SQUIRE SANDERS | LEGAL COUNSEL WORLDWIDE

Affordable Housing and Community Development ALERT

July 2008 www.ssd.com

President to Sign the Housing and Economic Recovery Act of 2008

Congress passed and sent on July 26, 2008 to the President for his signature the Housing and Economic Recovery Act of 2008 (the Act), which will become effective on the date the President signs the bill (Effective Date).

The changes address (i) the availability and allocation of tax credits, (ii) project level structural, finance and cost issues and (iii) occupancy guidelines and modifications. Unless otherwise noted, the following provisions are effective for buildings placed in service after the Act's Effective Date. Because of the way that the Effective Date operates, there are some issues to be resolved and planning that needs to be done, some of which are described in this *Alert.* As issues arise, we will issue further *Affordable Housing Alerts* discussing them and planning considerations.

Tax Credit and Tax Exempt Bond Availability and Allocation

- **Tax Credit Ceiling Increase.** State credit ceilings for calendar years 2008 and 2009 will be increased by $0.20 per resident or, in the event of a state operating under the small state exception, by 10 percent.
- **Fixed Applicable Percentage (9 percent deals).** The applicable percentage for nonfederally subsidized projects placed in service after the Effective Date and prior to December 31, 2013 will be not less than 9 percent. This is a very significant and welcomed change for the industry. However, to the extent that a project qualifies for additional credits, state agencies must still provide additional

Save The Date: Exploring the 2008 Housing Act

On Tuesday, **August 5, 2008** Squire Sanders will host a teleconference webinar to discuss how the Low Income Housing Tax Credit Program is affected by the Housing and Economic Recovery Act of 2008. Participants will learn about immediate affordable housing opportunities in the Act. In addition, the program will be broadcast to our offices in Tampa, Cleveland, Columbus and Phoenix.
Event Details and Registration

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allocations to the project. Additional issues to be resolved include (i) whether projects that have "locked" the applicable percentage will be able to change to 9 percent, (ii) whether the state agencies will re-underwrite the amount of its tax credit allocation at the Form 8609 stage if the 9 percent rate is applicable and (iii), in multiple building projects, whether buildings placed in service before the Effective Date would have the pre-Act rate and buildings placed in service after the Effective Date would have the 9 percent rate (which appears to be the intent). The applicable percentage for "30 Percent Present Value" credits (which now are limited to bond financed projects) will continue to be set monthly.

- **Discretionary Basis Boost.** For 9 percent deals, state allocating agencies may designate specific buildings to receive a 30 percent basis boost for such buildings to be financially feasible. With falling prices and lower income targeting, this is a significant tool for the state agencies and the housing industry.
- **Private Activity Bond Volume Cap Increase.** The 2008 private activity bond volume cap is increased by $11 billion, to be used for housing bond issues (single or multifamily) and to be allocated among the states in the same manner as the current private activity volume cap allocation, which is based on population.
- **Repeal of AMT Limitation.** For (i) the interest on single family and multifamily housing bonds issued after the Effective Date, (ii) credits determined under Section 42 to the extent attributable to buildings placed in service after December 31, 2007 and (iii) credits determined under Section 47 to the extent attributable to rehabilitation expenditures incurred after December 31, 2007, the alternative minimum tax limitations (AMT) have been repealed. This is another positive change, as some traditional LIHTC and HTC investors and most institutional purchasers of housing bonds are presently subject to the AMT.
- **Additional Qualified Allocation Plan (QAP) Selection Criteria.** For allocations made after December 31, 2008 state allocating agencies must consider a project's energy efficiency and historic nature.

Project Level Structural, Finance and Cost Concerns

- **Modified 10-Year Rule for Federally and State-Assisted Buildings.** The 10-year rule will not apply for a Federally Assisted Building or a State-Assisted Building. In general, Federally Assisted Building means any building substantially assisted, financed or operated under Section 8 of the United

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States Housing Act of 1937, Section 221(d)(3), Section 221(d)(4) or Section 236 of the National Housing Act, Section 515 of the Housing Act of 1949 or any other housing program administered by HUD or the Rural Housing Service of the Department of Agriculture. The term State-Assisted Building means any building substantially assisted, financed or operated under any similar state law program.

- **Modification of the Definition of Related Persons.** The 10 percent attribution rule used to determine whether parties are related for purposes of determining whether an existing building qualifies for the low-income housing credit is repealed. Two persons are related for this purpose if they bear a relationship to each other specified in Sections 267(b) or 707(b)(1), which is a 50 percent related party rule, rather than the 10 percent rule.
- **Relief for Below Market Federal Loans.** Below market federal loans will not be considered federal subsidies. Furthermore, 9 percent projects receiving below market HOME loans are no longer prohibited from receiving the 30 percent basis boost.
- **Federal Grants Used for Eligible Basis Costs.** Eligible basis of a building does not include costs (eligible basis costs) financed with federal grant proceeds whether received before or during the compliance period. It is not clear yet whether federal grants used for non-eligible basis project costs (such as land) reduce eligible basis, although that could be the case.
- **Federal Grants Received During the Compliance Period.** No basis reduction is required for federally funded grants to enable the property to be rented to low-income tenants received during the compliance period if those grants do not otherwise increase the taxpayer's eligible basis in the building. The significance of this change is that federally funded rental, operating and interest reduction subsidies received during the compliance period will no longer reduce eligible basis.
- **Increased Rehabilitation Expenditure Minimums.** For buildings that receive credit or bond allocations after the Effective Date the minimum rehabilitation expenditures necessary to qualify for tax credits have been increased to the greater of (i) 20 percent of the adjusted basis of the building or (ii) $6,000 per unit. The $6,000 threshold will be increased annually by a cost of living adjuster for buildings placed in service after 2009.
- **Modification of 10 Percent Test.** Taxpayers have one year from the date of the allocation to incur 10 percent of the project's cost.

- **Bonding and Recapture Requirements Modified.** After the Effective Date, there is no longer a bonding requirement or a recapture event upon the disposition of a building or interest therein if it is reasonably expected that the building will continue to be operated as a qualified low-income building for the remainder of the compliance period. The statutory period for the assessment of a recapture event with regard to any reduction in qualified basis shall run for three years after the IRS is notified of such reduction in qualified basis. This modification is ***also*** effective for interests in buildings disposed of on or before the Effective Date if it is reasonably expected the buildings will remain qualified low-income buildings and the taxpayer elects this treatment in the manner prescribed by the IRS, in which case outstanding bonds may be retired and premiums may be saved.
- **Community Service Facility Eligibility for the Credit.** The size of the community service facility that may be included in qualified basis has been increased. The size of the community service facility may not exceed the sum of (1) 25 percent of the eligible basis of the project (for the first $15 million of eligible basis) and (2) 10 percent of any excess over $15 million of the eligible basis.
- **Recycling of Multifamily Housing Bonds.** Multifamily Housing Bonds may be refunded, and the proceeds used to finance a second project, under the following circumstances:
    1. Within six months of the receipt of repayment of the original bonds, the new bonds are issued;
    2. Within four years of the original bond's issuance, the new bonds are issued; and
    3. The maturity date of the new bonds is not later than 34 years after the date the original bond was issued.
- Since the new, "recycled" bonds would not have a private activity bond volume cap allocation, it appears that the state agency would need to provide an allocation of tax credits from the state's housing credit ceiling for the project to generate tax credits. The recycling of bonds amendment is applicable to repayments of loans received after the Effective Date.

Occupancy Guidelines and Modifications

- **Modifying Rural Area Median Gross Income.** For determinations made after the Effective Date, area median gross income limitations for projects in rural areas shall be measured by the greater of area median gross income or national nonmetropolitan median income. This new income targeting rule does not apply in the case of buildings that do not require a low-income housing credit allocation because they are substantially bond-financed.

- **Setting a Floor for Area Median Income.** For determinations made after 2008, any determination of area median gross income with respect to a project shall not be less than the immediately preceding year. HUD Hold Harmless projects face differing adjustment guidelines set forth more fully in the Act.
- **Eligibility of Foster Care Students.** For determinations made after the Effective Date, foster care students do not disqualify a unit for purposes of the student rule.
- **General Public Use Clarifications.** For a building placed in service before, on or after the Effective Date, a building will not be disqualified as a low-income building solely because occupancy of the building is restricted to, or preference is given to, individuals (a) with special needs, (b) who are members of a specified group under a federal program or state program or policy that supports housing for such a specified group or (c) who are involved in artistic or literary activities. The housing must still comply with applicable Fair Housing laws.
- **Military Allowances Excluded from Income.** For determinations made after the Effective Date and before January 1, 2012, and subject to additional qualifications set forth in the Act, for certain "qualified buildings" basic pay allowances provided by the military will be excluded for the purposes of determining income.
- **Bond Projects: Next Available Unit Rule, Student Credit Rules and SROs.** For determinations made after the Effective Date, projects financed with tax-exempt bonds and 4 percent credits, the next available unit rule is now applied on a building, not project, basis, the student credit rules will now mirror Section 42, and a unit will not fail to be deemed a residential unit merely because the unit is a single-room occupancy unit.
- **Section 8 Moderate Rehabilitation.** The prohibition on the use of credits with regard to a building to which Section 8 moderate rehabilitation assistance is provided has been repealed.
- **Income Recertifications.** After the Effective Date, income recertifications will not be required for 100 percent low-income projects.

The contents of this update are only a general summary of the Act and are not intended to serve as legal advice related to individual situations or as legal opinions concerning such situations. Counsel should be consulted for legal planning and advice.