

BOARD AGENDA ITEM: 8.D.(1)

DATE: August 28, 2008

SUBJECT: Approval, Implementation Plan, The Housing and Economic Recovery Act of 2008 (HR 3221), Low Income Housing Tax Credit Program

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BACKGROUND:

The Federal Tax Reform Act of 1986 created the Housing Tax Credit Program (HTC) for qualified residential rental properties. The HTC Program is the principal federal subsidy contained within the tax law for acquisition/substantial rehabilitation and new construction of low-income rental housing.

Section 42 of the Internal Revenue Code (IRC), requires that state allocating agencies develop an Allocation Plan for the distribution of the tax credit within their jurisdiction. The Allocation Plan is subject to modification or amendment to ensure the provisions conform to the changing requirements of the IRC and applicable state statute. The Board issued final approval to the Agency's 2009 Qualified Allocation Plan (QAP) at its meeting on March 27, 2008.

On July 30, 2008, Congress enacted the Housing and Economic Recovery Act of 2008 (HR 3221) (the "Act"). The Act results in a wide variety of important IRC revisions resulting in the most significant changes to the HTC program since its inception.

Three Key Revisions of the Act

Three key revisions of the Act are:

1. An increase of twenty cents to the Minnesota per capita housing tax credit allocation for each of years 2008 and 2009, resulting in approximately \$1,000,000 additional credit cap to the state,
2. Setting the 70 percent present value credit (“9 percent”) applicable percentage at a full fixed 9 percent instead of a lesser varying rate, and
3. Authorizing state housing credit agencies to award a 30 percent “basis boost” to buildings that are determined to need the boost to be financially feasible. Recommendations for the criteria to be used in applying this boost follow in this report. All of these revisions will greatly enhance the value of the credit as a capital source in the production of affordable housing.

Temporary Increase to Per Development Credit Limit

The implementation of the above tools, although greatly beneficial to the financial feasibility of the developments, will potentially cause several to exceed the current \$780,000 per development credit limit. Staff believes that the most effective way to accommodate this condition is to temporarily amend the per development cap for the 2008 and 2009 credit program years to a not-to-exceed \$1,000,000 limit. Developments exceeding this \$1,000,000 limit would require Board approval of a cap waiver on an individual basis as provided for in the QAP.

2009 Round 1

The immediacy of the Act’s July 30, 2008, effective date necessitates Minnesota Housing Finance Agency (Agency) to quickly and strategically determine an approach to implementation. The Agency’s operation under an HTC “forward selection” principal and under a review process directly related to the Agency’s Super RFP application processing, creates a more complex environment in which to implement the provisions of the Act. For example, the Agency has already allocated most of its 2008 tax credits in calendar year 2007 with balances funded in early 2008. The Agency currently has completed a significant portion of the required underwriting and evaluation of its 2009 Round 1 tax credit applications submitted in June, 2008. Funding decisions made on this round would typically absorb most of the 2009 tax credits.

In an effort to preserve the progress made to-date and avoid interruption in evaluating 2009, Round 1 applications, staff believes it is most effective to continue evaluations applying the following recommendations to the 2009 Round 1 applications with the intention of formally amending the QAP to implement all of the Act’s provisions prior to the 2009 Round 2 application submission date. This will give applicants the opportunity to apply to 2009 Round 2 under the amended QAP, having incorporated all of the legislative changes, and to maintain the existing tax credit program’s application submission/allocation schedule for 2009 Round 1.

According to the QAP, Article 14, *Amendments to the Qualified Allocation Plan*, “the QAP is subject to modification or amendment at any time to ensure that the provisions conform to the requirements of the Code and applicable Minnesota law. The Agency may also make non-substantive changes to the QAP to update population changes, dates, or minor updating. Written explanation will be made available to the general public for any allocation of a housing credit dollar amount that is not made in accordance with the Agency’s established priorities and selection criteria”. Section 42(m)(1)(A)(iv) of the IRC also provides for this written explanation provision.

Staff believes that the provisions of Article 14 allow the Agency to continue to evaluate and make selection decisions on 2009 Round 1 applications and allow applicants the opportunity to apply to 2009 Round 2, under an amended QAP.

State Designated 30 Percent Basis Boost Criteria:

It is the goal of the Agency to optimize the use of all available sources of funding for multifamily developments; including private investor equity, amortizing loans and deferred loans; to produce the maximum number of affordable rental units in the most sustainable, quality, cost effective and geographically diverse developments possible which meet the Agency’s strategic priorities. Consistent with this goal, the following criteria will be used to determine if, when, and in what amount, the Agency will provide a basis boost for housing tax credit developments on a building by building basis to obtain financial feasibility.

- Development must meet state identified housing priorities as evidenced by competitive tax credit score.
- Funding gaps remain for top ranking tax credit developments.
- Credits allocated in connection with the basis boost shall be no more than needed to achieve financial feasibility.

2008 Credit Program Year and 2008 Carryover Processing

Several of the Act’s effective dates not only impact the 2009 HTC program, but also reach back and impact the 2008 HTC program. Following the conclusion of Round 2 of a program year, it is typical for the majority of Agency tax credit developments to pursue a carryover allocation versus proceeding directly to placed-in-service. Carryover process requires that the owner of a selected tax credit development make formal application to the Agency for a carryover review. The carryover review provides the Agency the opportunity to perform a more current underwriting assessment and to provide additional tax credits based on need and financial feasibility.

The issuance of tax credits based on need and financial feasibility may also be issued by selecting a development from the Waiting List established at the time the Board approves of selections for Round 2 of a program year. The Waiting List for 2008 was approved by the Board at its meeting on April 24, 2008. According to the 2008 QAP, developments from this list may also be considered for receipt of the additional 2008 credits made available by the Act.

In limited cases, a tax credit development, obligated to an imminent closing date and needing additional credits due to market conditions, may be unable to take advantage of the carryover or waiting list process to acquire the credits due to timing constraints. Allowing Agency discretion to award additional credits as necessary outside of the carryover or the waiting list process is recommended to allow a development to achieve financial feasibility and to meet its closing obligation.

Staff believes the most effective way to implement the Act's provisions affecting the 2008 HTC program is to implement them through the carryover application and review process, where appropriate through use of the 2008 Waiting List and through use of discretionary processing as necessary to allow a development to achieve financial feasibility and progress to closing.

A more detailed explanation of the proposed changes affecting the processing of 2009 Round 1, the 2008 Program year and its Carryover process, and the amendment to the 2009 QAP will be made available to the public for review and comment prior to the October 29, 2008 Public Hearing. Staff will review all comments and, as appropriate, consider incorporation into the QAP. The Board will review the preliminary Amended 2009 HTC QAP and Procedural Manual at its October 23, 2008 Board meeting the final Amended 2009 HTC QAP and Procedural Manual at its December 18, 2008 Board meeting. Upon obtaining the final Board approval of the Amended 2009 HTC QAP, it will be forwarded to the Governor's Office for approval and then posted to the Agency website.

IMPLEMENTATION PLAN:

The following are staff's recommendations for the implementation plan:

2009 Round 2 Applications

- Hold formal process including public hearing to address provisions of the Act and amend the 2009 QAP, HTC Program Manual and related program documents. Obtain preliminary and final Board approval on the Amended 2009 QAP prior to staff processing 2009 Round 2 tax credit applications.

2009 Round 1 Applications

- Continue standard evaluation of the 2009 Round 1 applications along established timelines and incorporate the following items.
- Allocate additional 2009 twenty cent per capita increase.
- Apply the 9 percent applicable percentage to developments.
- Apply the 30 percent boost according to the criteria defined in this report.
- Temporarily amend the per development cap not-to-exceed \$1,000,000.
- Adjust applications as appropriate to recognize changes in the IRC definition of Federally Subsidized and allow use of the 9 percent credit where supported by the application.

2008 Additional Volume Cap and 2008 Carryover Applications

- Allocate the additional 2008 per capita volume cap at carryover for 2008 projects by applying the 9 percent applicable percentage for projects requiring additional credits at carryover and as appropriate by use of the 2008 Waiting List.
- Apply the 30 percent basis boost according to the criteria defined in this report.
- Temporarily amend the per development cap not-to-exceed \$1,000,000.
- For developments needing additional credits due to market conditions, allow Agency discretion to apply the above options outside of the carryover or the waiting list process to projects as necessary to achieve financial feasibility and progress to closing.

TIMETABLE:

October 23, 2008	Board Approval - Preliminary Amended 2009 QAP
October 29, 2008	Public Hearing on Proposed Amended 2009 QAP
December 18, 2008	Board approval – Final Amended 2009 QAP
Early January, 2009	Finalize and Distribute Amended 2009 QAP
February 5, 2009	2009 Round 2 Application Deadline

MEETING AGENCY PRIORITIES:

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| <input checked="" type="checkbox"/> End Long-Term Homelessness | <input checked="" type="checkbox"/> Finance New Affordable Housing Opportunities |
| <input type="checkbox"/> Increase Emerging Market Homeownership | <input checked="" type="checkbox"/> Preserve Existing Affordable Housing |

RECOMMENDATION:

Staff recommends the adoption of a motion to approve the Implementation Plan as described in this report to implement changes to the 2008 and 2009 Housing Tax Credit Programs to accommodate the provisions of The Housing and Economic Recovery Act of 2008.