

Low-Income Housing Tax Credit Frequently Asked Questions

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I. HOW THE HOUSING CREDIT WORKS

What is the Low-Income Housing Tax Credit (Housing Credit)?

The Housing Credit provides the private sector with an incentive to invest in affordable rental housing for low-income families. Since President Reagan signed it into law in 1986, the Housing Credit has financed the construction and preservation of more than 3 million affordable rental homes nationwide, at a rate of nearly 100,000 per year. Today it produces virtually all new affordable rental housing and is our primary tool for preserving existing affordable rental housing.

How does the Housing Credit work?

The federal government issues Housing Credit authority to states based on their populations. In 2018, states were to receive the greater of \$2.40 per capita or \$2.77 million. However, the change to a “chained” consumer price index (CPI) legislated in the Tax Cuts and Jobs Act, which will decrease inflation adjustments in Housing Credit and private activity bond allocations, is sure to affect the minimums small states receive. It is to be determined whether per capita rates will also be altered.

Each year, state allocating agencies establish criteria for awarding credits (known as a Qualified Allocation Plan, or QAP) that address the state’s local housing needs and priorities, subject to broad federal guidelines and after receiving public comment. Developers submit applications for credit authority through a highly competitive process; each year, allocating agencies receive applications requesting two to three times more Housing Credits than the agencies have to allocate. Housing Credits are then awarded to developers based on how well their proposed projects meet the criteria established in the QAP.

State allocating agencies underwrite every Housing Credit property to ensure that each development receives only the amount of Housing Credits necessary to ensure its financial feasibility, while avoiding over-subsidization. The agencies consider all sources and uses of funds, the length of the affordability period, the market price for tax credits, and the expected operating expenses to determine the Housing Credit amount for each property.

Developers exchange the ten-year stream of Housing Credits for up-front equity capital from investors. The equity capital enables the property to be financed with lower levels of debt, which makes it possible to offer apartments to low-income residents at rents they can afford. The annual credit percentage is determined by the type of development – there is a “9 percent” credit for new construction and substantial rehabilitation, and a “4 percent” credit for acquisition and rehabilitation, described in greater detail below.

At a minimum, at least 20 percent of the apartments in a Housing Credit property must be targeted to residents at or below 50 percent of area median income (AMI), or 40 percent of the apartments must be targeted to residents at or below 60 percent of AMI. The amount of Housing Credit authority for which the property is eligible depends on the proportion of the apartments in the property that are reserved for low-income households and rented at affordable rates. In practice, many developers target nearly all of the apartments in these properties to low-income tenants. The low-income residents pay 30 percent of the income threshold as rent.

It is only after the property is constructed, meets all federal requirements, and is occupied by income-eligible tenants paying affordable rents that an investor can begin claiming the tax credits. In the rare case that a property falls out of compliance at any time over the next fifteen years, credits are subject to recapture. The private sector, not taxpayers, bear the financial risk. The property is also subject to continued affordability restrictions enforced by the states for at least another 15 years, though many states impose even longer affordability periods.



What are Tax-Exempt Multifamily Housing Bonds (Housing Bonds)?

Multifamily Housing Bonds, a category of private activity bonds, are a tax-exempt financing tool issued by states and local governments to enable the acquisition, construction, and rehabilitation of multifamily housing for low-income renters. When 50 percent or more of a property is financed using multifamily Housing Bonds, that property becomes eligible to receive “4 percent” Housing Credits, which provide a shallower subsidy that is generally used for preservation and rehabilitation of existing properties. The 4 percent Credit is especially important to [recapitalizing existing public housing](#) through the Rental Assistance Demonstration (RAD) and preserving other federal investments through HUD and USDA rural rental housing. About half of all Housing Credit apartments produced each year are financed with “4 percent” Housing Credits and Housing Bonds.

Investors in multifamily Housing Bonds are willing to accept a lower yield than they would get on taxable bonds because the interest on the investment is exempt from federal income tax. The tax exemption allows developers to access debt at a lower interest rate than would be available with conventional financing. In 2018, states received the greater of \$105 per capita or \$311 million in private activity bond authority. However, as with the Housing Credit amounts, these may be revised down due to the shift to a chained CPI.

Like other Housing Credit properties, Housing Bond-financed Housing Credit developments must comply with the state’s allocation plan established in the QAP and with all other applicable Housing Credit program rules, including those related to income targeting and the affordability period.

Who does the Housing Credit serve?

In order to move into a Housing Credit development, residents must earn at or below 60 percent of AMI, but many Housing Credit developments serve much lower-income tenants. In fact, federal [tax credit statute](#) explicitly requires that each state’s QAP must give preference to “projects serving the lowest income tenants... for the longest period of time.” The most recent [HUD Housing Credit tenant study](#), released in 2017, found nearly half of all Housing Credit renters earn at or below 30 percent of AMI. Over four in five Housing Credit tenants (81.4 percent) are very low-income, meaning they have household incomes at or below 50 percent of AMI.

The Housing Credit also serves communities with particularly acute affordable housing needs, including [veterans](#), [seniors](#), [Native Americans](#), [people with disabilities](#), and [rural communities](#).

How do states provide oversight and prevent against fraud?

As directed by Congress, state allocating agencies are responsible for providing oversight of the Housing Credit program and working closely with the IRS to monitor project compliance. State agencies regularly conduct reviews of Housing Credit developments to inspect their physical and financial condition, certify their occupancy by qualified low-income residents, and ensure overall compliance with federal rules.

[A recent GAO study](#) of state agencies’ administration of the program found that states often go above and beyond the compliance monitoring responsibilities required of them by law. Multiple parties – both public and private – scrutinize each transaction from beginning to end, providing independent checks and balances, and tenants have full enforcement rights as well. Because the Housing Credit is a pay-for-performance credit that subjects equity investors to forfeiture of the tax benefits if properties are not in compliance with the law, Housing Credit properties are subject to vigilant private sector oversight. The record of states monitoring for compliance is strong and the affordable housing community supports all efforts to investigate and vigorously prosecute any violations.

How does the cost of building Housing Credit properties compare to other types of housing?

Comparing the cost of developing Housing Credit properties to market-rate multifamily housing is difficult for a number of reasons. For example, many single family home builders are able to take advantage of processes not available in any multifamily construction. Also, market-rate apartments often have greater efficiencies of scale due to placing more units on a site. Another crucial difference is the limited rent growth means less ability to replace components over time, creating an incentive to use higher-quality, longer-lasting materials. Despite all of these factors there is no evidence of Housing Credit properties costing more to build than other apartment complexes.

II. PROPOSALS TO STRENGTHEN AND EXPAND THE HOUSING CREDIT

What is the Affordable Housing Credit Improvement Act?

The Affordable Housing Credit Improvement Act is bipartisan legislation that would make numerous modifications to strengthen the Housing Credit by providing states with additional flexibility, making the financing of affordable housing more predictable and streamlined, facilitating Housing Credit development in challenging markets like rural and Native American communities, increasing the Housing Credit's ability to serve extremely low-income tenants, and supporting the preservation of existing affordable housing. The Senate version of the bill would also increase the annual Housing Credit allocation by 50 percent, phased in over five years, to make a meaningful step towards addressing our nation's severe shortage of affordable rental housing. The legislation was introduced in the Senate (S. 548) by Senator Maria Cantwell (D-WA) and Senate Finance Committee Chairman Orrin Hatch (R-UT), and in the House (H.R. 1661) by Representative Pat Tiberi (R-OH-12) and Ways and Means Committee Ranking Member Richard Neal (D-MA-1). With Rep. Tiberi leaving Congress at the beginning of 2018, Rep. Carlos Curbelo (R-FL-26) has assumed the role of lead House sponsor. Read a summary of the [Senate bill](#) and the [House bill](#).

Is there enough developer demand to absorb a significant increase in Housing Credits?

Yes. In 2015 – the most recent year for which data is available – state Housing Credit allocating agencies received applications requesting nearly three times their available Housing Credit authority. Many more potential applications for worthy developments are not submitted in light of the program's intense competition, suggesting the demand may be even broader.

What does the Housing Credit cost? What would it cost to expand it by 50 percent?

According to the congressional Joint Committee on Taxation (JCT), the Housing Credit currently costs roughly \$8 billion per year in foregone revenue, which includes the cost of credits that have been issued in prior years. The JCT estimates that a 50 percent expansion of the Housing Credit phased in over five years would cost roughly \$4.1 billion over the next ten years.

III. TAX REFORM'S IMPACT ON THE HOUSING CREDIT

How was the Housing Credit impacted by the Tax Cuts and Jobs Act?

On December 22, 2017 President Trump signed the "[Tax Cuts and Jobs Act](#)", H.R. 1, into law. The bill retained the Housing Credit as well as private-activity bonds, including multifamily Housing Bonds, which together finance virtually all affordable housing in the U.S. While it is critical that both core affordable housing financing tools remained intact, affordable housing will still be significantly impacted by the decrease in the top corporate tax rate from 35 to 21 percent, since a substantially lower corporate rate



reduces the value of the Housing Credit to investors, which decreases the amount of equity leveraged by the Housing Credit and ultimately overall production.

According to an [estimate by accounting firm Novogradac and Company.](#), the lower corporate rate and the change in the annual inflation factor for state Housing Credit allocations and private activity bonds volume caps will reduce our future supply of affordable homes by roughly 235,000 over the next ten years. The provision in the Affordable Housing Credit Improvement Act that would increase the Housing Credit allocation by 50 percent would offset this reduction.

The bill also created a base erosion and anti-abuse tax (BEAT), which will prevent certain U.S. corporations with a foreign parent or affiliate from receiving the full value of Housing Credit investments and may cause some Housing Credit investors to exit the market as well as offload a portion of their portfolio on the secondary market, further depressing investment and affordable housing production.

IV. THE NEED FOR THE HOUSING CREDIT

Why does the federal government need to invest in affordable housing?

America faces a severe and growing shortage of affordable rental housing. According to the 2017 “[State of the Nation’s Housing](#)” report from the Harvard Joint Center on Housing Studies (JCHS), more than a quarter of all renters – over 11 million households – are “severely rent burdened,” meaning they pay more than half of their income on rent. This creates financial instability and puts households at risk of eviction and homelessness in the face of unforeseen expenses. Fewer than one in four households eligible for federal housing assistance actually receives it, and there are scarce affordable options available in the private market.

The rental housing crisis will likely grow. Analysts expect an average of over 400,000 new households – many of whom will be low-income – to enter the rental housing market each year over the next decade. However, the rental housing industry develops less than this number of new rental homes each year, and mostly on the higher end of the market. Meanwhile, hundreds of thousands of affordable homes are lost each year to rent increases or obsolescence. According to [estimates from Enterprise Community Partners and JCHS](#), the number of severely rent burdened households will rise by 11 percent to 13.1 million in 2025, up from 11.8 million in 2015.

If there is so much demand for affordable housing, why doesn’t the private sector provide it?

The economics of rental housing development make it financially infeasible to build affordable housing without a subsidy such as the Housing Credit. The Housing Credit enables developers to raise equity capital from investors, which reduces the debt on properties, enabling lower rents. [According to JCHS](#), “to develop new apartments affordable to renter households with incomes equivalent to the full-time minimum wage, the construction costs would have to be 28 percent of the current average” – essentially making the financing impossible.

Why do we need to build affordable housing – can we just use housing vouchers?

The affordable housing crisis our nation faces is multifaceted, thus the Housing Credit and vouchers have been designed to play different and complementary roles in our nation’s response to that crisis. Indeed, the Housing Credit is often creatively combined with resources from other housing programs, including vouchers, to create better outcomes than is possible with just one affordable housing tool.

Vouchers are one of the primary vehicles for providing affordable housing choices to extremely low-income families, especially in low-cost housing markets. However, in many markets, voucher holders struggle to find apartments that are within HUD’s voucher payment standard and for which landlords will accept a



voucher as payment. This problem is especially acute in tight housing markets with low vacancy rates and rapidly escalating rents.

The Housing Credit, on the other hand, expands and preserves the affordable housing stock as a long-term community asset. It provides more apartment homes in areas that lack the affordable housing to meet community housing needs, and it supports the revitalization of communities through new investment. The Housing Credit also produces housing that incorporates targeted services, such as supportive housing for veterans, seniors, people with disabilities, the chronically homeless, and foster youth. Vouchers, though extremely important, are not designed to achieve these objectives. Likewise, it can be difficult for the Housing Credit, as a capital subsidy, to ensure that apartments are affordable to the very lowest income renters. Thus the Housing Credit and vouchers are often used together to address the spectrum of housing needs: the Housing Credit to build new and preserve existing affordable housing on a long-term basis, and the voucher to enable those already low-cost apartments to be more affordable to the lowest income tenants.

How does the Housing Credit impact surrounding neighborhoods?

The Housing Credit supports economic growth in communities and surrounding neighborhoods in a number of ways. The National Association of Home Builders (NAHB) [estimates](#) the Housing Credit adds \$9.1 billion in income to the economy and generates approximately \$3.5 billion in federal, state, and local taxes each year. Housing Credit development also supports jobs – roughly 1,130 for every 1,000 Housing Credit apartments developed, according to NAHB. This amounts to roughly 96,000 jobs per year, and more than 3.25 million since the program was created in 1986, across a diverse range of industries, including the manufacturing of lighting and heating equipment, lumber, concrete, and other products, as well as jobs in transportation, engineering, law, and real estate.

Conversely, a lack of affordable housing negatively impacts economies. [Research](#) shows that high rent burdens have priced out many workers from the most productive cities, resulting in 13.5 percent foregone GDP growth, a loss of roughly \$1.95 trillion, between 1964 and 2009.

Housing Credit development also positively impacts neighborhoods in need of renewal. About one-third of all Housing Credit properties help revitalize distressed communities. [Stanford University](#) research shows that Housing Credit investments improve property values and reduce poverty, crime, and racial and economic isolation, generating a variety of socio-economic opportunities for Housing Credit tenants and neighborhood residents.

How does the Housing Credit reduce spending on other government programs?

Housing Credit development can also help reduce government costs and save taxpayer money. A report from the Bipartisan Policy Center, “[Building the Case: Low-Income Housing Tax Credits and Health](#),” found that when affordable housing is coupled with supportive services, such as those targeted to assist the chronically homeless, those living with serious mental illness, and veterans, it can lead to significant public savings in shelter costs, the criminal justice system, and health care costs. [One study](#) of a pilot program in Ohio found that supportive housing saved an average of over \$6,000 a year per person in health care.