

2007 — The Year in Review

By Michael J. Novogradac, CPA

As 2007 draws to a close, it's time to take a look at the year's progress in efforts to produce and preserve low-income tax credit housing. No one can deny it's been a busy year in which legislation has been introduced and passed, regulations proposed, hearings held, letters written and concerns expressed. But despite the ramped-up activity on issues that have been on the table, some for several years, there was little decisive action in 2007.

Affordable Housing Trust Fund

In highlighting some of these actions, we'll look first the efforts to create an affordable housing trust fund. On June, 28, House Financial Services Committee Chairman Barney Frank, D-Mass., along with Reps. Maxine Waters, D-Calif, John McHugh, R-N.Y., and Jim Ramstad, R-Minn., introduced The National Affordable Housing Trust Fund bill that would produce, rehabilitate and preserve 1.5 million housing units over the next 10 years. H.R. 2895 would initially allocate between \$800 million and \$1 billion annually to states and local communities without increasing government spending or the federal deficit. The Trust Fund would be funded with monies from H.R. 1427, the House-passed government-sponsored enterprises (GSE) reform bill, and H.R. 1852, the FHA modernization bill, and any other sources of funds subsequently identified.

The U.S. House of Representatives on October 10 approved legislation to create the fund, despite a presidential veto threat. The vote was 264-148, short of the two-thirds margin needed to override a veto. In warning of the veto, the Office of Management and Budget (OMB) said the administration "strongly supports" providing federal assistance to needy families but "strongly opposes" using FHA and GSA revenues for the housing trust fund. A move to establish a national affordable housing grant fund within the HOME program was defeated 257-163.

For advocates, however, the victory in the House was a milestone moment for the families, elderly and disabled who cannot afford a safe and healthy home. Frank, calling the growing shortage of affordable housing one of the most serious social and

economic problems facing our country, said, "Given our severely constrained fiscal realities, we are today doing the best we can to address this – creating a low income housing trust fund that will be paid for in ways that do not draw from federal tax revenues." The bill was referred to the Senate on October 15, read twice and referred to the Committee on Banking, Housing and Urban Affairs.

Utility Allowance and Qualified Contract Regulations

Several hearings were held in 2007 that would bring change to the LIHTC landscape in the form of guidelines that the industry has sought for some time. Two of the more recent and significant hearings addressed the IRS' proposed regulations regarding utility allowances and qualified contracts.

On June 18, 2007, the Internal Revenue Service (IRS) issued its long-awaited proposed regulations that would provide new options for estimating tenant utility costs. Subsequently, a hearing on utility allowances was held on October 9, and the IRS heard from several affordable housing representatives who for the most part praised the IRS' efforts to adjust the gross unit rent when a low-income housing resident pays for utilities.

Current IRS rules require tax credit rents to include a utility allowance for resident-paid utilities; however, it is widely agreed that the methods used to estimate the resident's utility cost tend to overestimate them and thus, reduce the gross rent received by owners.

When the proposed regulations were issued last summer, Jim Arbury, National Multi Housing Council/National Apartment Association (NMHC/NAA) senior vice president of government affairs, called the IRS-approved methods to calculate utility allowances "outdated," and characterized them as a threat to the financial viability of many existing properties and discouraging to investors who wanted to undertake new projects. "We commend the IRS for stepping forward to correct this problem," he said at that time.

The proposed regulations would allow state

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LIHTC allocating agencies to provide utility estimates; allow property owners to submit data from their utility company or use the data from a new HUD utility modeling program; provide a grace period before rents can be adjusted during the initial stabilization period; require rents to remain unadjusted for a period of one-year, or until the property has achieved 90 percent occupancy for 90 consecutive days, whichever comes first.

The National Affordable Housing Management Association's (NAHMA) voiced its concerns with the proposed utility allowance regulations, focusing on the difficulty owners and managers would face in obtaining cost estimates from each of many utility providers in order to calculate utility allowances; many states and communities have multiple providers in the electric and gas markets. Michelle Norris, NAHMA's president, also called on the IRS to allow owners to time their utility allowance adjustments to their annual rent certifications.

Several commenters asked the IRS to consider allowing developers, owners and property managers to use the services of state-certified engineers who would derive utility allowance adjustments by applying consumption and analysis models. Paul Emrath, assistant vice president of housing policy research for the National Association of Home Builders (NAHB), was joined by David Cardwell, vice president of capital markets, and Ronald Nickson, vice president of building codes, both of the National Multi Housing Council (NMHC), in calling for the use of such energy analysis models. Emrath said current methods of calculating utility allowances do not account for energy efficiencies in newer LIHTC buildings whose construction often uses more efficient design and appliances and, therefore, require significant up-front costs for builders and developers. If utility allowances are calculated too high, he said, these costs are not recouped.

David Rammner, director of government relations for the National Housing Law Project (NHLP), called for transparency in utility allowance regulations so that a tenant can bring an objection to a neutral third party.

Qualified Contract Regulations

On October 15, Richard Goldstein, general counsel for the Affordable Housing Tax Credit Coalition, Miriam Colon, New York City Department of

Housing Preservation and Development, Scott Kline of the National Housing Trust/Enterprise Preservation Corp. and Rammner, presented testimony on proposed regulations to clarify a formula for determining the minimum purchase price of low-income housing under a qualified contract.

The hearing followed the June 19 Treasury Department release of its proposed regulations providing specific guidance on the qualified contract provisions of Internal Revenue Code §42. Under the statute, the owner of section 42 properties after complying with restricted rent and income limits for 15 years and the extended use agreement for an additional 15 years, can either (1) dispose of the property at the statutorily determined qualified contract price, or (2) transition the property to market rate over three years. In brief, the qualified contract allows the owner of an affordable housing property to request that the state housing credit agency find a buyer for the property at the statutorily determined qualified contract price. The state housing credit agency has one year to find a buyer for the property. In the event that a buyer cannot be located, the property can transition to market-rate housing over three years.

Issues raised by the commenters, as well as written submissions from others in the industry, included questions on definitions and calls for explanations or clarifications, among others, of a bona fide contract, cash distributions from the project, adjusted basis of the project, how certain items should be calculated, accounting for debt allocable to refinancing, how to control for buyer default on the qualified contract and valuation of the non-low-income portion of the building.

Rammner and Kline both noted that including land value in determining the minimum sales price would flaw the formula because the tax code on the qualified contract considers only the housing and not the land and thus the regulations would not reflect fair market value. Kline called for more attention to the appraisal process and more specific guidelines. Goldstein, a partner at Nixon Peabody LLP, recommended binding arbitration to resolve disputes.

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The National Council of State Housing Agencies (NCSHA) in its written comments recommended that state housing agencies be given the ability to set different submission requirements for qualified contract requests. The Affordable Housing Tax Credit Coalition (AHTCC) commented that it “believes strongly that housing credit agencies have no authority under Section 42(h)(6)(F) or otherwise to impose a different formula for computing the qualified contract price and no authority to impose a fair market value limitation on such price.”

Updated regulations are expected in 2008.

Modernization Bill

In early November efforts to move the low-income housing tax credit modernization bill in the House were set back when the House Ways and Means Committee revealed that its 2007 calendar could not accommodate a hearing and a bill could not be completed this year. The delay in the House hearing and drafting of a bill was a great disappointment to the LIHTC community. After the Democrats took control of the House, there were great expectations as the LIHTC community was led to believe that a hearing would be held in early summer 2007. But as early summer approached the hearing was not scheduled.

As each month passed, delays continued. The good news is that drafting of the bill will continue, even though the committee will not address the bill until 2008. The Housing Advisory Group (HAG) and others in the affordable housing industry have been working on this legislation that would modernize the LIHTC and U.S. Department of Housing and Urban Development (HUD) housing production programs. Sen. Maria Cantwell, D-Wash., a member of the Senate Finance Committee is preparing to introduce comparable legislation in the Senate. More on this legislation effort will be featured in the Washington Wire in the January issue of the Novogradac Journal of Tax Credit Housing, the new Novogradac & Company LLP monthly publication that combines the *LIHTC Monthly Report*, the *Housing Bond Report* and *The Valuation Report*.

While 2007 was a year of action on a variety of issues that the industry has advocated, in some cases for many years, it was a year of few final decisions. It is our hope and expectation that 2008 will see the fruition of actions begun in 2007, producing more results so that we in the affordable housing industry will be better able to produce and preserve the housing that the nation needs so desperately. While we have hope, we also have great trepidation, as 2008 is an election year, and we expect partisan battles to heighten. ❖