PROVIDE A NEIGHBORHOOD HOMES CREDIT

Current Law

There are no Federal tax provisions that directly support building or renovating affordable owner-occupied housing or that cover a development or financing gap for such housing. The low-income housing credit supports construction and rehabilitation of affordable housing for low-income renters. The mortgage interest deduction, tax-exempt housing bonds, and mortgage credit certificates assist homeowners by reducing the after-tax costs of their mortgage payments, but this support is not directed at addressing development cost gaps for affordable owner-occupied housing.

Reasons for Change

In neighborhoods where homes are in poor condition, property values are often too low to support new construction or substantial renovation of existing properties. The lack of move-in-ready homes makes it difficult to attract or retain homebuyers in these areas. A subsidy for home builders and homeowners seeking to rehabilitate these homes can encourage residential development in these neighborhoods. If targeted at homes sold to (or being rehabilitated by) owner-occupants, the subsidy can encourage further improvements to these areas, as owner-occupants generally have greater long-term interest in their neighborhoods than renters.

Proposal

The proposal would create a new allocated tax credit, the neighborhood homes credit (NHC), to encourage (a) new construction for sale, (b) substantial rehabilitation for sale, and (c) substantial rehabilitation by existing homeowners who will remain in their communities. The credit would be allocated through each State's Neighborhood Homes Credit Agency for projects meeting criteria described below.

Neighborhood Homes Credit Agencies (NHCAs): Each State would create or designate an NHCA to allocate potential NHCs to project sponsors – i.e., individuals or entities that organize the project. Sponsors seeking NHCs would apply to their State NHCA. The NHCAs would evaluate the applications and choose those deemed best suited to achieving the goals of the program. Furthermore, the NHCA would be responsible for monitoring compliance with all provisions governing NHCs and for reporting violations to the IRS. NHCAs would also set standards for developer fees, building quality (including all local criteria for habitability and safety), and development costs.

Allocation to States, U.S. territories, and the District of Columbia (collectively, States): Each State would have a specified amount of potential NHCs to allocate each year. For 2024 each State could allocate the greater of $8 million or the product of $6 times the State's population. The amounts would be indexed for inflation for subsequent years. States would be able to carry forward any unallocated potential NHCs for up to three years.

Eligibility criteria for NHC residences: Sponsors would only be eligible for NHCs if the residences they were constructing or rehabilitating met the following criteria:

1. The project must be a single-family home (including homes with up to four dwelling units), a condominium, or a residence in a housing cooperative.

2. The project must be in an NHC neighborhood (defined below).

3. The project must be sold, or in the case of owner-rehabilitation projects completed, within five years of the NHCA allocation of the credit.

4. After construction or rehabilitation, the home must be owned by an occupant who is an NHC-qualified owner (defined below).

Eligibility criteria for NHC neighborhoods: An NHC neighborhood is a census tract that meets at least one the following criteria:

1. Has median family income not exceeding 80 percent of the area/State median income, has a poverty rate not less than 130 percent of the area/State poverty rate, and has a median value for owner-occupied homes not exceeding the area/State median value;

2. Has median family income not exceeding area/State median income, is located in a city with a poverty rate of at least 150 percent of the area/State poverty rate and a population of at least 50,000, and has a median value for owner-occupied homes not exceeding 80 percent of the area/State median value;

3. Has median family income not exceeding area/State median income, is located in a non-metropolitan county, and has been designated by a NHCA; or

4. Is located in a disaster area.

Eligibility criteria for qualifying owners: An NHC-qualified owner is someone who will use the home as their primary residence, whose household income does not exceed 140 percent of area/State median income, and who, in the case of a sale, is not related to the seller.

Determination of credit amount: In general, the credit amount would increase as development costs increase and decrease as sales proceeds (or owner payments, in the case of rehabilitation for current homeowners) increase. In a determination of the credit amount, construction costs would count only to the extent they are incurred after a NHCA has allocated potential NHCs to the project, and acquisition costs for land and buildings would count only to the extent they are incurred not more than three years prior to such an allocation. For home sales, the credit would be limited to no more than 35 percent of the lesser of development costs and 80 percent of the national median sales price for new homes. The credit amount would smoothly phase out such that it would be zero when sales proceeds are five times area median family income. (An alternative phase out would apply in the case of residences with more than one dwelling unit.) A taxpayer would always be better off obtaining a higher sales price, and a small increase in sales price would not trigger a disproportionate loss of credits. In the case of a rehabilitation of an owner-occupied residence, the credit would not exceed the lesser of $50,000 and 50 percent of rehabilitation costs. Similar to the case of a home sale, a taxpayer would always be better off obtaining a higher owner payment for home rehabilitations, and a small increase in owner payments would not trigger a disproportionate loss of credits.

Treatment of losses: If a taxpayer sells or rehabilitates a home for a loss (which will generally be the case), the credit will not be considered compensation for that loss for purposes of determining whether the loss is deductible.

Return of unused credits: If any credits allocated to a project are unused five years after the NHCA allocation, they are returned to the pool of potential credits for the NHCA to re-allocate. As with other potential credits that the NHCA receives for a year, these returned credits may be carried forward for up to three years.

Timing of owner occupancy: A taxpayer may claim NHCs only after construction and inspection are complete and the home is occupied by an NHC-qualified owner. If, within five years of the date of qualification for the NHC, the purchasing or rehabilitating owner-occupant sells or rents the home, there may be NHC-related financial consequences to the owner-occupant. In the case of a sale, up to 50 percent of the gain from the sale would have to be paid to the NHCA. In the case of renting, during the five-year period expenses with respect to renting would not be deductible against Federal income taxes.

Implementation and reporting: The Secretary and her delegates (Secretary) would be given authority to prescribe rules to implement this provision. NHCAs would be required to submit an annual report to the Secretary specifying the amount of potential NHCs allocated to each project for the previous year, information on each NHC residence completed in the previous year, and such other information as the Secretary may require.

The proposal would be effective for taxable years beginning after December 31, 2023.