

## Updated White Paper Provides Revised Recovery Estimates for Frozen LIHTC Rents

By Alex Ruiz, Managing Editor, Novogradac & Company LLP

Last month, Novogradac & Company LLP published an update to its white paper entitled “Effect of HUD’s Revised Income Calculations on Housing Tax Credit Properties: How Long Until Qualifying Incomes & Tax Credits Rise.” The original paper took a quantitative approach to analyzing the impact of the U.S. Department of Housing and Urban Development’s (HUD’s) revised income calculations for metropolitan and nonmetropolitan areas for 2007. The update, or 2008 edition of the paper, serves to benchmark the recovery estimates from 2007 against the revised estimates from this year.

2007 was the first year that new area median income (AMI) calculations had been implemented using the American Community Survey data. There was a significant decrease in the calculated AMI across all counties in the United States. In the 2007 edition of the white paper, Novogradac & Company LLP estimated that more than 84.5 percent of the counties or similar areas experienced a drop in AMI.

The very-low income limit (VLI) is typically calculated as 50 percent of an area’s AMI. HUD uses a set of “hold-harmless” tests to prevent VLI from dropping as a result of decreases in AMI. Each county or similar area is run through various tests before its final VLI limit is determined. These tests are: state area median income, high housing cost, low housing cost, and the historical exception (also commonly referred to as the hold harmless exception). This policy is used in areas where income limits decreased, or didn’t rise above the prior held harmless levels, and is intended to prevent low-income housing tax credit (LIHTC) rents — and rents under other programs where HUD income limits are directly related to project revenues — from falling below the previous year’s levels.

The estimated median family income for the United States for fiscal year 2008 is \$61,500. HUD says the fiscal year 2008 median family income level is about 4 percent higher than the level for fiscal year 2007. Not all geographic areas, however, show an increase in the median family income. Again this year, HUD has not let current year income limits fall below income limits for the previous year. HUD implemented this policy in 637 of 2,043, or approximately 31 percent, of non-metropolitan areas. The hold harmless policy was also implemented in 190 out of 532 metropolitan areas for fiscal year 2008, or roughly 36 percent of metropolitan areas.

Under HUD’s hold harmless policy rents won’t rise until median family income levels increase above the hold harmless levels. This gap may take several years to close in many areas and, therefore, rent and income levels will likely remain flat for several years. In the meantime, owners and managers of LIHTC properties are keeping a close eye — closer than usual — on the operating budgets of their properties, which are developed and managed with relatively narrow financial margins, and which could face even greater financial pressure. If expenses grow while revenues remain flat some properties may eventually be unable to meet debt service.

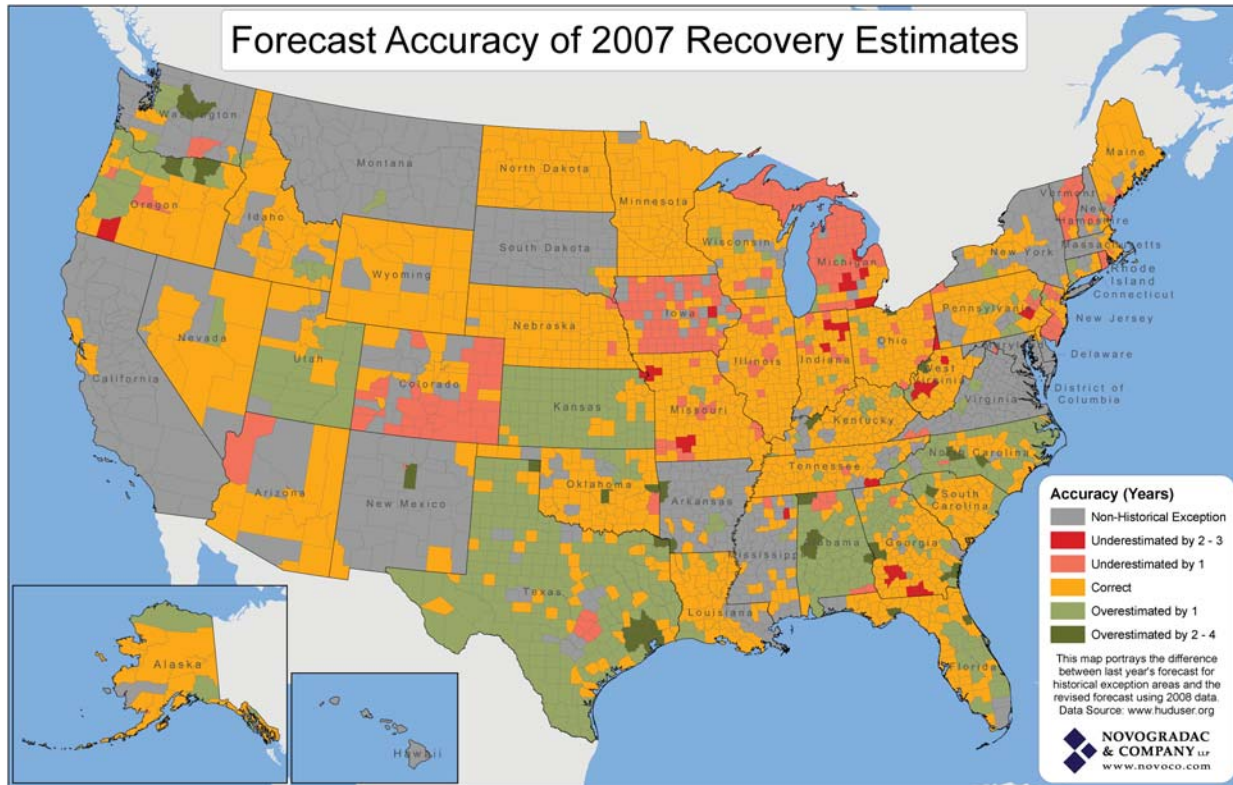
In some cases, the situation could be even worse. In most tax credit properties, allowable rents are reduced by an allowance for the cost of utilities paid for by tenants. As expenses rise, this utility allowance rises, and the amount of rent paid by the tenant actually falls.

It is interesting to note that in addition to the areas where income levels are frozen under the hold harmless policy,

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many areas fell under the state AMI exception, which provides that income limits are never set at less than the relevant state non-metropolitan AMI. In 2008, income limits in 850 non-metro counties and 47 metro areas were set at the state AMI. This number is more than twice that of 2007 when income limits for 237 non-metro areas and 24 metro areas were set at the state AMI level. However, initial analysis indicates that, overall, fewer areas' very low income numbers were adjusted in 2008 than in 2007.

One of the most significant findings of the update to the white paper involves the accuracy of the predicted recovery times in areas where rents were held flat. Last year, the conservative estimate presented in the white paper was that 1,172 areas — or about one-third — would recover within one year. A more optimistic estimate projected that 2,069 areas (or 60 percent) would recover within one year. The median estimate was that 1,598 areas would recover within one year. The actual number of areas that recovered within one year was 1,538 — an accuracy percentage of more than 96 percent. The map above illustrates the accuracy of the predictions set forth in the 2007 edition of the white paper.

Using the new data, the estimated recovery time for these areas is presented in the 2008 edition of "Effect of HUD's Revised Income Calculations on Housing Tax Credit Properties: How Long Until Qualifying Incomes & Tax Credits Rise." The 2008 edition provides a breakdown of these recovery estimates and a comparison to the original white paper. The 2008 edition, which includes access to an online database of the information on which the analysis was based, can be ordered online at [www.novoco.com/products](http://www.novoco.com/products). ♦

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