreement), and [Part 154](#) (Building Identification Numbers).

Note: The Credit Period (discussed in [Part 136](#)) differs from the Compliance Period. The Credit Period represents the first 10 years (or, in some situations, 11 years) of the Compliance Period. The Compliance Period is a component of the Extended Use Period (discussed in [Part 900](#)).

Part 162 : Overview of Compliance Requirements

- Responsibilities - see [Chapter 2](#).
- Tenant Eligibility Certification Process - see [Chapter 3](#) (Qualifying Tenants for Restricted Units).
- Tenant Demographics and Household Composition - see [Chapter 5](#).
- Compliance Procedures and Forms - see [Chapter 6](#).
- Federal and State Laws and Regulations - see [Part 566](#).
- Tenant File Audits - see [Part 708](#).
- Physical Inspections - see [Part 732](#).
- On-going Certifications and the MSHDA’s On-line Tenant Data Reporting System - see [Part 700](#).
- Compliance Requirements during the Extended Use Period - see [Chapter 9](#).
- Unit-, Building-, and Project-level Rules - see [Chapter 8](#).
- Noncompliance - see [Chapter 10](#).

IRC §42(h)(6)

The commitments made by the Owner to receive an allocation of credit are initially identified in a Carryover Allocation Agreement, and are later evidenced in a Regulatory Agreement. The Regulatory Agreement is a restrictive covenant recorded with the Register of Deeds, and is called an “Extended Use Agreement” in Section 42. The Regulatory Agreement is also sometimes referred to as a Land Use Restrictive Agreement (LURA).

The restrictive covenant binds the owner and any successors to maintain specified low-income occupancy during the extended use period. The extended use period may end in the event of foreclosure or if, during or after the 14th year of the tax credit period, the owner requests that the credit agency find a buyer willing to enter into a “qualified contract” to purchase the property and maintain its low income use for the remainder of the extended use period. For information, see **Part 906** (Qualified Contract) and **Part 160** (Compliance Period).

As stated in the IRS 8823 Guide, Extended Use Agreements must:

- specify that the applicable fraction for the building for each year in the extended use period will not be less than the applicable fraction specified in the extended use agreement and which prohibits the eviction or the termination of tenancy (other than for good cause) of an existing tenant of any low-income unit, or any increase in the gross rent with respect to such unit not otherwise permitted under IRC §42.
- allow individuals (whether prospective, present, or former occupants) who meet the income limitation applicable to the building under IRC §42(g) the right to enforce in state court the requirements and prohibitions under IRC §42(h)(6)(B)(i), including maintaining the applicable fraction and prohibiting the eviction or the termination of tenancy (other than for good cause) of an existing tenant of any low-income unit, or any increase in the gross rent with respect to such unit not otherwise permitted under IRC §42. These prohibitions apply throughout the extended use period.¹
- prohibit the disposition to any person of any portion of the building unless all of the building is disposed of to that person.
- prohibit the refusal to lease to section 8 voucher holders because of the status of the prospective tenant as such a holder,
- provide that the agreement is binding on all successors of the taxpayer, and
- the extended use agreement must be recorded as a restrictive covenant with respect to the property under state law.

In addition, as specified in IRS Revenue Ruling 2004-82, extended use agreements must contain language prohibiting eviction or termination of tenancy of a low-income household other than for good cause for the entire extended use period. **See Part 626** (Good Cause for Lease Terminations and Evictions) for additional information.

Many projects, particularly those allocated in 1994 and beyond, elect to extend the number of low-income use restriction years (some into perpetuity) in order to receive additional points in the scor-

ing process. The option of requesting that the credit agency find a purchaser under the qualified contract process is not available to owners who agreed to longer compliance periods or to owners of projects that allocated credit in or after 2005.

MSHDA prepares a Regulatory Agreement prior to issuance of the IRS Form 8609. The document must be recorded by the owner before the end of the calendar year for which credit is first claimed. When the original recorded document is returned to MSHDA, all fees have been paid, and all other required documents have been submitted to MSHDA, the IRS Form 8609 will be sent to the owner by MSHDA.

For additional information about the extended use commitment, see **Part 900** (Extended Use Period).

Part 166 : **Year 15 and After the LIHTC Compliance Period**
: **Ends**

If the project's allocation(s) of credit was prior to 1990 and there is no Regulatory Agreement recorded for the property, activity of the property (unit events, physical property, etc.) will be monitored through December 31 of the 15th compliance year. Final analysis will be performed after receipt of the last tenant data, audit and physical inspection. For example:

A property was allocated credit in 1988. The project does not have a Regulatory Agreement and the owner elected to defer credit until 1989. The project's 15 year compliance period ended on December 31, 2003.

If the project received an allocation of credit in 1990 or later, a Regulatory Agreement was recorded for the property. The agreement is a restrictive covenant recorded against the property and extends the low-income use of the property beyond the initial 15-year compliance period. Regulatory Agreements are discussed in **Part 164**.

For information about requirements for the time period following year 15 of the compliance period, see IRS Revenue Ruling 92-79 (Extended-Use Commitment) and IRS Revenue Ruling 95-49 (Tenant Right to First Refusal). The scope of monitoring activities after year 15 is discussed in **Chapter 9** (Compliance and Monitoring after Year 15 of the Extended Use Period).