


Anker Heegaard  
The Compass Group



**HOME + LIHTC**

...effectively use HOME and LIHTC together given today's market conditions and provide insight on key regulatory issues when combining the two sources.



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HOME + LIHTC  
**Topics**

- HOME Basics
- LIHTC Basics
- Combining HOME + LIHTC
  - Concepts
  - Development Finance / Underwriting
  - Monitoring & Asset Management
  - Preservation & Exit Considerations



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HOME Basics  
**Max HOME \$\$**

- Lesser of amount represented by
  - 'Fair Share'
  - 221(d)(3) limits
  - Actual gap



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HOME Basics

## Fixed and Floating Units

- Method of managing HOME unit mix varies depending on whether units fixed or floating:
  - Fixed projects only worry about HOME assisted units – all other units not considered
  - Floating projects concerned with proportion of HOME units to total units
    - Uses concept of “next available unit”
    - Necessary method if project has LIHTC but not 100%
    - Example: if HOME unit occupied by over income household at recertification, next vacant market unit becomes a HOME unit
- Rules for treating over income HOME tenant rent also different fixed v. floating



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HOME Basics

## High and Low HOME Rents

- Initial rent structure established at time of project commitment
- HOME rents
  - High HOME and Low HOME rent limit
    - Published by HUD by geographic area
  - Actual unit rents (as reflected by the lease) can be less but not more than HOME limits
    - Rents not usually set as a percentage of individual household income
  - Special provision for low HOME units with project based assistance



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HOME Basics

## Income Restrictions

- At *Initial Occupancy*
  - High-HOME  $\leq 80\%$  AMI
  - Low-HOME  $\leq 50\%$  AMI
- Incomes may rise after move-in; rules apply to maintaining the mix.
- Households can never be evicted for income increases.



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HOME Basics

## Recourse and Recapture

- Approx. 15% of projects can't get to year-20
- Written agreement should provide options to PJ
- Deed-restricted affordability  
\_\_\_\_\_ repays HUD if affordability is not achievable



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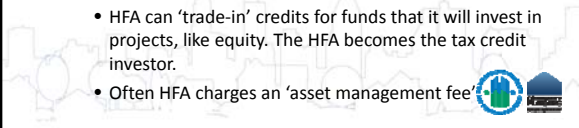
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LIHTC Basics

## Types of Programs

- 9% and 4% LIHTCs
  - More about this in a sec
- TCAP
  - Grants/Loans from HFA to replace equity lost to pricing crisis. Often soft 2nds, 3rds
- §1602 'Exchange'
  - HFA can 'trade-in' credits for funds that it will invest in projects, like equity. The HFA becomes the tax credit investor.
  - Often HFA charges an 'asset management fee'



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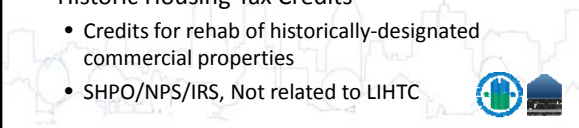
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LIHTC Basics

## Types of Programs, Cont'd

- State Housing Tax Credits
  - Some states (not all) provide a credit on investors' state income taxes
  - Good only for investors in that state
  - Worth less (state taxes are a deduction on federal)
- Historic Housing Tax Credits
  - Credits for rehab of historically-designated commercial properties
  - SHPO/NPS/IRS, Not related to LIHTC



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LIHTC Basics

## Explaining Credits and Equity

- HFA allocates 10 years of federal low-income housing tax credits to project
- Investor buys 10 years of credits - project required to comply for 15 years
- \$100K in *annual* credits is \$1,000,000 in total tax reduction.
- May claim tax credits if (a) has tax liability, and (b) project is in compliance.
- \$1 Credit is \$1 reduction in taxes
- Credits are a reduction of expenses (taxes)



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LIHTC Basics

## Calculating Equity

$$\begin{array}{l} \text{Eligible Basis} \\ \times \\ \text{Basis Boost} \\ \times \\ \text{Applicable Fraction} \\ \times \\ \text{Credit Percentage} \\ \times \\ 10 \text{ (Years)} \\ \times \\ \text{Price / Credit} \\ \times \\ \text{LP Share} \\ = \\ \text{Equity} \end{array}$$


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LIHTC Basics

## Key Concepts

- Credits/Equity not related to depth of affordability
- Credits/Equity not related to length of affordability
- Only owner (LP Investor) may claim LIHTCs



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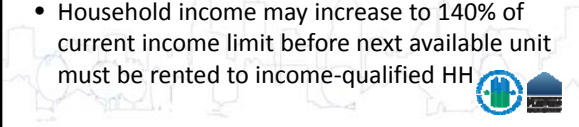
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LIHTC Basics

## Income Restrictions & Targeting

- LIHTC 20/50 or 40/60 *minimum*
- Maintain first-year applicable fraction
- Low-HOME generally serve as LIHTC
- High-HOME serve as LIHTC with lesser income limit (LIHTC) and lesser rent (HOME or LIHTC)
- Household income may increase to 140% of current income limit before next available unit must be rented to income-qualified HH



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LIHTC Basics

## Recourse and Recapture

- IRS HFA partnership
- Investor consequences become developer consequences
- Initial occupancy determines applicable fraction and max credits over ten years
- Maintain required applicable fraction, or else

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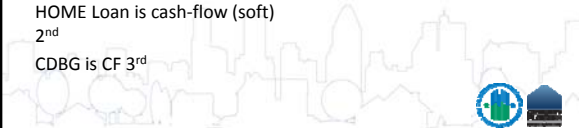
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Combining HOME + LIHTC: Concepts

## Typical 9% LIHTC Project

**50-unit New Construction**  
 \$12M TDC  
 100% Applicable Fraction  
 50 LIHTC units at 60% AMI  
 10 HOME (2 low- and 8 high-HOME Units)  
 HOME Loan is cash-flow (soft)  
 2<sup>nd</sup>  
 CDBG is CF 3<sup>rd</sup>

Category	Percentage
HOME	15%
9% Equity	60%
1st Mort	23%
DDF	6%
CDBG	6%



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Combining HOME + LIHTC: Concepts

## Typical 4% LIHTC Project

**50-unit Acquisition-Rehab**

- \$6.5M TDC
- 100% Applicable Fraction
- 50 LIHTC units at 60% AMI
- 10 HOME units (2 low- and 8 high-HOME)
- HOME Loan is cash-flow (soft) 2<sup>nd</sup>
- CDBG is CF 3<sup>rd</sup>

Source	Value
HOME	1.5
4% Equity	1.4
1st Mort	2.3
DDF	0.6
CDBG	0.7

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Combining HOME + LIHTC: Concepts

## Periods of Affordability

- **HOME** affordability period is based on \$/unit and type of investment
  - Acquisition/Rehab
    - <\$15K/unit = 5 Years
    - \$15K - \$40K/unit = 10 Years
    - >\$40K/unit = 15 Years
  - New Construction
    - Any Amount = 20 Years
- **LIHTC** Use Restrictions have 2 stages:
  - Initial Period of Affordability
  - Extended Period of Affordability

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Combining HOME + LIHTC: Concepts

## Periods of Affordability

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Combining HOME + LIHTC: Concepts

### Most Restrictive Rule Applies

- Lower income limit
- Lower rent limit
- Greater frequency



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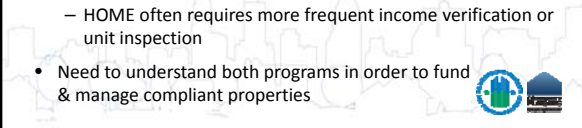
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Combining HOME + LIHTC: Concepts

### HOME Who?

- Key in HOME & LIHTC projects:
  - Balance needs/interests of all parties -- while complying with both sets of rules, most restrictive applies
- Common HOME & LIHTC issue: Owners comply with LIHTC & forget about HOME
  - HOME rents & income limits may be more restrictive
  - HOME affordability period is often longer than LIHTC
  - HOME often requires more frequent income verification or unit inspection
- Need to understand both programs in order to fund & manage compliant properties



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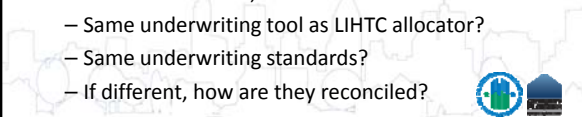
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Combining HOME + LIHTC: Development Finance

### Process Coordination

- Timing of HOME, LIHTC awards and contingencies
  - HOME, contingent on award of credits?
  - Credits, contingent on award of HOME?
- Applications
  - Same information, or different?
  - Same underwriting tool as LIHTC allocator?
  - Same underwriting standards?
  - If different, how are they reconciled?



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Combining HOME + LIHTC: Development Finance

### About QAPs

- o Action Plan
- o Threshold requirements
- o Application format
- o Pools and points
- o HFA Fees (app & CM)
- o Developer Fees
- o Underwriting
- o Market analysis
- o Post-award
- o Placement in service
- o Reprocessing
- o Use agreement



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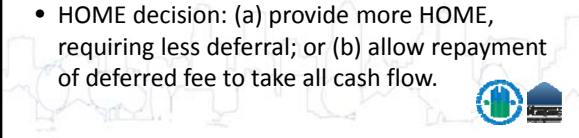
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Combining HOME + LIHTC: Development Finance

### About Developer Fees

- Rules, limits outlined in QAP
- 'Consulting' fees generally are developer fees
- Dev fee is included in LIHTC Basis, but deferred amount must be recoverable from cash flow (proforma)
- HOME decision: (a) provide more HOME, requiring less deferral; or (b) allow repayment of deferred fee to take all cash flow.



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Combining HOME + LIHTC: Development Finance

### Gap Financing Issues

- Underwriting is an estimate: SLR is a true-up.
- Fund during construction or at-completion
  - low-cost + high-risk vs. high-cost + low-risk
- Cash flow rights
- Deed-restricted U/A



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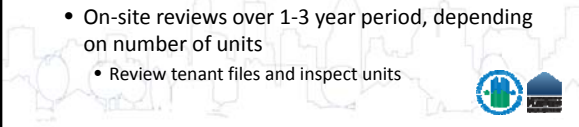
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Combining HOME + LIHTC: Monitoring & Asset Management

### Monitoring Requirements

- PJs must verify compliance with HOME requirements each year
  - Desk review for property condition includes pictures of property, maintenance records, work orders, and tenant complaints
  - Provide a reporting format!
  - On-site reviews over 1-3 year period, depending on number of units
    - Review tenant files and inspect units



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Combining HOME + LIHTC: Monitoring & Asset Management

### Other Requirements

- HOME triggers environmental review
- Housing Property Standards
- Frequency and sampling of inspections
- FH, Affirmative FH Marketing, ADA, Section 504



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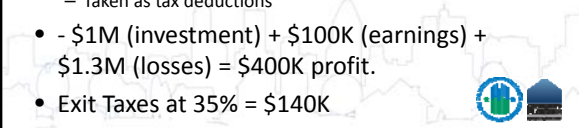
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Combining HOME + LIHTC: Preservation & Exit Considerations

### Exit Tax Primer

- Original Investment: \$1M
- Share of 15-Year Cash Flow: \$100K
  - Does not include depreciation and interest costs
- Losses over 15 years: (\$1.3M)
  - Includes depreciation and interest accrual
  - Taken as tax deductions
- - \$1M (investment) + \$100K (earnings) + \$1.3M (losses) = \$400K profit.
- Exit Taxes at 35% = \$140K



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Combining HOME + LIHTC: Preservation & Exit Considerations

### 'Qualified Contract'

- Sell for exit taxes plus existing debt to:
  - Government agencies;
  - Qualified nonprofit organizations;
  - Tenants; and
  - Resident management corporations.



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