AFFORDABLE RENTAL HOUSING A.C.T.I.O.N.
A Call To Invest in Our Neighborhoods

Frequently Asked Questions

The Low-Income Housing Tax Credit

HOW THE LOW-INCOME HOUSING TAX CREDIT WORKS

What is the Low-Income Housing Tax Credit (Housing Credit)?

The Housing Credit is a federal tax credit created by the Tax Reform Act of 1986 and is designed to encourage the private sector investment in the new construction, acquisition, and rehabilitation of rental housing affordable to low-income households. Since President Reagan signed it into law in 1986, the Housing Credit has financed the construction and preservation of nearly 3.5 million affordable homes nationwide, at a rate of more than 120,000 per year. Today it produces virtually all new affordable rental housing and is our primary tool for preserving existing affordable housing.

How does the Housing Credit work?

The Housing Credit offers a dollar-for-dollar reduction in a taxpayer's income tax liability in return for making a long-term investment in affordable rental housing. State agencies award Housing Credits to developers, who engage private investors in the property's ownership. The investors provide upfront equity capital to fund the construction and rehabilitation of affordable housing, allowing developers to borrow less money and pass through the savings in lower rents for low-income tenants. Investors, in turn, receive a 10-year stream of tax credits based on the cost of constructing or rehabilitating apartments that must be rented to low-income households.

The incentive allows states to allocate Housing Credits to developments they select pursuant to qualified allocation plans (QAPs) they develop that identify the type, location, and other characteristics of affordable rental housing needed throughout the state. The QAPs must describe the criteria agencies will apply in allocating the Credit and are subject to review after a public hearing and comment process. In this way, the Housing Credit empowers states to respond to the housing needs, priorities, and challenges they consider most important.

Developers submit applications for credits through a highly competitive process using the QAP as a guide. Each year, allocating agencies receive applications requesting two to three times more Housing Credits than the agencies have to allocate. Housing Credits are then awarded to developers based on how well their proposed projects meet the locally established criteria.

The Housing Credit has two components: the "9 percent" Credit and the "4 percent" Credit. The annual amount of 9 percent Housing Credit authority in each state is based on the state's population. In 2021, the state Credit cap is $2.81 times the state's population, with a state minimum of $3,245,625.[1] Volume cap figures are published by the IRS on an annual basis and subject to an inflation adjustment.

The 4 percent component is typically generated by the use of tax-exempt private activity multifamily Housing Bonds. The 4 percent Housing Credit is also used for acquisition, which comes out of the state ceiling. Housing Bonds and the 4 percent Housing Credit finance approximately 50 percent of Housing Credit rental homes every year. Because multifamily Housing Bonds are limited by the Private Activity Bond (PAB) volume cap, the 4 percent Credit is not subject to the Housing Credit volume cap. Not only do Housing Bonds make possible the production of substantial numbers of new Housing Credit properties, they are essential to state efforts to preserve affordable housing. In 2021, the state PAB cap is $110 times the state's population, with a state minimum of $324,995,000.[2] Like the Housing Credit cap, the IRS publishes PAB cap amounts annually and provides an inflation adjustment.

Only once the property is constructed, meets all federal requirements and is occupied by income-eligible tenants paying affordable rents can the developer begin claiming credits. In the rare case that a property falls out of compliance at any time over the next fifteen years, credits are subject to recapture. The private sector, not taxpayers, bear the financial risk. The property is also subject to continued affordability restrictions enforced by the states for at least another 15 years, though many states impose even longer affordability requirements.

What are Tax-Exempt Multifamily Housing Bonds (Housing Bonds)?

Multifamily Housing Bonds are critical to the Housing Credit program because the use of these bonds is the primary way to generate 4 percent Housing Credits.

Multifamily housing bonds are used by states and local governments to finance low-interest loans for affordable rental housing developers seeking to acquire, construct, and/or rehabilitate multifamily housing for low-income renters. These bonds are a type of tax-exempt private activity bonds (PAB), which are bonds used by private owners for activities that serve a public purpose. Like the Housing Credit, the amount of PAB authority each state receives annually is based on population.

Under current law, if multifamily Housing Bonds are used to finance at least 50 percent of the aggregate land and building costs of a property, 4 percent Credits are available on the property's full qualified basis. These 4 percent Housing Credits do not count against the state's annual allocated Housing Credit cap. Instead, 4 percent Housing Credits are essentially limited because PAB authority is limited.

Bond-financed Housing Credit developments must comply with the state's allocation plan established in the QAP and with all other applicable Housing Credit program rules, including those related to income targeting and the affordability period.

[1] U.S. Department of Treasury, Internal Revenue Service, Notice 2020-45
[2] Ibid.

Whom does the Housing Credit serve?

The Housing Credit program generally serves low-income working households earning 60 percent of area median income (AMI) or less, with congressional direction to serve the lowest income households possible. In practice, states well exceed this statutory requirement, reaching families with incomes much lower than the program's income limits. According to HUD data on Housing Credit resident demographics, nearly 45 percent of all households living in Housing Credit apartments are extremely low income, meaning they earn 30 percent of AMI or less.[3] Another 34 percent were very low income, earning between 30 and 50 percent of AMI, and the remaining 21.5 percent earn more than 50 percent of AMI.[4]

In 2018, Congress amended the Housing Credit statute to allow owners to opt to *income average* in any individual property. Under the new Average Income Test (AIT), a household could qualify to live in a Housing Credit property if their income is no greater than 80 percent of AMI ***as long as*** the average income limit in the property is at or below 60 percent of AMI. This means, if an owner allows households between 60 and 80 percent of AMI to rent units in the property, they must also set aside units in that property for households at lower income levels in order to maintain an average of no more than 60 percent of AMI. Income averaging preserves rigorous targeting to low-income households, while providing more flexibility to the program and greater income-mixing potential. The IRS recently proposed regulations implementing this provision. Many in the affordable housing community have provided feedback on these proposed regulations, encouraging the IRS to publish final regulations that effectively implements the AIT.

The flexibility of the Housing Credit has made it an attractive tool for meeting housing needs across rural, urban, and suburban areas. It finances housing for low-income families with children, seniors, veterans, members of Native American tribes, and people with disabilities. The Housing Credit has been instrumental in the production of permanent supportive housing for persons experiencing homelessness, those recovering from opioid addictions, and other special needs populations.

How do states provide oversight and prevent against fraud?

As directed by Congress, state allocating agencies take the lead on oversight and work with the IRS to monitor project compliance. State agencies regularly conduct extensive reviews of Housing Credit developments to inspect their physical and financial condition, certify their occupancy by qualified low-income residents, and ensure overall compliance with federal rules. State agencies also underwrite transactions to make sure that costs are reasonable and that the amount of Housing Credits awarded is the minimum needed to complete the project. A 2017 GAO study of state agencies' administration of the program found that states often go above and beyond the compliance monitoring responsibilities required of them by law. Multiple parties – both public and private – scrutinize each transaction from beginning to end, providing independent checks and balances, and tenants have full enforcement rights as well.

[2] HUD: Understanding Whom the LIHTC Serves: Data on Tenants in LIHTC Units as of December 31, 2017
[4] HUD: Understanding Whom the LIHTC Serves: Data on Tenants in LIHTC Units as of December 31, 2017

There is no evidence of widespread fraud in the Housing Credit program. Out of 40,000 properties developed, very few isolated cases have been found and the violators have been prosecuted swiftly. The record of states monitoring for compliance is strong and the affordable housing industry supports all efforts to investigate and vigorously prosecute any violations.

PROPOSALS TO STRENGTHEN AND EXPAND THE HOUSING CREDIT

What is the Affordable Housing Credit Improvement Act?

The Affordable Housing Credit Improvement Act of 2021 (S. 1136 and H.R. 2573) is bipartisan legislation that would make numerous modifications to strengthen the Housing Credit by providing states with additional flexibility, making the financing of affordable housing more predictable and streamlined, facilitating Housing Credit development in challenging markets like rural and Native American communities, increasing the Housing Credit's ability to serve extremely low-income tenants, and supporting the preservation of existing affordable housing. It was introduced in the Senate by Senators Maria Cantwell (D-WA), Todd Young (R-IN), Ron Wyden (D-OR), and Rob Portman (R-OH), and in the House by Representatives Suzan DelBene (D-WA), Jackie Walorski (R-IN), Don Beyer (D-VA), and Brad Wenstrup (R-OH).

Is there enough developer demand to absorb a significant increase in Housing Credits?

In 2019 – the most recent year for which data is available – state Housing Credit allocating agencies received applications requesting more than twice their available Housing Credit authority. Many more potential applications for worthy developments are not submitted in light of the program's intense competition, suggesting the demand is even broader.

What does the Housing Credit cost? What would it cost to expand it by 50 percent?

According to the congressional Joint Committee on Taxation (JCT), the Housing Credit currently costs roughly $10 billion per year in foregone revenue, which represents an annual snapshot of all Housing Credit properties placed in service in their initial 10-year Credit period.[5]

THE NEED FOR THE HOUSING CREDIT

Why does the federal government need to invest in affordable housing?

The Housing Credit is necessary because our nation faces an affordable housing crisis, which is growing more and more critical. The U.S. rental market remains extremely tight, and increased demand for rental housing in recent years has caused rents to rise drastically. Renter households have been especially vulnerable to the economic disruption caused by COVID-19. Data from the Household Pulse Survey from late September found that 28 percent of renters used their onetime federal stimulus checks to cover basic needs, including rent, and 17 percent used unemployment insurance benefits. But many households have

[5] Joint Committee on Taxation, *Estimates of Federal Tax Expenditures for Fiscal Years 2020-2024*.

simply fallen behind on rent payments, making them vulnerable to eviction.[6] Housing costs are rapidly rising, with rents rising at twice the pace of inflation on average nationwide.[7]

According to HUD's most recent *Worst-Case Housing Needs* report, 7.72 million very low-income renter households had worst-case housing needs in 2017, meaning they did not receive government housing assistance and paid more than half of their incomes for rent, lived in severely inadequate conditions, or both — a 7.1 percent decrease in just two years.[8]

Currently, there is a shortage of more than 7 million affordable rental units for extremely low-income (ELI) renters, with only 37 affordable and available units for every 100 ELI renter households nationwide, and 70 percent of ELI renters are spending more than half of their incomes on housing.[9] Low-income renters who are unable to find affordable apartments are forced to pay a significant portion of their incomes for housing — leaving little money left over for other necessities like food, transportation, childcare, healthcare, and utilities.

The Housing Credit is an efficient and effective tool for providing affordable housing to the people who need it most. The Credit accounts for the vast majority of the country's new and substantially rehabilitated rental housing affordable to low-income people, creating affordable housing opportunities for the millions of families in our country today who otherwise pay an excessive portion of their incomes for housing, live in substandard and overcrowded conditions, or face homelessness. Our nation also relies on the Housing Credit more and more to preserve the existing affordable rental housing stock that is often desperately in need of recapitalization.

If there is so much demand for affordable rental housing, why doesn't the private sector provide it?

The economics of rental housing development make it financially infeasible to build safe and decent affordable housing without a subsidy such as the Housing Credit. The Housing Credit enables developers to raise equity capital from investors, which significantly reduces the debt on properties, enabling lower rents. 9 percent Housing Credit equity typically represents about 50-75 percent of the total development costs. According to JCHS, "to develop new apartments affordable to renter households with incomes equivalent to the full-time minimum wage, the construction costs would have to be 28% of the current average" – essentially making the financing impossible.

Why do we need to build affordable rental housing – can we just use vouchers?

The Housing Credit is often creatively combined with resources from several programs**,** including vouchers, to create better outcomes than is possible with just one affordable housing tool. Vouchers are one of the primary vehicles for providing affordable housing choices to extremely low-income families, especially in low-cost housing markets. However, vouchers are not a replacement for the Housing Credit, which expands or preserves the affordable housing stock as a long-term community asset. Likewise, the

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6 Joint Center for Housing Studies of Harvard University, *The State of the Nation's Housing 2020*
7 Joint Center for Housing Studies of Harvard University, *America's Rental Housing 2020*
8 U.S. Department of Housing and Urban Development, *Worst Case Housing Needs 2019*
9 National Low Income Housing Coalition, *The Gap: A Shortage of Affordable Homes 2021*

Housing Credit, as a capital subsidy, cannot on its own ensure apartments are affordable to the very lowest income renters. Housing Credits and vouchers are often used together to address complementary issues: the Housing Credit to bring down the cost of the unit on a long-term basis, and the voucher to enable that already low-cost unit to be more affordable to the lowest income tenants.

There are several rental housing market challenges that the Housing Credit is uniquely positioned to address, such as expanding supply in tight markets, producing housing for households with special needs, providing affordable housing options in areas experiencing job growth, recapitalizing and preserving aging properties, and revitalizing low-income communities. The Housing Credit also enables voucher holders to access a broader array of housing options. As it is, many voucher holders are unable to find available units or a landlord who will accept their voucher. This problem has exacerbated in recent years as demand for rental housing has increased while vacancy rates have declined and rents have skyrocketed. Housing Credit properties are required by law to accept voucher holders.

How does the Housing Credit impact surrounding neighborhoods?

The Housing Credit supports economic growth in communities and surrounding neighborhoods in a number of ways. Using a 2020 National Association of Home Builders (NAHB) study, the Housing Credit is estimated to have added $23.9 billion in income to the economy and generates approximately $8.3 billion in federal, state, and local taxes in 2019. Housing Credit development also supports jobs – roughly 1,600 for every 1,000 Housing Credit apartments developed, according to NAHB. This amounts to roughly 96,000 jobs per year, and more than 5.5 million since the program was created in 1986, across a diverse range of industries, including the manufacturing of lighting and heating equipment, lumber, concrete, and other products, as well as jobs in transportation, engineering, law, and real estate.

Conversely, a lack of affordable housing negatively impacts economies. Research shows that high rent burdens have priced out many workers from the most productive cities, resulting in 13.5 percent foregone GDP growth, a loss of roughly $1.95 trillion, between 1964 and 2009.

Housing Credit development also positively impacts neighborhoods in need of renewal. About one-third of Housing Credit properties help revitalize distressed communities. Stanford University research shows Housing Credit investments improve property values in low-income communities and reduce poverty, crime, and racial and economic isolation, generating a variety of socioeconomic opportunities for Housing Credit tenants and neighborhood residents.