

# MASSACHUSETTS COMPLIANCE GUIDE

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## Tax Credit Overview

*Credits at  
9% or 4%*

*Qualified  
Allocation Plan*

# INTRODUCTION

## 1.1 The Low-Income Housing Tax Credit (LIHTC)

The Tax Reform Act of 1986 established a tax credit for low-income rental housing that was directly based on the number of low-income tenants residing in the complex. Section 252 of the Act and Section 42 of the Internal Revenue Code (IRC) govern the Low-Income Housing Tax Credit (LIHTC) program that began in 1987 and received permanent authorization with the Omnibus Budget Reconciliation Act of 1993. The LIHTC program provides incentives for investment of equity capital in the development of affordable single family or multifamily rental housing. The credit is a dollar-for-dollar reduction in tax liability to investors in exchange for equity participation in the construction or acquisition and rehabilitation of rental housing units that will remain income and rent restricted for an extended period of time.

Credits are allocated based on a federal economic formula of approximately 9% for non-federally subsidized projects or below market rate interest deals, i.e., “conventional” developments, or approximately 4% if the project is federally subsidized or given an interest subsidy, such as tax-exempt bonds or Rural Development. The acquisition credit for existing buildings is approximately 4%. Developers may be for-profit or nonprofit. Investors, often represented by limited partnerships, apply the tax credits to reduce their income tax liabilities. Individuals can claim Credits up to the equivalent of a \$25,000 deduction. Corporate and bank investors have no limit on credit amount.

Massachusetts Qualified Allocation Plan (QAP) includes guidelines for the competitive ranking of applications. The amount of credits given to each state is based on population, indexed for inflation, with a minimum of \$2 million. Massachusetts may also have credits from previously unallocated or returned credits or by using the credits originally allocated to other states that failed to use them. The latter are referred to as credits from the “National Pool.”

Many recognize the tax credit’s influence on development, but its effect on management must also not be minimized. In order

## Purpose of the Manual

### *Reference for owners and managers*

*Note: Owners are encouraged to consider joining trade associations, participate in LIHTC trainings and keep themselves informed, aware and involved.*

for properties to qualify initially for the LIHTC and to continue to receive the credit without risk of recapture, management must at minimum, follow all tax credit regulations throughout a 15-year compliance period. From a management perspective, a thorough understanding of the tax regulations governing this program is imperative.

## 1.2 Purpose of the Tax Credit Compliance Manual

This manual is intended to help owners and managers of LIHTC projects in the State of Massachusetts fulfill their obligations in maintaining compliance pursuant to Section 42 of the IRC. The *General Explanation of the Tax Reform Act of 1986* (the “Blue Book”) [Section 8], IRC Section 42 regulations [Section 9], and excerpts from HUD Handbook 4350.3 REV-1 [Sections 22-24] are included in this manual for reference. Additional Massachusetts requirements for owners of a tax credit property are delineated in the Declaration of Restrictive Covenants for Low-Income Tax Credits.

### **Owners are responsible for being aware of all applicable federal and state rules and regulations that govern their properties.**

This manual focuses on the responsibilities of owners and managers of LIHTC projects from the beginning of the lease up period through the end of the compliance period. Subjects discussed include:

- Owner’s recordkeeping requirements
- Occupancy regulations
- Properly evaluating tenant income, assets and eligibility at move-in and at re-certification
- Determining the maximum gross rent for units
- Regulatory considerations when leasing vacant units

Sample forms, including those required for tenant certification procedures, are provided in Section 6 of this manual. “Required” forms are specified in the instructions for that section.

*Note: Rules and interpretations are subject to change. If you are not sure your information is up to date contact your allocating agency or their authorized agent.*

## Credit Period

*Credits given over a 10-year period*

*Note: Properties must be in continuous compliance with all rules and regulations to be eligible for credits.*

## Compliance Period

*Compliance required for 15 years. Plus an addition 15 years for extended use.*

In the State of Massachusetts, The Department of Housing and Community Development (DHCD) is the housing credit agency administering LIHTC allocations. DHCD is dedicated to providing quality affordable housing and is committed to helping owners of LIHTC properties understand and fulfill their obligations under the program. This manual is intended as a reference to promote a better understanding of the LIHTC program.

### 1.3 Credit Period

Once an LIHTC allocation has been finalized for a property, the tax credits can be claimed annually on a building-by-building basis over a 10-year period, beginning either with

- (a) the taxable year in which the building is placed in service, or
- (b) at the election of the taxpayer (owner), the succeeding taxable year.

The election under subparagraph (b), once made, is irrevocable. No credits are given if the building does not comply with IRS regulations for meeting initial compliance. This means that eligible households must occupy the required number of units throughout the ten-year credit period plus an additional five (5) year term (see “Compliance Period”). The housing units designated for the LIHTC must also be rent-restricted for a specific period of time.

### 1.4 Compliance Period

The tax credit program requires fifteen (15) years of continuous compliance, but allows the credit to be taken over a ten (10) year period. Beginning with 1990 allocations (and no later than 1991) state housing credit agencies began the requirement of extended low-income housing commitments that are recorded in local land records. Owners of these developments must agree to commit to at least an additional 15-year low-income use of the project beyond the initial 15-year compliance period. It is important for management to understand that such projects are committed to a minimum 30-year time frame of compliance with tax credit eligibility requirements.

*Extended  
low-income  
use period*

*Note: Noncompliance after the 15th year is not reported via 8823 to the IRS. However, it can impact future developments with your state allocating agency. Take your extended use requirement seriously!*

If a building is not initially qualified by the end of the first year of the credit period, tax credits associated with unqualified units can earn two thirds credit over the compliance period.

The Declaration of Restrictive Covenants binds the owner and any successors to maintain specific occupancy and affordability requirements for the projects. The agreement may list the exact number and size of units that must be low-income at designated income levels (including state deep skew set-asides), provisions for allowing staff units, and special needs groups to be served.

The extended use period may terminate for any building if:

- (a) acquired by foreclosure, or
- (b) the housing credit agency is unable to find a buyer in the 1-year period following the current owner's request in the last year of the compliance period to acquire the owner's interest in the low-income portion of the building.

Section 42 also provides that each individual state has the power to impose additional requirements over and above the federal standards to better address local housing needs inclusive of extending the period for which the property is kept as affordable housing, and Massachusetts has used this authority to provide for an extended use period of more than thirty (30) years that is not subject to prior termination in certain cases, for example, if owners have obtained a higher ranking for their project in the application process by committing to extended affordability.

An additional factor complicating management of tax credit projects is that LIHTC properties are often coupled with subsidy programs (both project-based and tenant-based) that have other government housing regulations. There are times when conflicts between programs arise. *Care must be exercised to ensure that the most restrictive of these competing program requirements is met.*

### **1.5 Five Tax Credit Regulation Periods**

Since the 1986 enactment of the LIHTC, Congress has changed or amended the laws governing the program, yet many changes have not been retroactive. In some cases, the change in regulations brought forth by a technical correction is minor; in others, the effect is substantial. Management must not only be aware of the

*The years  
referenced  
pertain to the  
allocation year.*

differences in regulations, but must have full knowledge of what tax credit law applies to each particular building and/or project. The relevant law for management/compliance purposes is that applicable to the year in which tax credits were allocated by the state housing credit agency. Currently, there are five specific tax credit regulation periods as follows:

I. January 1, 1987 – December 31, 1989

Properties receiving credit allocations during this period based rent on the number of people living in the unit. Rents were subject to change whenever the household composition changed. The Omnibus Reconciliation Act of 1993 allowed owners of these projects a one-time opportunity to either maintain the per person rent formula or elect to change to the formula based on apartment bedroom size used for 1990 and later allocations. The owner had to write to the IRS no later than February 6, 1994 to request this election. Once made, the decision to switch formulas or not was irrevocable. The new rent formula only affected new move-ins on or after the election date. A copy of the election letter must have been provided to DHCD or its Authorized Delegate and must be available during any compliance review. *Please note that all properties allocated credit during this time period have now completed their compliance periods.*

II. 1990

- Rent is calculated by number of bedrooms in a unit (not retroactive).
- Gross Rent Floor adopted (not retroactive).
- Extended Low-Income Housing Commitment required.

III. 1991

- AFDC Student Rule exception (retroactive).
- FmHA Overage Rule (not retroactive).
- Extension on Initial Compliance with Set-Aside (not retroactive).

IV. August 10, 1993

- Married Students Rule (retroactive).
- Single Parent Student Rule (not retroactive).
- 1987-89 Rent Change Option (special rule).

Additional Ruling

*Note: Rule changes and interpretations can be subject to change. Owners are responsible for staying informed. Modifications to this manual are not made with every change.*

- Section 8 requirement (retroactive) where projects cannot refuse to lease to Section 8 tenants.
- V. - Single Parent Student Rule revised, December 2007 (retroactive) [Section 27]

**1.6 Additional Rule Change**

Another important revenue ruling was later issued that was not retroactive.

I. September 9, 1992

- IRS Revenue Ruling 92-61 deals with treatment of staff units as part of the eligible basis [Section 13].

NOTE: Owners must be familiar with HUD 4350.3 change 27 revision 2 in addition to IRS Section 42 requirements.

## Important Compliance Factors

*Income eligible  
and rent restricted*

*Note: Keep key  
documents available  
to everyone involved  
in keeping your  
property in  
compliance.*

*These include but are  
not limited to:*

*8609s  
Regulatory Agreement  
Training/Educational  
Materials*

*Allocation year*

# COMPLIANCE ISSUES

## 2.1 General Compliance

Unlike any other federal housing program, the LIHTC program is administered by the IRS. The key to the entire tax credit program, as well as an owner's ability to claim the full amount of tax credits allocated to the project, is *continuous compliance* with federal and state LIHTC regulations throughout the compliance period.

The two fundamental components of compliance are as follows:

- Tax credit units must be rented to households that are income eligible at move-in;
- Rent must be restricted according to the maximum limits imposed by using the appropriate formula and income limits.

An LIHTC project may have both tax credit units (low-income units) and market (unrestricted rent) units, or it may have 100% tax credit units. The project may also have nonresidential units specified in the LIHTC application and designated in the Declaration of Restrictive Covenants for Low-Income Tax Credits. The income eligibility and restricted rent requirements apply only to the low-income units. These issues will be discussed in more detail later in this manual.

Each Allocating Agency or their Authorized Delegate must monitor owners to ensure properties are in compliance. A leading cause of noncompliance stems from the owner's failure to inform management of the specific regulatory commitments that have been made. Once credits have been allocated for a property, it is imperative that management be given copies of all regulatory and extended use documents to keep on file, including the Tax Credit Application, IRS Form (s) 8609 [Section 10], and Certificates of Occupancy.

Additional key issues are as follows:

- A. **Allocation year** – As previously stated in Section 1, different compliance regulations are in force depending on the year the tax credit allocation was awarded. The most

*Recordkeeping  
by building*

*Monitoring begins  
when a building  
places in service.*

*To be eligible for  
credits, a unit must be  
Rented to an income  
eligible tenant. It  
must be occupied on  
a non-transient basis.*

*For Rehab:  
A temporary  
Certificate of  
Occupancy can be  
used as the Placed In  
Service Date.*

important compliance issue is that all monitoring/compliance is based on the year of **allocation**. *The first two numbers of the Building Identification Number is the allocation year.* Maintain a record of this date.

**B. Compliance by building** – All monitoring/compliance is a **building** issue. Records must be kept by building and by unit number, not by project or alphabetical order by tenant. Every LIHTC building receives a separate IRS Form 8609 and is assigned its own BIN (Building Identification Number). Required annual reports must be submitted by BIN.

**C. Placed-in-service date (PIS)**– For the LIHTC, a building’s **placed-in-service date** initiates the start of compliance monitoring for that building. Each building has only one placed-in-service date for new construction or rehabilitation credits. It is possible to have the same or different dates for different buildings. For new construction, this date is the certificate of occupancy date—“the date on which the building is ready and available for its specifically assigned function, i.e., the date on which the first unit in the building is certified as being suitable for occupancy in accordance with state or local law.” [Section 19] It is the date when the first unit in a building *could* be occupied, not when it *was* occupied. For rehabilitation of an existing building, the owner selects any date within a 24-month period over which rehab expenditures are aggregated. The placed-in-service (PIS) date is recorded on the 8609 form for each building. Be sure you have documentation to back up the PIS date for every building in your project. *It is important to note: If you have Section 8 tenants, as in a HUD project based property, you must certify your tenants income eligible before you can claim the unit as a tax credit unit. You cannot rely on old certifications (previous year) for this purpose. If you will have both acquisition credits and rehab credits, and you have performed a Tenant Certification for the Acquisition PIS date, you may rely on that certification and are not required to complete another certification for the rehabilitation PIS date.*

**D. Eligible basis** – “Eligible basis consists of

- (1) the cost of new construction,

*Eligible basis equals allowable development costs*

*Note: Market apartments are included in eligible basis. Be sure to include them when completing your end of year reporting.*

*Compliance period begins when credits are claimed*

*Minimum number of LIHTC units required*

(2) the cost of rehabilitation, or

(3) the cost of acquisition of existing buildings acquired by purchase... . Only the adjusted basis of the depreciable property may be included in the eligible basis. The cost of land is not included in adjusted basis.” [General Explanation of the Tax Reform Act]

Eligible basis includes the cost of low-income units, facilities for use by the tenants (e.g., common areas, elevators, corridors, roofs) and other facilities reasonably required by the project. The allocable costs of tenant facilities such as swimming pools, other recreational facilities, and parking areas may be included provided there *is no separate fee* for the use of these facilities and they are made available on a comparable basis to all tenants in the project. Costs of the residential rental units in a building which are not low-income units may be included in eligible basis only if such units are not above the average quality standard of the low-income units. Rehabilitation costs may not be included in eligible basis if such expenditures improve any unit beyond comparability with the low-income units. **Eligible basis does not include commercial space.**

Any change in the eligible basis that results in a decrease in the *qualified basis* of the project is noncompliance that must be reported to the IRS. See Section 2.4.

- E. **Initial credit period** – Owners may initially claim credits for the year that the building is placed in service or may defer claiming credits until the close of the following year. It is important for management to know when the credits were or will be claimed for the first time because the compliance period runs fifteen (15) years starting with the first year credits are claimed. The owner makes the election for the initial credit period on each building’s Form 8609. Once made, the election is irrevocable. Credits may not be claimed until the minimum set-aside is met.
- F. **Minimum set-aside (MSA)** – Also an irrevocable election, the minimum set-aside establishes both the minimum number of low-income units to be maintained in a project and the applicable income limit for households to qualify for all tax credit units. See discussion in Section 2.2.

*Criteria for  
tax credit unit*

**G. Qualified LIHTC unit** – A low-income unit qualifies for the tax credit when the following conditions are met:

- Tenant eligibility verified and certified
- Restricted rent
- Nontransient residency
- Unit suitable for occupancy
- Unit recorded as LIHTC unit
- Tenant eligibility re-certified annually
- Available to the public on a non-discriminatory basis

Units meeting these requirements may be counted in the **qualified basis** for tax credit purposes (See Section 2.4).

*Keep first year  
records for 21 years*

**H. Record keeping requirements** – IRS regulations list the LIHTC record keeping and record retention requirements for owners to follow to maintain compliance. Project owners and managers should be familiar with this list and understand that required records could be subject to monitoring at any time. In addition, the first year records must be kept for 21 years. It is strongly recommended that these original documents be stored in a secure fireproof and waterproof location.

Minimum  
Set-Aside**2.2 Minimum Set-Aside Election**

**T**he most critical compliance issue for a low-income housing tax credit project is the minimum set-aside (MSA) requirement. In order for an owner to claim tax credits, a project must have a minimum number of qualified tax credit units. The owner must select one of two minimum set-asides, which establishes both the minimum percentage of tax credit units at the project and the income limit used to determine tenant eligibility. The IRS requires the selection and adherence to a minimum set-aside as follows:

“A residential rental project providing low-income housing qualifies for the credit only if

(1) 20 percent or more of the aggregate residential rental units in the project are occupied by individuals with incomes of 50 percent or less of the area median gross income, as adjusted for family size, or

(2) 40 percent or more of the aggregate residential rental units in the project are occupied by individuals with incomes of 60

*20/50 or 40/60  
to qualify for credit*

*Multiple building vs.  
building-by-building*

*Allocation year  
affects MSA*

*Note: Remember, Owners can choose to begin the credit period either the year the building/project places in service or the year after. If the building/project does not meet the MSA, no credits can be claimed.*

percent or less of the area median gross income, as adjusted for family size.” \*

The owner specifies the MSA when applying for a tax credit allocation and makes the MSA election on the Form 8609 for each building. This election is irrevocable and sets the applicable income limit for *all* LIHTC units in the project. The minimum set-aside must be met within the initial credit period or the property will not be eligible for tax credits. In addition, the MSA must be maintained for the entire 15-year compliance period or recapture of the credit for all units will result.

If a building is identified as part of a **multiple building project** on Line 8b of the Form 8609, the minimum set-aside may be met across all so noted buildings in the project. If the building is not identified as part of a multiple building project, the MSA must be met **within that building**. Properties with several buildings may have buildings noted differently on the form 8609, so management must be aware of the status of **each building**.

*Example 2-1:* The owner of a 10-building, 100-unit tax credit project has elected the 40/60 minimum set-aside to be met as a “multiple-building” project, meaning that 40% of 100, or **40 units project-wide**, must be rented by the end of the initial credit period to tenants who are eligible at the 60% area median gross income limit or no tax credits are available.

*Example 2-2:* In this case, the owner of the same 10-building, 100-unit tax credit project has elected the 40/60 MSA to be met on a *building-by-building* basis. If the project were comprised of 6 buildings with 12 units each and 4 buildings with 7 units each, 40% of a 12 unit building = 4.8 or 5 units and 40% of a 7 unit building = 2.8 or 3 units. Thus the MSA = (6 buildings x 5) plus (4 buildings x 3) = 30 plus 12 = 42 units. In this example, the MSA must be met by the end of the initial credit period for each building or the building will not be eligible for tax credits. *Management must be aware of the distinction between per building and project-wide MSA.*

The MSA must be met prior to any credits being claimed, thus if an owner wanted to claim credits at the end of year one, the MSA would have to be met as needed, by building or project, by 12/31 of the first year. If the owner has deferred the first credit year to the year after placing in service, the MSA must be met by 12/31 of the second year after placing in service.

*MSA not to be confused with state set-asides*

*Note: Multiple layers of financing mean multiple layers of rules. Keep Track!*

## Income Limits

*VLI=50% limits*

*50% x 1.2 =60%*

*Use new income limits within 45 days*

The tax credit MSA should not be confused with other set-asides such as state set-asides that earned extra points in the allocation process and are recorded in the project's Land Use Restriction Agreement (LURA). States may impose set-asides that require certain units to be rented to the elderly or to large families, or may impose lower income limits than the LIHTC would require. In addition, the MSA should not be confused with HOME fund requirements or subsidy programs such as HUD Section 8 or Rural Development. Always determine the tax credit MSA first and review allocation documents to identify any additional set-asides. Implement a tracking system for all set-asides to ensure compliance with these requirements. Follow the most restrictive set-asides so that the project will remain in compliance with all set-asides.

### 2.3 Income Limits

Each year, the Department of Housing and Urban Development (HUD) publishes the Section 8 area median gross income limits for all states. The IRS requires these income limits, as adjusted for family size, to be used when determining eligibility of LIHTC tenants at move-in. The minimum set-aside election establishes whether the 50% or 60% area median gross income (AMGI) limit applies to the project's tax credit units.

HUD's **50 Very Low Income** amounts equal the **50% AMGI** limits for households of one to eight persons. The **60% AMGI** limit equals 120% of the HUD Very Low Income amount for the corresponding family size. Calculate the 60% limits by multiplying the 50% AMGI figures by 1.2

*Example 2-3:* If the 50% income limit for a 2-person household equaled \$25,100, the 60% income limit for a 2-person household would be  $\$25,100 \times 1.2 = \$30,120$ . (While HUD rounds figures to the nearest \$50 or \$100, there is no provision in the code for rounding the 120% calculation up or down.)

Where State set-asides at lower income percentages are in place, these limits would also need to be calculated. Most Allocating Agencies provide the income limits for any additional set-asides. *When HUD publishes new income limits, owners are required to implement the new income limits no later than 45 days after the effective date.* Be aware that any fluctuations up or down in the income limits may have a corresponding impact

## Qualified Basis

*Determines the amount of tax credits the owner can claim each year*

*Applicable fraction is lesser of unit fraction and floor space fraction*

*Note: Managers need to know which fraction applies in order to maintain compliance with the Next Available Unit Rule and the Vacant Unit Rule. Do not just assume it is the same fraction every year.*

on maximum gross rent amounts.

### 2.4 Qualified Basis & Low Income Occupancy

The amount of tax credits an owner can claim depends on the number of rent-restricted, qualified LIHTC units in each building of the project. The percentage of TC units (applicable fraction) in the building multiplied against the allowable development costs (eligible basis) establishes the amount for the building's qualified basis. The qualified basis multiplied by the project's particular tax credit percentage (9% or 4%) determines the amount of credit an owner can claim each year for the 10-year credit period.

The **applicable fraction** is calculated for each building and is the lesser of:

- (a) the unit fraction—the proportion of low income units to all residential rental units in the building, or
- (b) the floor space fraction—the proportion of floor space of the low-income units to the floor space of all residential rental units in the building.

Owners have until the end of the initial credit period to establish the project's original low-income occupancy—the applicable fraction for each building. The low-income occupancy achieved by the end of the initial credit period establishes the project's original qualified basis (QB). Once the QB has been initially established and credits are claimed, the QB is locked in and must be maintained for the entire 15-year compliance period or recapture will result. Only low-income units in the original qualified basis are eligible to receive the full tax credit value during the accelerated 10-year credit period. The qualified basis of a building may be increased subsequent to the initial determination only by reason of an increase in the number of low-income units or in the floor space of the low-income units. Credits claimed on such additional qualified basis are determined using 2/3 of the value of the credit which is now “de-accelerated” through year 15.

A decrease in a project's applicable fraction reduces its qualified basis. If a project's qualified basis for a given tax year decreases from the previous year, this results in noncompliance and recapture by the IRS of some or all of the accelerated portion of the project's credits claimed in prior years.

Maximum  
Gross Rent

*Restricted Rents*

**2.5 Maximum Gross Rent**

Units qualifying for tax credits are subject to a rent restriction formula that sets the maximum gross rent that may be charged. The maximum gross rent may not exceed 30% of the applicable qualifying income limit. Gross rent equals the tenant portion of rent plus the cost of tenant-paid utilities (except telephone and cable) and any other non-optional charges. If low-income tenants are charged more than the allowable rent, the unit is in noncompliance and recapture of credits may result. Whenever utility costs are paid directly by the tenant, gross rent must include an allowance for utilities. Section 2.6 provides more information regarding utility allowances.

The maximum gross monthly rent is calculated by this formula:

$$\text{Maximum Gross Rent (including Utilities)} = (\text{Applicable Income Limit divided by 12}) \times 30\%$$

If the rent calculation ends with a decimal point, always round the amount down since you may never charge more than the maximum. Rounding up would charge more than the maximum allowable rent, resulting in noncompliance.

*Example 2-4:* If the applicable income limit = \$17,500, then divide by 12 to get **\$1458.33** then multiply by .30 , to get **\$437.49**. Round down to **\$437** so as not to exceed the maximum. The maximum gross rent including utilities cannot exceed this figure.

# Persons		1	2	3	4
Income Limit	50%	13,600	15,550	17,500	19,450
	60%	16,320	18,660	21,000	23,340

# Persons		1	2	3	4
Rents	50%	340	388	437	486
	60%	408	466	525	583

**A. 1990+ Projects**

For 1990 and later allocations, rent is based on unit size, not the number of people in the household. The rent formula uses an imputed family size of 1.5 persons per bedroom to determine the applicable income limit upon which to base rent calculations. For efficiency or studio units which do not have separate bedrooms, the 1 person income limit is used.

# Bedrooms	0	1	2
Income Limit	1 person	1.5 person	3 person

*Example 2-5:* To determine which income limit amount to use for the bedroom size rent formula, use the imputed household size of 1.5 persons x the actual number of bedrooms, with an efficiency/studio using the one person income limit.

# Persons	1	1.5	3	
Income Limit	50%	13,600	14,575	17,500
	60%	16,320	17,490	21,000

For the 1.5 person income limit, take the 1 person limit, add to the 2 person limit and divide the answer by 2. Using the limits provided in Example 2-5 above, the income limits and resultant maximum gross rents for the bedroom size formula would be

# Bedrooms	0	1	2	
Income Limit	50%	340	363	437
	60%	408	437	525

*Note: When completing End of Year Reporting. Do not include subsidies when listing tenant rent.*

**B. Rent Subsidies**

Gross rent does not include any housing assistance payments made to an owner to subsidize a tenant’s rent, such as from Section 8 or any comparable federal or state rental assistance program to a unit or its occupants. Only the actual rent paid by the tenant, including tenant-paid utilities, is counted toward the maximum gross rent allowable. For example, if the LIHTC maximum gross rent was \$350 and the total tenant payment was \$250 with Rental Assistance paying an additional \$150 subsidy to

reach the Basic or Contract Rent of \$400, there is no problem. The rent meets tax credit guidelines because the total tenant payment inclusive of utilities does not exceed \$350.

### C. Section 8 Rent

The HUD Section 8 program protects subsidized tenants from ever paying more than 30% of their adjusted gross income for rent. For this reason, in 1989 the IRS ruled that if the tenant portion of rent increases above the LIHTC maximum gross rent, thereby reducing the Section 8 subsidy, the higher rent may be charged.

### D. Rural Development Overage

In RD 515 projects, overage rents may result when 30% of the tenant income minus the utility allowance exceeds the RD program's Basic Rent. If this overage rent exceeds the maximum LIHTC rent, then the overage cannot always be charged. For 1991 and later year projects, the overage can be charged for amounts that are turned over to RD. In 1987-1990 projects, the overage cannot be charged to the tenant since this provision is not retroactive.

## Utility Allowances

*Mandatory amenities or services in gross rent*

*Note: If a tenant is not directly informed a service/amenity is not required as a condition of occupancy, it is presumed to be required and must be included in the gross rent calculations.*

## 2.6 Utility Allowances

The maximum gross rent includes the amount of tenant paid utilities inclusive of costs for heat, lights, air conditioning, water, sewer, oil, and gas, where applicable. Utilities do not include telephone or cable television. Whenever the tenant directly pays utility costs, a utility allowance must be used to determine the maximum unit rent that may be charged. The utility allowance must be subtracted from the maximum gross rent to calculate the maximum tenant portion of rent.

In addition, any *mandatory* supportive service or amenity charge must be counted as part of the gross rent for these units. Such costs may include parking fees, housekeeping, trash removal, meal service, or other required costs. Charges for *optional* services other than housing do not have to be included in gross rent, but such services must truly be optional. *NOTE: Fees may not be charged for any item that is part of the eligible basis (See Section 2-1).*

*Example 2-6:* If the maximum gross rent on a unit is \$525 and the tenant pays utilities with a utility allowance of \$75, the maximum tenant portion of rent allowable is \$450 (\$525 – \$75).

*Example 2-7:* If the same tenant pays an additional mandatory parking fee of \$25 per month, the maximum tenant portion of rent allowable is \$425 (\$525 – \$75 – \$25).

The IRS issued a notice on 5/4/94 to clarify utility allowances in LIHTC projects. Utility allowances should be calculated as follows:

- (1) Rural Housing Services (RHS) - If a building receives assistance from the RHS the applicable utility allowance (UA) for all rent-restricted unit in the building is the RHS UA. Additionally, if any tenant in the building receives RHS rental assistance the applicable UA for ALL units in the building (including those occupied by tenants receiving HUD assistance) is the applicable RHS allowance.
- (2) HUD buildings – If neither a building nor any tenant receives RHS assistance and the rents and utility allowances are reviewed by HUD on an annual basis, the applicable UA for all units in the building is the HUD UA.
- (3) Other buildings – If a building is not subject to either 1 or 2 above, the applicable UA is determined under the following methods:
  - A. Local utility company estimate.
  - B. HUD Utility Schedule Model available at [www.huduser.org/datasets/lihtc.html](http://www.huduser.org/datasets/lihtc.html) .
  - C. Energy Consumption Model whereas the project obtains a qualified professional approved by DHCD to calculate the UA.

Under a, b, and c above the applicable UA for any unit occupied by tenants receiving HUD rental assistance payments (vouchers) is the applicable Public Housing Authority allowance established for the Section 8 program.

Utility allowances must be updated at least annually since they are included in the maximum allowable rent calculations.

*Update utility allowances annually and submit with annual reports*

## Additional LIHTC Regulations

*Recapture may result from renting comparable size units in the BIN to ineligibles while a TC unit is vacant*

*Note: Keep records of your marketing efforts. Be sure to note when your advertisements, open houses, etc. took place. Store these records with your annual records similar to your utility allowance.*

## Available Unit/140% Rule

Copies of utility allowance documentation must be submitted with DHCD's required annual year-end reports. Realize that any changes in utility allowances have a direct impact on the net chargeable rent to the tenant. *Any new allowance must be implemented within 90 days of the change.*

### 2.7 Additional LIHTC Regulations

The following is a list of additional LIHTC regulations.

#### A. Vacant unit rule

If a low-income unit becomes vacant during the year, the unit remains LIHTC compliant and eligible for the tax credit for purposes of the set-aside requirement and determining the qualified basis provided reasonable attempts are made to rent the unit or the next available comparable or smaller size unit to an eligible household and no other comparable or smaller size units in the project are rented to non-qualifying individuals. See Section 25 for IRS explanation of this rule.

“Reasonable attempts” indicates that efforts toward marketing and renting a unit that is suitable for occupancy must be made. *Under no circumstances can you claim credit on the unit if you violate this rule.* Concurrently, if an owner of three vacant units violates this rule by renting to a non-eligible applicant, credit on all three vacant units will be lost and the units cannot be counted toward the minimum set-aside.

Units that have never been occupied are termed “empty” rather than vacant, and cannot be counted as low-income units. However, they must be included in the building's total unit count for purposes of calculating the applicable fraction.

Owners are required to keep records for each qualified low-income building in the project showing for each year of the compliance period the low-income unit vacancies and data for when, and to whom, the next available units were rented.

#### B. Available unit rule / 140% rule

If the household income for residents in a qualified unit

Remember: The “Reasonable Attempts” wording is *not* a part of the Next Available Unit Rule.

increases to more than 140% of the current applicable income limit, the unit is considered an “over-income unit” but may continue to be counted as a low-income unit as long as two conditions are met. The unit must continue to be rent restricted and the next comparable size unit in the building must be rented to a qualified low-income tenant. The owner of a low-income building must rent to qualified residents *all* comparable units that are available or that subsequently become available in the same building until the applicable fraction (excluding the over-income units) is restored to the percentage on which the credit is based.

IRS Regulation 1.42-15, effective September 26, 1997, allows over-income tenants who were previously LIHTC eligible to move to a new unit within the same building, because when a current resident moves to a different unit within the building, the newly occupied unit adopts the status of the vacated unit [Section 21].

*Violating this rule means losing the credits on all 140% units. These units would no longer count toward the MSA.*

### Relocating tenants

*Note: If it is the same building, owners can choose to:*

- 1) *Transfer the certification effective date (and all related paperwork) to the new unit and include a narrative in the file.*  
*OR*
- 2) *Treat the transfer as a move-out of the old unit and a new move-in, complete with a new certification and supporting documentation.*

### C. Relocating existing tenants

When an existing tenant moves to another unit within the same building, the status of the two units swaps. Thus, if a qualified tenant moves to an ‘empty’ unit, the new unit ceases to be ‘empty’ and becomes a qualified unit. The original unit will then be deemed ‘empty’.

When the transfer occurs between different buildings in the same project, a similar rule applies as long as the tenant’s income did not exceed 140% of AMI at the most recent certification. Please note that for purposes of this test, if on the 8609 the owner elected so say ‘No’ to line 8b, then the owner has chosen to treat each BIN as a separate project. In this case, a transfer would require a new certification and the tenant would have to be qualified at the time of move-in.

During the initial credit period, existing tenants cannot be relocated for purposes of qualifying more than one LIHTC unit to count toward the minimum set-aside or applicable fraction. *Under no circumstances can one household be used to initially qualify more than one tax credit unit in the project.*

*Units occupied  
by staff*

*6-month  
minimum initial  
lease term required  
except for SROs or  
transitional housing  
for the homeless*

#### **D. Staff units**

Revenue Ruling 92-61 [Section 13], effective September 9, 1997 allows a unit for a *full-time* staff member to be considered part of a project's "common area." Such units are not classified as residential rental units and thus are not included in either the numerator or denominator of the applicable fraction under section 42(c)(1)(B) for purposes of determining the building's qualified basis.

Revenue Ruling 2004-82 [Section 25] further expanded staff units to include a unit occupied by a full-time security officer for the building if the building owner requires the security officer to live in the unit.

Two options apply:

(1) If the staff unit is a rental unit and is to be counted as part of the qualified basis, then the staff must be income eligible, be certified, and sign a lease the same as any low-income tenant. In this case, if the staff member receives free rent or a rental discount, the imputed value of the rent or discount must be included as income.

(2) If the unit is not a residential rental unit but used as common area by full-time staff, then the staff does not have to be income eligible, certified, leased, or considered a tenant.

The owner's LIHTC application and the allocation documents should stipulate the number of common area units set-aside for staff. If not, the owner should work with DHCD on amending or clarifying the language in the Declaration. This revenue ruling does not apply to any building placed in service prior to September 9, 1992 or to any building receiving an allocation of credit prior to that date unless the owner filed a tax return that is consistent with this ruling.

#### **E. Nontransient occupancy**

"Residential rental units must be for use by the general public and all of the units in a project must be used on a nontransient basis....Generally, a unit is considered to be used on a nontransient basis if the initial lease term is six months or greater."

[General Explanation of the Tax Reform Act of 1986]

“In General—A unit shall not be treated as a low-income unit unless the unit is suitable for occupancy and used other than on a transient basis.”

[Section 42(i)(3)(B)(i)]

To be in compliance, a six-month minimum lease term is required at initial occupancy of low-income units. A six-month lease addendum should be signed with in-place tenants who do not have six months left on an existing lease when the building is placed in service. The only exceptions to this requirement would be SRO housing rented on a month-by-month (30-day lease) basis or transitional housing for the homeless as specified below.

*LIHTC  
ineligible facilities*

**F. General public / fair housing**

All residential rental units in the project must be available for use by the general public. LIHTC properties are subject to Title VIII of the Civil Rights Act of 1968, also known as the Fair Housing Act, prohibiting discrimination in the sale, rental, and financing of dwellings based on race, color, religion, sex, national origin, familial status, and disability. The State of Massachusetts also prohibits discrimination against marital status and age.

*Know accessibility  
requirements*

Tax credit units may not be provided only for members of a social organization or provided by an employer for its employees. In addition, any residential rental unit that is part of a hospital, nursing home, sanitarium, life-care facility, dormitory, trailer park, retirement home providing significant services other than housing, or intermediate care facility for the mentally and physically handicapped is not for use by the general public and is not eligible for credit under Section 42.

*Discrimination  
prohibited*

The Fair Housing Act also mandates specific design and construction requirements for multifamily housing built after March 13, 1991, to provide accessible housing for individuals with disabilities. Owners are expected to be familiar with accessibility requirements applicable to their projects.

The IRS 8823 Report of Noncompliance form states:

*“The failure of low-income housing credit properties to comply with the requirements of the Fair Housing Act*

*Student status  
determined on a  
tax-year basis*

*No grandfathering  
due to student status*

*will result in the denial of the low-income housing tax credit on a per-unit basis.”*

“Available to the general public” applies to all residential rental units, market and tax credit.

**G. Students**

Many students are considered to be transient and thus are not LIHTC eligible. The issue with students is only a concern when *everyone* in the household is a full-time student, defined by the IRS as taking 12 credit hours a semester or attending school full-time 5 months per year at an educational institution with regular facilities, other than a correspondence or night school. The IRS has made it clear that student status is to be monitored on a tax-year basis, thus an applicant would not be eligible if the person had been a full-time student for 5 months of the tax year, even if they had graduated prior to applying for an LIHTC unit. Owners and managers should adjust tenant certification procedures to consider student status according to this interpretation. In addition, there is no grandfathering of eligibility because the tenant was not a student when they moved in and later became one. For this reason, tenant student status must be re-verified at annual certifications to confirm continuing eligibility of the household. Failure to verify student status is noncompliance.

*Exceptions:* A unit would not be disqualified for tax credits if it is occupied as specified in Section 42(i)(3)(D)—

(i) by an individual who is—

1. a student and receiving assistance under title IV of the Social Security Act, or
2. enrolled in a job training program receiving assistance under the Job Training Partnership Act or under other similar Federal, State, or local laws, or
  - entirely by full-time students if such students are—
3. single parents and their children and such parents are not dependents (as defined in section 152) and the children are not dependents of another individual other than the parents, or
4. married and files a joint return.

5. Student was previously under the care and placement Responsibility of the local county children services agency.

The single parent exception was changed as noted above in December 2007.

#### H. Section 8 certificates / vouchers

Section 42 states that LIHTC properties may not refuse Section 8 certificate or voucher holders simply on the basis of their Section 8 status. However, this does not assure tenant selection, because applicants eligible for Section 8 may have incomes exceeding LIHTC income limits, may have negative references, may not be able to afford the rent with vouchers in some situations, or the unit rent may exclude certificate holders due to a conflict with the local Fair Market Rent.

#### I. Suitability of unit

A unit must be continuously suitable for occupancy in accordance with state or local codes in order for credits to be claimed. If the unit is not habitable, no credits can be claimed. In a related situation, the IRS has ruled that should a unit be destroyed due to casualty loss (i.e., fire, flood, or any other disaster) for which credits cannot be claimed while the unit is being replaced, if the unit is restored within a reasonable time within a taxable year, credits can again be claimed and no recapture would occur. Tax credit units that are vacant must be made ready in a timely manner. Otherwise, they would not be considered suitable for occupancy and would not be eligible for credit.

*Note: Do not leave vacant units dirty or unpainted because you have other units ready for rent. The unit you leave unready is not credit worthy!*

## Tenant Eligibility for LIHTC

*Income and student status must be considered*

## Household Size

# DETERMINING TENANT ELIGIBILITY

## 3.1 Overview

Owners must determine and document the eligibility of potential low-income tenants in accordance with LIHTC requirements. A tenant's income eligibility is determined by comparing the household's gross annual anticipated income per HUD Section 8 guidelines to the LIHTC 50% or 60% area gross median income limits that apply to the project. As previously mentioned in Section 2.7(G) of this manual, student status may also affect the eligibility of a household. Owners must verify the household's income and the student status of all household members and the tenant and owner must certify the accuracy of the verified information. Since household composition, income, and student status may change over time, owners must re-certify the eligibility of tenants in tax credit units annually, on or before the anniversary date of the previous certification.

## 3.2 Household Size and Income Limits

Section 42 mandates that HUD Section 8 income limits as adjusted for household size be used in determining income eligibility for the LIHTC. A household can consist of one or more persons. Members do not need to be related to be considered a household. Count all household members and compare to the per person 50% or 60% income limits currently in effect. Full-time students residing together in a unit do not constitute a household under LIHTC requirements unless one of the exceptions listed in Section 2.7(G) applies.

Certain individuals are not considered members of the household in determining the income limits.

Do NOT count the following in determining income limits:

- Live-in Attendants
- Visitors or Guests
- Foster Children
- Foster Adults

*Note: Spouses not currently residing with the applicant but who may return are counted as household members. Separation agreements, estrangement and divorce documents must all be on file to exclude income of spouses that are not expected to become members of the household.*

*Unborn children and children being adopted counted for income limits*

## **Definition of Income**

Temporarily absent members who *would* be included in the household size determination include:

- Children temporarily absent due to placement in a foster home
- Children away at school, but who live with the family during school recesses
- A person confined to a hospital or nursing home per family decision
- A son or daughter on active military duty *only* if this person leaves dependents or a spouse in the unit

Households may choose whether or not to count permanently absent family members. When HUD issued Change-27 on September 29, 1995, the following determination on household size appeared for the first time:

*“Unborn children and children who are in the process of being adopted (who do not live in the unit) are considered household members for purposes of determining unit size and income limits....”*

HUD 4350.3 CHG-27, Figure 3-6  
Currently found in HUD Handbook 4350.3 REV-1, 3-7

Massachusetts recognizes unborn children and children in the process of being adopted as household members in determining income limits.

### **3.3 Gross Annual Income**

The code states—“Tenant income is calculated in a manner consistent with the determination of annual income under Section 8 of the United States Housing Act of 1937 (“Section 8”), not in accordance with the determination of gross income for federal income tax liability.” In the HUD Handbook 4350.3 REV-1, 5-3 annual income is defined as the anticipated total income from all sources received by the family head and spouse (even if temporarily absent) and by each additional member of the family, including all net income derived from assets for the 12-month period following the effective date of certification of income, exclusive of certain types of income.

<b>Total Income from all Sources</b>		=	<b>Annual Income</b>	
Gross Earned/ Unearned Income	+	Net Income from Assets	=	Annual Income

For information regarding what annual income includes/excludes and how to calculate annual income, see Section 23 for excerpts from HUD Handbook 4350.3 REV-1, 5-6. Note that LIHTC total income is gross annual income, *not* “adjusted” annual income. Allowances used in some government programs, such as childcare allowance and medical expense allowance, are not deducted from the household’s annual gross income to determine income eligibility for LIHTC units.

## Net Asset Income

*Cash value of assets  
and asset income  
must be verified  
for entire household*

*If net assets > \$5,000  
use the greater of  
actual income  
of imputed income*

*If net assets <  
\$5,000  
Management may  
use the Under  
\$5,000 Asset Form.*

*Assets disposed of  
for less than fair  
market value  
must be considered*

### 3.4 Assets

**T**he net income from assets must be considered when determining the tax credit eligibility of a household. Asset information for all household members (including minors) should be obtained at the time of application. Information regarding what net family assets include/exclude is provided in Section 23 excerpts from HUD Handbook 4350.3 REV-1, 5-83, Exhibit 5-2.

**The cash value for all assets and asset income must be verified by the owner obtaining third party documentation as specified by HUD verification procedures.** Owners may use the sworn statement for assets referenced under IRS Revenue Procedure 94-65 [Section 17]. Assets must be verified for the initial certification of the household and for each recertification.

*If utilizing the procedure 94-65, please be aware that the income from the asset must always be identified and included as income on the certification.*

If net family assets exceed \$5,000, the asset income to be included in household income will be the greater of: (a) the actual asset income, or (b) an imputed income from assets, which is the net family assets multiplied by the passbook rate specified by HUD. Until further notice, owners must use a rate of 2 percent (.02).

At each certification and annual certification, applicants and tenants must declare whether or not an asset has been disposed of

## Application Procedure

for less than fair market value during the two years preceding the date of application or the effective date of the recertification. An asset is considered to be disposed of for less than fair market value if the cash value of the disposed asset exceeds the gross amount the family received by more than \$1,000. If it does, for a period of two years owners must include in the total household assets the difference between the cash value of the asset and the amount received. See Section 23 HUD Handbook excerpts 5-33 for examples of assets disposed of for less than fair market value.

### 3.5 Tenant Application Procedure

**B**ecause the LIHTC program uses special definitions for income, assets, and household composition, standard property management application forms may not collect sufficient information to determine tenant eligibility. A comprehensive housing application is critical to the accurate identification of full-time student status, all assets, and anticipated income sources to be verified in the determination of tenant eligibility for the LIHTC. *The application must be sufficiently detailed with regard to income, assets, and student status enabling an owner to effectively make a determination of eligibility for this program.*

The information furnished on the fully completed application is reviewed along with supplementary historical documents.

The application procedure *must* include an interview with all adult household members to review the application and historical documents and clarify any discrepancies or missing information. (For example, if the recent 1040 form and W-2s show 2 employers, but the application only lists one, question what happened to the second job and confirm its termination.) This interview is documented with the **recommended Interview Checklist**, also included in Section 6 which is signed and dated by management and all adult applicants.

#### *Interview Checklist*

One application and interview checklist signed by all co-applicants should be submitted per household. This document must be current to 120 days of the certification date.

*Note: The stronger your verification procedures, the less likely you are to be found out of compliance. Do not default to the minimum standards of documentation.*

### *Verifying Income*

*Note: As a means of comparison, Owners are encouraged to obtain pay stubs along with third party documents.*

*Note: The only way to protect your credits in the event of tenant fraud is to take action immediately. Do not wait until your monitoring agent points out what you already should have known.*

## **3.6 Tenant Income Verification**

**D**etermination of annual income of individuals and area median gross income adjusted for family size must be made in a manner consistent with HUD Section 8 income definitions and guidelines. HUD Handbook 4350.3 REV-1 is the reference guide to be used for identifying the income/assets to be included or excluded when determining household income and appropriate excerpts from the HUD Handbook 4350.3 REV-1 are included in Section 23 of this manual.

The anticipated earned income of every prospective household member 18 years of age or older must be verified. Unearned income, assets and asset income of all household members, including minors, must be verified. Verifications must be received by the owner/ management agent prior to the execution of the certification of tenant eligibility and lease. Information concerning acceptable forms of verification, the effective term of verifications, proper verification methods to follow, and how to calculate total income is provided in HUD Handbook 4350.3 REV-1 included in Section 23. To summarize:

### **A. Effective Term of Verifications**

Third-party verifications are valid for 120 days following receipt. Owners may not rely on verifications that are more than 120 days old. After this time, a new written verification must be obtained.

### **B. Verification Methods**

Written third party verifications are preferred. An authorization to release information must be signed by the applicant/tenant and must accompany verification requests. Owners must send verifications directly to the source and the source must return them directly to the owner.

*Verifications must not be hand-carried by the applicant/tenant to or from the source.* If written verification is not possible, direct contact with the source, in person or by phone, is acceptable. The owner must document this verbal verification in the tenant file and must obtain all information as requested on the written verification [See Section 23 HUD Handbook 4350.3 REV-1, 5-49].

### **C. Differences in Reported Income**

Significant differences between the income/asset amounts

*Note: When calculating income, be conservative. If you decide a lesser number is warranted explain why. Use of telephone clarifications when information is incomplete or vague is encouraged.*

## Certification of Income

*Note: The purpose of the certification worksheet is to show the math that results in the amounts listed on the Tenant Income Certification. Consider highlighting the figures on the verification that are used.*

## Lease

reported on the application and amounts reported from third party verifications should be explained by the applicant/tenant and documented in the tenant file utilizing a form such as the Telephone Verification.

Sample recommended verification forms are included in Section 6. If forms currently in use at your property are comparable to the forms in this section, you may continue to use your current forms. However, since these forms are being provided only as examples, noncompliance will occur if forms in use do not adequately meet LIHTC and HUD certification or verification requirements.

### 3.7 Tenant Income Certification

Once all the income and asset information has been obtained, data should be recorded and computations done on a form similar to the **Certification Worksheet** found in Section 6. If the total 12-month projected household income is less than or equal to the maximum allowable qualifying income in effect at the time of tenant certification, the household is income eligible for a tax credit unit. If the total household income exceeds the maximum allowable qualifying income, the household can not be certified eligible for a tax credit unit.

Upon receipt of all verifications, owners/managers should review all documentation and calculations. If it is determined that all requirements for eligibility are met, the **Certification of Tenant Eligibility** found in Section 6 must be filled out and executed along with the lease prior to move-in. All adult members of the household must sign the Certification form. It is preferred that the Certification be executed by tenants and owner/manager no earlier than 5 calendar days prior to move-in and in no event after the execution of the lease.

### 3.8 Lease

All tenants occupying tax credit units must be certified and under lease (as specified in the Code) no later than the date the tenant takes possession of the unit. The lease must be signed by all parties to the agreement by the beginning lease term date to be properly in effect and the unit in compliance.

*Note: Leases must be signed in good faith. A number of short tenancies despite a six month lease can raise questions about procedures. If a tenant vacates early, consider including an explanation (if known) in the file.*

*Note: Only when a tenant receives section 8 subsidy can the tenant portion of rent exceed the LIHTC maximum rent limit.*

DHCD does not specify a model dwelling lease to be used by owners however, some leasing guidelines are listed below.

- A. The lease should include, but is not limited to:
- The legal name of all parties to the agreement and all additional occupants
  - Identification of the unit to be rented (number, street address, etc.)
  - The date the lease becomes effective
  - The term of the lease
  - The amount for rent—If this reflects a contract rent amount which may include a subsidy payment, rather than just the tenant portion of the rent, a lease addendum listing only the tenant share of rent is recommended.
  - The rights and obligations of the parties, including the obligation of the tenant to recertify income annually (or more frequently as required)
  - Language addressing changes in income, utility allowance, income limits, basic rent (RD or HUD 236 projects), family composition or any other change and its impact on the tenant's rent
  - Signature dates
- B. The tenant portion of rent plus utility allowance and other mandatory fees must not exceed the maximum gross rent allowed by Section 42 of the Code.
- C. The initial lease term must be at least 6 months on all tax credit units, except for SRO housing which may have a 30-day lease or transitional housing for the homeless (as specified in Section 2.7(E) of this manual) which provides “temporary housing” and has no lease requirement. Succeeding leases are not subject to a minimum lease term.

The beginning term of the lease and effective date of the certification should be concurrent. Signatures should be no greater than 5 days prior to these dates.

Additionally, the lease should not contain any clauses that would allow termination prior to the six month tax credit requirement.

## Recertification

Annual certifications ensure affordable housing units are occupied by income eligible households, and provide a means to ensure compliance with the Next Available Unit Rule and student status.

### 3.9 Recertification

Recent changes in IRS regulations no longer require annual certifications for properties that are 100% tax credit. Allocating agencies can still require them and DHCD is no exception.

#### FOR 100% TAX CREDIT PROPERTIES:

DHCD requires that recertification of residents be completed on at least an annual basis (though failure to recertify tenants on an annual basis is no longer cause for the issuance of IRS Form 8823). What is required has changed significantly. *Every* LIHTC household is expected to undergo a complete annual recertification *the year following move in*. Subsequent years, require a self-certification.

DHCD can require properties that have rented to ineligible households or demonstrated inadequate certification/documentation procedures to revert to full annual recertification procedures as with properties containing market units.

#### FOR PROPERTIES WITH MARKET UNITS:

Section 42 states: “The determination of whether the income of a resident exceeds the applicable income limit shall be made at least annually on the basis of the current income of the resident.” While the recert does not determine continued eligibility, it does identify the 140% rule situation, student status, and possible household composition changes. Properties with market units must complete a full annual recertification every year. **Self certifications cannot be used.**

#### FOR ALL PROPERTIES:

The timing of the recertification is critical. Recertification must be completed within 12 months from the initial certification date, or 12 months from the most recent certification.

### 3.10 Annual Recertification Waiver

DHCD has chosen to continue requiring an annual recertification of tenant income in 100% low-income projects. The Annual Recertification Waiver is not an option at this time.

## Section 8 Qualification

Note: With a section 8 tenant your annual recertification folder could consist of just two documents. The certification and a section 8 income verification Form. Be careful to ensure that the information provided is no more than 120 days old.

### 3.11 Qualifying Section 8 Tenants

**A**dditional forms of income verification may be used for tenants who receive housing assistance through the HUD Section 8 program. For these tenants only, acceptable forms of income verification include a signed copy of the appropriate HUD form 50058 or 50059, a letter from the HUD Contract Administrator (e.g., local PHA) stating that the tenant's annual gross income is less than the applicable LIHTC income limit, OR a Section 8 verification form as found in Section 6. These forms may be used as income verification documentation to support the **Tenant Income Certification** which must be executed for every LIHTC household.

*Proof of tax credit eligibility must be on file for all Section 8 tenants. Section 8 eligibility does not guarantee tax credit eligibility. Student requirements will never be identified or verified by the local PHA. Proof of income eligibility and tax credit eligibility is the responsibility of the owner.*

Recordkeeping  
and  
Retention

# RECORDKEEPING & RECORD RETENTION

## 4.1 LIHTC Recordkeeping

The LIHTC program requires owners to maintain project records in accordance with program requirements and to provide annual reports to their State Monitoring Agency documenting project occupancy. IRS regulations set forth in 26 CFR Part I - 1.42-5(b) [Section 26-1] specify the tax credit recordkeeping and record retention provisions that owners must follow to maintain compliance. Recordkeeping responsibilities include three types of project records:

- Tenant files
- Monthly unit data tracking
- Project files, including records regarding the use of facilities included in the project's eligible basis

An owner must keep records for each qualified low-income resident by building and unit number throughout the Compliance Period.

Owners must also provide three documents regarding a project's status:

- LIHTC Owner's Compliance Certification; *annually*
- LIHTC Unit History Report. *annually*

In addition, Unit History information must be gathered and submitted electronically. Owners and managers will be updated on changing technology.

Failure of the owner to provide reports in a timely manner when requested is regarded as noncompliance.

## 4.2 LIHTC Record Retention

The owner must retain the above-described records for the first year of the credit period for at least **6 years** beyond the due date (with extensions) for filing the federal income tax return

for the last year of the Compliance Period, meaning original files must be retained for **21 years**. All other records are required to be retained for at least **6 years after the due date** (with extensions) for filing the federal income tax return for that year.

# NONCOMPLIANCE

## 5.1 Types of Noncompliance

**L**IHTC noncompliance may be defined as a period of time the development, specific building, or unit has failed to follow proper procedures. These procedures may be IRS Section 42 requirements or HUD certification procedures. Noncompliance can lead to recapture of tax credits for a given period of time.

Most noncompliance issues as identified by IRS definitions may be found on the IRS Form 8823 Low-Income Housing Agencies Report of Noncompliance [Section 20]. In general, noncompliance issues can occur for:

*A compliance checklist*

- Inadequate certification documents
- Failure to obtain and retain proper income verifications
- Missing signatures
- Late certifications or certification signature dates
- Lease issues, i.e., not signed, late, or no 6 month term
- Failure to re-certify by the certification anniversary date
- Violations of UPCS or local inspection standards
- Failure to submit year-end documentation on time
- Failure to respond to requests for additional information
- Incomplete record-keeping
- Failure to properly identify full time students
- Failure to maintain and update utility allowance documentation
- Charging unrestricted rents
- Failure to maintain the minimum set-aside
- Any change in the applicable fraction or eligible basis that results in a decrease in the qualified basis
- Housing a non-eligible tenant
- Disposal of ownership interest.

*This list is representative and not meant to be all-inclusive.*

## **5.2 Recapture of Tax Credits**

Recapture

**T**he most serious action the IRS can take against an ownership is the recapture of credits previously claimed. Only the IRS determines this course of action. Consequences to issues of reported noncompliance are not governed by the monitoring agency. If the owner discovers at any time that credits were claimed in error, miscalculated, or the basis was incorrectly listed, IRS Form 8611 may be submitted to voluntarily recapture credits.

## **5.3 Liability**

Owner Liability

**Compliance with the regulatory requirements of Section 42 is the responsibility of the owner(s) of the building for which credit is allowable. DHCD's obligation to monitor for compliance and report any issues of noncompliance with Section 42 regulations to the IRS does not make DHCD liable for an owner's noncompliance.**

NOTE: Don't confuse required forms with required paperwork.

With the possible exception of Section 8 Voucher holders, every tenant file must have an application or recertification update and verifications. You are also required to prove you have interviewed the tenant/applicant to ensure the information you received is adequate and complete.

## FORMS

This section contains copies of recommended forms. The combination of these forms sufficiently meets the Section 42 code requirements for record-keeping and, in striving to reach a consistent standard of accurate tenant file documentation, their use is recommended.

In filling out each form, see that every line item is addressed. Make certain that all forms are filled out completely, including returned verification forms. Do not assume that a blank line means "Not Applicable." *Third party verifications should be mailed or faxed to the source, never hand-carried.* Pursue phone verification to clarify any missing or ambiguous information.

Never use correction tape or liquid to revise information on any document. If revision or correction is required, draw a line through the change, then write the correct information above it. All parties must initial each change or correction.

### A. Required Forms For Tenant Certification

1. Tenant Income Certification
2. Self Certification

### B. Annual Year End Forms

These forms are **required to be submitted by March 1st** following the close of every calendar year of the compliance period for each building. They can be downloaded from the SPECTRUM website [www.spectrumlihtc.com](http://www.spectrumlihtc.com).

1. DHCD Annual Report/Owner's Certification
2. Utility Allowance Information
3. Software Download / Status Report database

### C. Recommended Forms for Tenant Certification

*Note:* If the corresponding forms currently in use at your property are comparable to the forms in this section, you may continue to use your current forms. However, since these forms are being provided at no additional expense as examples of tenant information to request/verify and document for tenant files, noncompliance will occur if the form in use does not adequately meet LIHTC and HUD certification or verification requirements. Should there be any question regarding comprehensiveness of your forms, please submit your forms to SPECTRUM for approval.

*Note: Contact your allocation agency or their authorized agent if your tenant's circumstances are unusual. They can provide specific forms or inform you what information you need to obtain..*

1. Employment Income Verification (Third Party)
2. Unemployment Verification (Third Party)
3. Public Assistance/TANF Verification (Third Party)
4. Child Support or Alimony Certification (Third Party & Self Affidavit)
5. Social Security/SSI Verification (Third Party)
6. Pension Verification (Third Party)
7. Veteran's Pension/Benefits Verification (Third Party)
8. Asset Income Verification (Third Party)
9. Real Estate Verification (Third Party)
10. Real Estate Asset Worksheet
11. Telephone Verification/Clarification (Third Party)
12. No Change in Income Statement (Self-Affidavit)
13. Section 8 Income Verification (Third Party)
14. Life Insurance Verification (Third Party)
15. Student verification (Third Party)
16. Household Student Status Verification (Retroactive, Self-Affidavit)
17. Self-Employment Affidavit
18. Verification of Terminated Employment (Third Party)
19. Annuity Verification
20. Certification Worksheet

# COMPLIANCE MONITORING

## 7.1 Fulfilling Compliance Obligations

**Y**our compliance monitoring *begins when you place in service*. The IRS requires specific recordkeeping requirements that may be found in Recordkeeping Requirements of Section 42 in Section 4 of this manual. **In order to maintain compliance with Section 42 and Massachusetts Requirements, you should immediately notify DHCD when you place in service.** DHCD will help you identify specific submission requirements for your property.

A file review of 20% of the files for 1/3 of the LIHTC properties annually is required by the IRS. Currently, SPECTRUM Enterprises performs compliance monitoring under contract as the Authorized Delegate for the State of Massachusetts. On the SPECTRUM Web site, [www.spectrumlihtc.com](http://www.spectrumlihtc.com), you will find information regarding yearly submission requirements. You will need to contact SPECTRUM to receive specific details for the yearly submission requirements and to notify SPECTRUM & DHCD of your placed in service dates. You will be placed on the SPECTRUM mailing list as soon as it is determined you have placed in service, and you will be notified when any required yearly submissions are due. However, if you place in service earlier than targeted and do not contact SPECTRUM & DHCD, you may miss submission deadlines required by the IRS. Information and updates will be posted on the SPECTRUM Web site. This information will include but not be limited to forms, industry Web links, and industry information. Additionally, we will be sending notices via email, in an attempt to reduce paper communications.

### *Yearly submission requirements*

**What are the yearly submission requirements?** In short, an owner is required to submit an annual report and certification [Section 6] and unit history for all tax credits units. Unit history information is collected electronically for the previous year. You may download software and instructions from the SPECTRUM Web site at [www.spectrumlihtc.com](http://www.spectrumlihtc.com).

This information is required by law, so it is very important that

*Site visit within two years of PIS date*

information submitted is timely and accurate. Failure to submit on time, incomplete submissions, or inaccurate submissions may be determined noncompliant.

An Owner must realize that the *Owner* is required to maintain and submit the records. Managers must realize that the Owner is financially responsible for late submissions or inaccurate submissions.

**When will SPECTRUM visit the site?** By 12/31 of the second year after the last building places in service and at least once every three years thereafter SPECTRUM will audit 20% of your files, inspect 20% of your units, and inspect all of common area in all buildings. You will be notified at least 30 days in advance of the site visit. While we can accommodate emergency situations, audit dates are not negotiable. Our schedules are tight and geographically coordinated. Normal procedures are as follows:

1. A SPECTRUM Monitor will contact Management by phone to inform them of an upcoming on-site review. The monitor will answer any questions or concerns about the review.
2. A Confirmation Letter (see sample below) will be sent verifying the date, time, and requirements for the review.
3. We visit the site, auditing 20% of the tenant files, inspecting 20% of the units and all common areas
4. An Owner's Report is then written and forwarded to the Owner, with management copied. There is a thirty (30) day period in which to respond. Late submissions will be considered noncompliance. Submissions after an IRS Form 8823 is generated will not be reviewed without DHCD authorization.
5. The Owners' responses to the Owner's Report will be reviewed and a notification to the Owner will be sent out informing the Owner of his compliance status. Management is again copied. If non-compliance is being reported, an unsigned copy of the generated Form 8823 will be included as an attachment.

*Sample confirmation  
letter*

The following is a sample confirmation letter:

[date]

[name]

[address]

[address]

Re: LIHTC Compliance Monitoring For **[property name]**

Dear [name] :

This letter is to confirm our scheduled inspection and review of the referenced property on **[day, date, and time, e.g. Tuesday, June 26, at 10:30AM]**. We will review (#) LIHTC files and inspect (#) LIHTC units and all common areas. The files and units will be chosen at random upon our arrival. To help prepare for our inspection and review, please comply with all of the following:

1. Ensure that all LIHTC residents are notified of the upcoming site inspection. Additionally, it is **required** that an Owner's representative be present at all times during the site inspection, preferably a maintenance staff person familiar with the building systems and also an administrative person familiar to the residents. SPECTRUM Monitors *will not* enter a unit or a room in any building unaccompanied. The Owner's representative must be able to keep pace with the Monitor to facilitate the review. If the Owner is unable to provide such a representative, the building/unit will be failed and it will be reported to the Internal Revenue Service (IRS) as non-compliance.
2. All common area emergency lighting will be tested during the inspection by throwing the circuit breakers and walking the hallways. Circuit breakers for emergency lighting *must* be identified, labeled, and accessible at the time of inspection. This system test is the most accurate portrayal of an emergency situation. This type of system test will be conducted unless loss of power to the building would automatically bring the fire department or unless the building has a generator back up system.
3. The following documents are **required** for the review. Those documents identified as items **b-g** will be taken back to the SPECTRUM office for our records. An Owner's representative familiar with the resident files **must** be present during the file review.

- a. LIHTC resident files including certifications, verifications, applications and lease agreements;
- b. A current Rent Roll showing rents charged to LIHTC residents (*please provide this immediately*);
- c. Copies of original 8609's, signed by the owner (*first year only*), and also Schedule(s) A and form(s) 8586.
- d. Copy of the Tenant Selection Criteria in use for the property;
- e. Copies of Utility Allowance documentation for *all* years under review;
- f. Copy of a listing of all LIHTC units, *organized by BIN* (Building Identification Number);
- g. A management forms package including: tenant application, income certification, interview/questionnaire, worksheet, employment verification, certification of child support, and other applicable third party verifications.

*Please Note:* Failure to comply with any of these monitoring requirements will hinder the review and will be reported to the IRS as noncompliance.

SPECTRUM utilizes State Building Codes when conducting physical inspections. Should you have any questions or concerns, please contact our office directly.

**As stated in the Code, Section 1.42-5(g), Compliance with requirements of Section 42 is the responsibility of the owner of the building for which the credit is allowable. The Agency's obligation to monitor for compliance with the requirements of Section 42 does not make the Agency liable for an owner's non-compliance.**

Thank you for your assistance.

Respectfully,  
LIHTC Monitoring Specialist

Please review the requirements listed in sections two and three of the sample letter. It is essential that these documents are available for the review. No excuses will be accepted. "Failure to comply with these requests will be considered noncompliance and would be reported to the Internal Revenue Service as such."

*What we expect  
regarding a file  
review*

**What expectations does SPECTRUM have regarding the file review?**

- \* Uniformly organized files
- \* Move-in certifications effective for the LIHTC move-in date and signed not more than 5 days prior to the effective date
- \* Back-up verification for all certifications
- \* Annual certification effective on or before the anniversary date
- \* Student Status identified and/or verified for every certification
- \* Worksheets showing calculations used on the certification
- \* A documented tenant interview at move-in
- \* An application sufficient to determine eligibility for a LIHTC property
- \* A re-certification update or questionnaire for the annual certifications
- \* Phone clarifications for any ambiguities or missing information on verifications (NO BLANKS)
- \* Child support and zero income affidavits addressing historical and anticipated income
- \* Zero employment affidavits
- \* Third-party verification of gross pension benefits, including verification of changes
- \* Verification of termination of employment where applicable
- \* All HUD criteria for acceptable forms of verification satisfied
- \* At minimum, a six-month lease in effect for the LIHTC move-in date without an early termination clause prior to six-months
- \* Utility allowance verification for each year of the credit

**Will SPECTRUM look at anything else?** SPECTRUM will audit your submissions on an annual basis. This review is separate from the on-site reviews. Additionally, SPECTRUM will monitor compliance with the Land Use Restriction Agreement, the original qualified basis, deep income targeting, next available unit rules, 140% rules, Fair Housing, ADA, and utility allowance requirements.

*What we expect regarding the physical inspection*

*Note: All items noted during the physical inspection are expected to be addressed, even if they do not rise to the level of a building code violation.. You could receive a report of noncompliance for failing to respond to minor inspection items.*

*Inoperable emergency lights and exit signs are the biggest source of 8823s in Massachusetts!*

## 7.2 Physical Inspection of Units

In Massachusetts, SPECTRUM uses State Building Codes. A physical inspection of all buildings in a project and 20% of the units in a project is a requirement of the Tax Credit Program. Physical inspections will generally be performed at the same time as file reviews. State physical inspection guidelines are strictly adhered to. The IRS requires reporting of violations. As all properties have knowledge of our arrival there is no excuse for common area violations such as smoke detectors, emergency lights, and fire alarm panel system faults. All violations must be reported to the IRS as non-compliance unless repaired prior to our leaving the property.

Examples of health and safety findings include:

- Structural and roof problems
- Blockage of fire exits
- Elevators functioning improperly
- Smoke/Carbon Monoxide detectors not functioning
- Pest infestation
- Serious electrical, heating, or plumbing problems
- Common area safety lighting problems

Routine violations are those that require correction but do not impair essential services and tenant safeguards.

### **What expectation does SPECTRUM have regarding the physical inspections?**

- \* All LIHTC residents should be notified of the upcoming site inspection
- \* An Owner's representative *must* be present at all times during the site inspection, preferably a maintenance staff person familiar with the building systems and an administrative person familiar to the residents
- SPECTRUM Monitors *will not* enter a unit or a room in any building unaccompanied
- \* Circuit breakers for emergency lighting *must* be identified, labeled, and accessible at the time of inspection
- \* All common area emergency lighting will be tested during the inspection by throwing the circuit breakers and walking the hallways. This system test is the most accurate portrayal of an emergency situation. This type of system test will be conducted unless loss of power to the

building would automatically bring the fire department or unless the building has a generator back up.

\* Since smoke detectors, carbon monoxide detectors, emergency lighting, fire alarm panel system faults, and blocked egress issues in common areas are automatic non-compliance, be sure to inspect all of these systems before our arrival.

The IRS requires that unit inspections be performed on the same units that are selected for file review. Units where admittance is not possible for any reason may be failed and/or subject to re-inspection at the owner's expense.