Average Income Set-Aside for Property Managers

MAAHMA / VHDA Conference

Wednesday, November 20, 2019

midatlanticahma

AFFORDABLE HOUSING MANAGEMENT ASSOCIATION

Today's Panel

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‘Demystify’ (Merriam-Webster): synonyms…

“clarify, clear (up), construe, demonstrate, explain, explicate, expound, get across, illuminate, illustrate, interpret, simplify, spell out, unriddle”

Objectives

- Demystify the Average Income Set-Aside Election (AI) for LIHTC projects.
- Review VHDA Requirements for Implementing AI
- Demonstrate the math behind the AI
- Describe and demonstrate the non-compliance uncertainty with AI.
- Share best practices for property management staff to successfully operate AI projects.

About the Average Income Set-Aside Election

What is the New Minimum Set Aside?

VJV


Form 8609
(Rev. May 2018)
Department of the Treasury
Internal Revenue Service
Part I Allocatio

Existing minimum set asides:

- At least 20% of units rent restricted and occupied by tenants at 50%or less of Area Median Income (AMI)
- At least 40% of units rent restricted and occupied by tenants at 60% of AMI
- NYC – special 25% of units at 60%of AMI

New Minimum Set Aside - Consolidated Appropriations Act of 2018. Law says:

- Applies to elections made after enactment – March 23, 2018
- Owner designates income limitation for each low-income unit
- In 10% increments, designation can be 20%, 30%, 40%, 50%, 60%, 70% or 80%
- Average of unit designations must be 60% or less of AMI
- Also at least 40% of units rent restricted
- One-time election for NEW properties*

Consult with your state HFA for their specific restrictions, criteria, do's and don'ts, etc.

How is the Average Income Election Made?

Form **8609**
(Rev. May 2018)
Department of the Treasury
Internal Revenue Service

Part I **Allocatio**

Part II **First-Year Certification**—Completed by Building Owners with respect to the First Year of the Credit Period

7	Eligible basis of building (see instructions)	7	
8a	Original qualified basis of the building at close of first year of credit period	8a	
b	Are you treating this building as part of a multiple building project for purposes of section 42 (see instructions)?	☐ Yes	☐ No
9a	If box 6a or box 6d is checked, do you elect to reduce eligible basis under section 42(i)(2)(B)?	☐ Yes	☐ No
b	For market-rate units above the average quality standards of low-income units in the building, do you elect to reduce eligible basis by disproportionate costs of non-low-income units under section 42(d)(3)(B)? . ▶	☐ Yes	☐ No
10	Check the appropriate box for each election. **Caution:** Once made, the following elections are irrevocable.		
a	Elect to begin credit period the first year after the building is placed in service (section 42(f)(1)) ▶	☐ Yes	☐ No
b	Elect **not** to treat large partnership as taxpayer (section 42(j)(5)) . . . . ▶	☐ Yes	
c	Elect minimum set-aside requirement (section 42(g)) (see instructions): ☐ 20-50 ☐ 40-60 ☐ Average income ☐ 25-60 (N.Y.C. only)		
d	Elect deep rent skewed project (section 142(d)(4)(B)) (see instructions)	☐ 15-40	

Basic AI Calculation

(spreadsheet demonstration)

- Many ways to get to 60% average
- Rents charged to tenants based on unit income designation
- Calculation not based on unit size or bedrooms– just number of units
- Units must be rent and income-restricted based on designation

VHDA Average Income Requirements

VHDA QAP Requirements

VHDA must review and approve designations and confirm Average Income election

Income averaging is permitted for all future developments. Projects already approved for funding will be reviewed on a case by case basis. The following are minimum requirements for selecting income averaging:

- 100% Low Income – No Market Units
- Line 8b of the 8609 form must be selected for Multiple Building Election
- Initial Unit Mix Showing the Average Set-Aside must be provided
- For deals that were funded prior to January 1, 2019, the Owner must forfeit the right to pursue a Qualified Contract
- Assigned Unit Set Asides Must Float
- Must Have a Reasonable Distribution of Set-Asides Across All Unit Sizes

Tax Credit Developments in the Extended Use period may elect this minimum set-aside but the existing

2019 Low-Income Housing Tax Credit Application For Reservation

L. UNIT DETAILS

1. **Set-Aside Election:** UNITS SELECTED IN INCOME AND RENT DETERMINE POINTS FOR THE BONUS POINT CATEGORY

Note: In order to qualify for any tax credits, a development must meet one of two minimum threshold occupancy tests. Either (i) at least 20% of the units must be rent-restricted and occupied by persons whose incomes are 50% or less of the area median income adjusted for family size (this is called the 20/50 test) or (ii) at least 40% of the units must be rent-restricted and occupied by persons whose incomes are 60% or less of the area median income adjusted for family size (this is called the 40/60 test), all as described in Section 42 of the IRC. Rent-and income-restricted units are known as low-income units. If you have more low-income units than required, you qualify for more credits. If you serve lower incomes than required, you receive more points under the ranking system.

#N/A

a. **Units Provided Per Household Type:**

Income Levels

# of Units	% of Units	
	#DIV/0!	20% Area Median
	#DIV/0!	30% Area Median
	#DIV/0!	40% Area Median
	#DIV/0!	50% Area Median
	#DIV/0!	60% Area Median
	#DIV/0!	70% Area Median
	#DIV/0!	80% Area Median
	#DIV/0!	Market Units
0	#DIV/0!	**Total**

Rent Levels

# of Units	% of Units	
0	#DIV/0!	20% Area Median
0	#DIV/0!	30% Area Median
0	#DIV/0!	40% Area Median
0	#DIV/0!	50% Area Median
0	#DIV/0!	60% Area Median
0	#DIV/0!	70% Area Median
0	#DIV/0!	80% Area Median
0	#DIV/0!	Market Units
0	#DIV/0!	**Total**

b. The development plans to utilize income averaging........... FALSE

If above is true, should the points based on the units assigned to the levels above **be waived** and not required the set-asides to be included in EUA?

20-30% Levels FALSE 40% Levels FALSE 50% levels FALSE

2. **Unit Detail** FOR YOUR CONVENIENCE, COPY AND PASTE IS ALLOWED WITHIN UNIT MIX GRID

In the following grid, add a row for each unique unit type planned within the development. Enter the appropriate data for both tax credit and market rate units.

	Unit Type (Select One)	Rent Target (Select One)	Number of Units	Number of Units 504 compliant	Net Rentable Square Feet	Monthly Rent Per Unit	Total Monthly Rent
Mix 1							$ -
Mix 2							$ -
Mix 3							$ -
Mix 4							$ -
Mix 5							$ -
Mix 6							$ -
Mix 7							$ -
Mix 8							$ -
Mix 9							$ -
Mix 10							$ -
Mix 11							$ -
Mix 12							$ -
Mix 13							$ -
Mix 14							$ -
Mix 15							$ -
Mix 16							$ -
Mix 17							$ -
Mix 18							$ -
Mix 19							$ -
Mix 20							$ -
Mix 100							$ -
TOTALS			0	0	0.00	$ -	$ -

Total Units	0	**Net Rentable SF:**	**TC Units**	0.00
			MKT Units	0.00
			Total NR SF:	0.00

Floor Space Fraction (to 7 decimals)	#DIV/0!

VHDA Unit Designation Unit Details Page

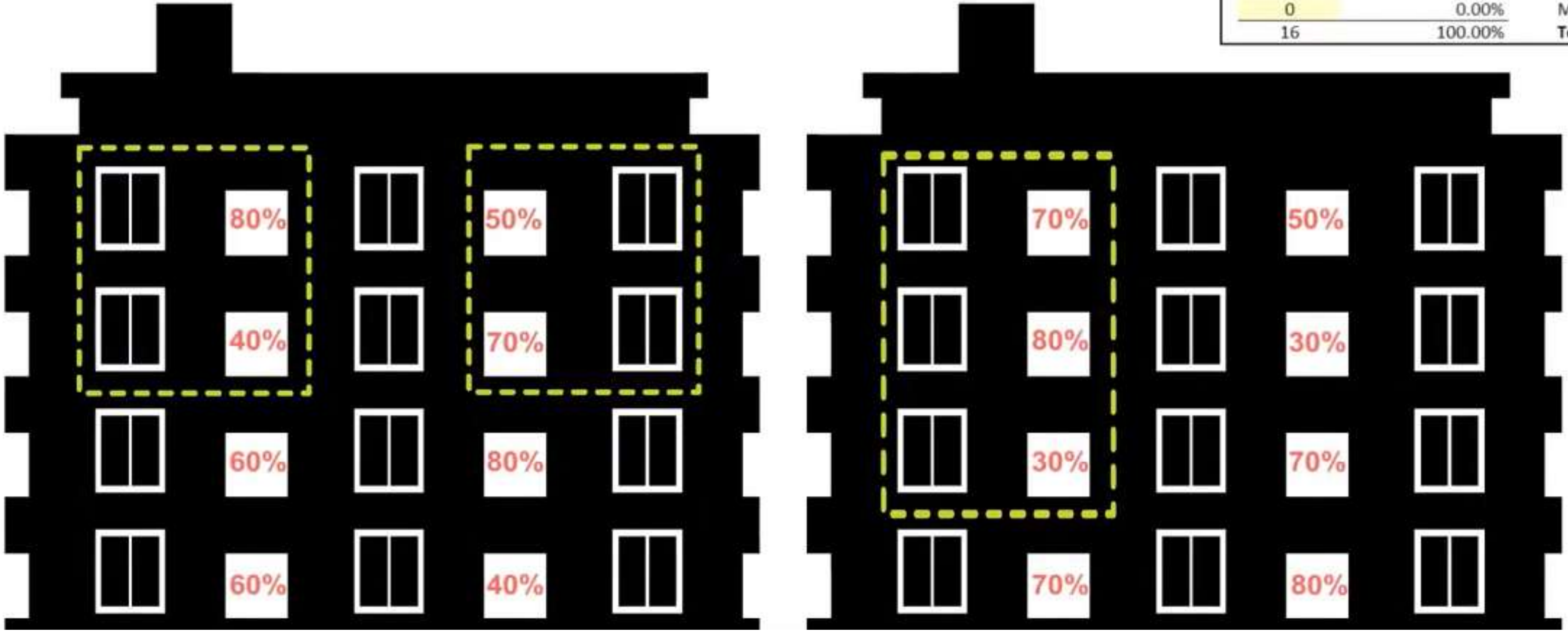
* For training purposes only

Sample Unit Mix for a Project with Average Income

2 buildings
16 units
Minimum of 6.4 or 7 units designated across both buildings

a. Units Provided Per Household Type:

Income Levels		
# of Units	**% of Units**	
0	0.00%	20% Area Median
2	12.50%	30% Area Median
2	12.50%	40% Area Median
2	12.50%	50% Area Median
2	12.50%	60% Area Median
4	25.00%	70% Area Median
4	25.00%	80% Area Median
0	0.00%	Market Units
16	100.00%	**Total**

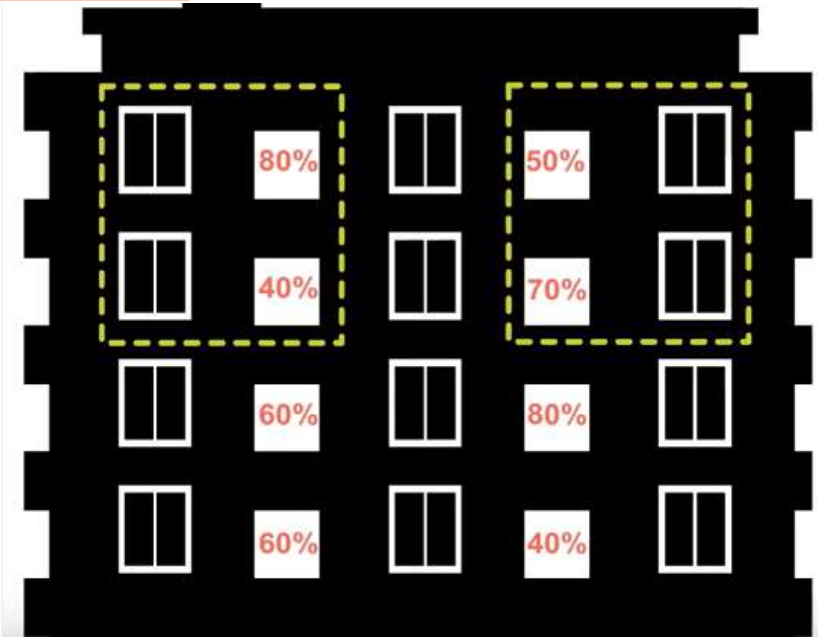


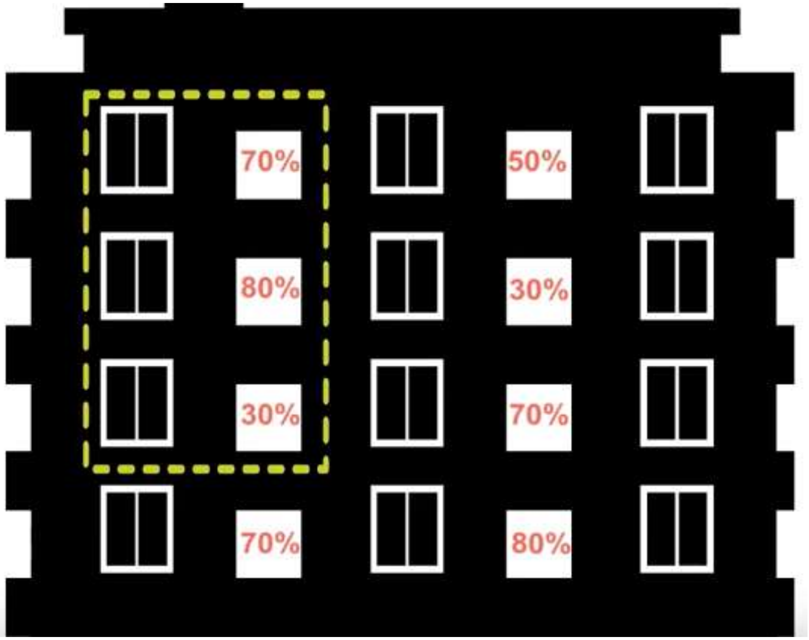
a. Units Provided Per Household Type:

Income & Rent Levels			
# of Units	**% of Units**		
0	0.00%	20% Area Median	**0**
2	12.50%	30% Area Median	**60**
2	12.50%	40% Area Median	**80**
2	12.50%	50% Area Median	**100**
2	12.50%	60% Area Median	**120**
4	25.00%	70% Area Median	**280**
4	25.00%	80% Area Median	**320**
0	0.00%	Market Units	
16	100.00%	**Total**	**960**
	60.00%	**Average Income of Unit Designations**	

a. Units Provided Per Household Type:

Income & Rent Levels			
# of Units	**% of Units**		
0	0.00%	20% Area Median	**0**
1	14.29%	30% Area Median	**30**
1	14.29%	40% Area Median	**40**
1	14.29%	50% Area Median	**50**
0	0.00%	60% Area Median	**0**
2	28.57%	70% Area Median	**140**
2	28.57%	80% Area Median	**160**
0	0.00%	Market Units	
7	100.01%	**Total**	**420**
	60.00%	**Average Income of Unit Designations**	





Math Behind Average Income Set-Aside in Two Scenarios

Consider for Each Scenario

A. Tax Credit Amount
B. Equity Raise
C. Gross Potential Rent

What Are the Potential Benefits of an Average Income Project?

- Broader income band of tenants – may speed lease-up and absorption
- Encourage more diverse mix of tenant incomes
- Higher applicable fraction – more equity possible
- More rents to property – more debt possible

(slides 16 – 18)

Scenario #1 – 100% LIHTC Project

with 40%, 50% and 60% AMI 1-BR Units

Tax Credit Amount & Equity Raise

		100% LIHTC Project 20 Affordable Units 0 Market-Rate Units 40-60 Set-Aside
TAX CREDIT AMOUNT		
A	**Eligible Basis**	$ 7,000,000
B	**Applicable Fraction**	100%
C = A x B	**Qualified Basis**	$ 7,000,000
D	**Applicable Percentage**	9.00%
E = C x D	**Annual Credit Amount**	$ **630,000**
EQUITY CONTRIBUTION		
F = E x 10 years	**Total Annual Credits**	$ **6,300,000**
G = F x $0.95 per $1 of credit	**LIHTC Equity Raise**	$ **5,985,000**

Unity Mix & Gross Potential Rent

GROSS POTENTIAL RENT

Set-Aside	Units	Unit Rent	GPR
Market-Rate	0	$ 1,000	$ -
80% AMI	0	$ 900	$ -
70% AMI	0	$ 800	$ -
60% AMI	10	$ 700	$ 7,000
50% AMI	5	$ 600	$ 3,000
40% AMI	5	$ 500	$ 2,500
30% AMI	0	$ 400	$ -
	20	**Monthly GPR**	**$ 12,500**
		Average AMI *	52.50%

Scenario #2 – Average Income Set-Aside Project
100% LIHTC with 1-BR Units

VJV

Tax Credit Amount & Equity Raise

			100% Tax Credit Project
			20 Affordable Units
			0 Market-Rate Units
			Average Income Set-Aside
TAX CREDIT AMOUNT			
A	**Eligible Basis**	$	7,000,000
B	**Applicable Fraction**		100%
C = A x B	**Qualified Basis**	$	7,000,000
D	**Applicable Percentage**		9.00%
E = C x D	**Annual Credit Amount**	$	**630,000**
EQUITY CONTRIBUTION			
F = E x 10 years	**Total Annual Credits**	$	**6,300,000**
G = F x $0.95 per $1 of credit	**LIHTC Equity Raise**	$	**5,985,000**

Unity Mix & Gross Potential Rent

GROSS POTENTIAL RENT

Set-Aside	Units	Rent	GPR
Market-Rate	0	$ 1,000	$ -
80% AMI	7	$ 900	$ 6,300
70% AMI	0	$ 800	$ -
60% AMI	3	$ 700	$ 2,100
50% AMI	5	$ 600	$ 3,000
40% AMI	5	$ 500	$ 2,500
30% AMI	0	$ 400	$ -
	20	**Monthly GPR**	**$ 13,900**
		Average AMI *	**59.50%**

Scenario Summary

Unit Mix, LIHTC Equity & Monthly GPR

	Project Type	Applicable Fraction	Total 10-Yr Tax Credits	Total Tax Credit Equity	Monthly GPR	Supportable Loan Amount
Scenario #1	40-60 AMI	100%	$ 6,300,000	$ 5,985,000	$ 12,500	277,986
Scenario #2	Average Income	100%	$ 6,300,000	$ 5,985,000	$ 13,900	481,037

But, isn't achieving a higher GPR dependent, in part, on rental market conditions?

Spreadsheet Demonstration of Non-Compliance Uncertainty with the Average Income Set-Aside*

IRS GUIDANCE NEEDED ON WHAT CAUSES US TO FAIL THE MSA!

**** Spreadsheet demo excluded from slide deck posted at VHDA's website.***

Keys to Success for Property Managers of LIHTC Projects with Average Income Set-Aside

Keys to Success for Property Managers

- Communicate, communicate, communicate…. ongoing in all life cycle phases
- Understand elections and expectations of the owner.
- Audit Tenant Files, with a second, maybe even third set of eyes for sign off on all move-ins
- Put together your ‘deal book’ together

  Example in following slides

Content for Property-Level Information Book

- Fully Executed Forms 8609 (acq/rehab vs new construction)
- Owner's AI unit mapping / designations for software set-up
- Extended Use Agreement or LURA
- Annual Utility Allowance Letter (source document (s))
- Annual PHA Utility Allowance

Content for Property-Level Information Book

- Program Information Sheet(s)
- Pricing Packages (Rents, optional fees)
- Resident Selection Criteria
- State Audits (include and Forms 8823)
- Annual Occupancy Status Report
- Special Services Packet (if applicable)
- Written Approval for Exempt Units…for example….

Keys to Success for Property Managers (continued)

- If you're a mixed income project, remember the NEXT AVAILABLE UNIT RULE and how to track it ongoing.
- Clearly Understand Other State and Federal Housing Programs and Requirements.
- Contact state HFA representatives with questions and concerns about your project.
- Annual Professional Development – conferences, webinars, certifications, HFA-sponsored events.

What About the *Next Available Unit Rule*?

Triggered if income of tenant increases above 140% of greater of:

- 60% of AMI or
- Designated income limitation (70% and 80%)

Next vacant unit of equal or smaller size rented to:

- Low income unit - rented at its designated income limit
- Market rate unit - rented at level to keep the average at 60% or below

Next Available Unit Rule – Mixed-Income Project

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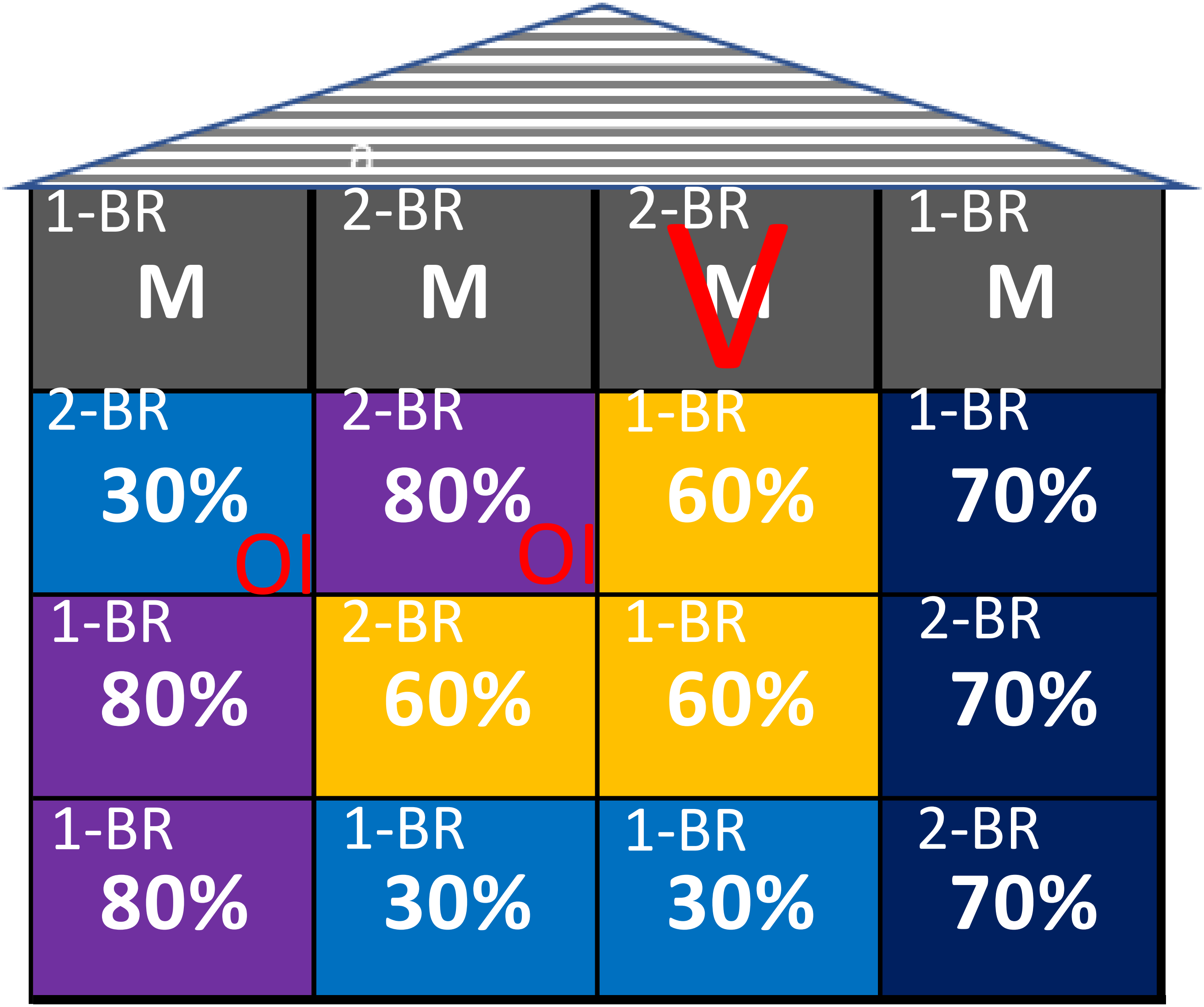


Scenario #1

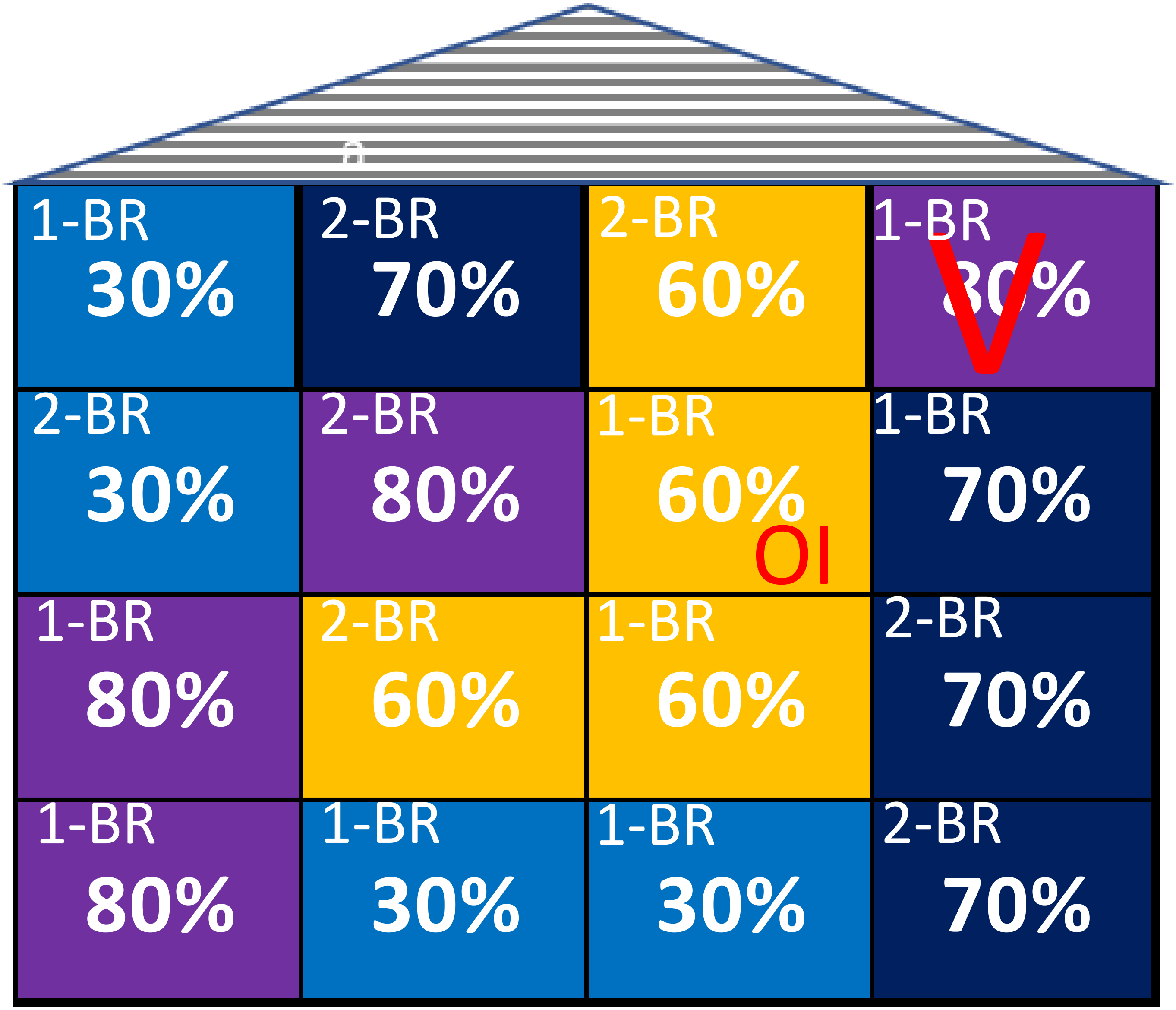
- **Mixed-income project, 1 building**
- **Twelve LIHTC and 4-market-rate units**
- **Designation average: 60%**
- **75% AF**

- **One 30% and one 80% unit go over-income**

- **Then, one market-rate unit goes vacant**

- **Per Section 42 NAUR, we must lease the next available unit to_______________________?**

Next Available Unit Rule – 100% LIHTC Project



Scenario #2

- **One 100% LIHTC project, 1 building**
- **Sixteen 1 an 2-BR units**
- **Designation average: 60%**
- **One 60% 1-BR unit goes over-income**
- **Then, one 80% unit goes vacant**

- **Per Section 42 NAUR, we must lease the next available unit to________________________?**

Additional Considerations and Challenges

- Planning opportunity for A/R deals – look at rent rolls and tenant incomes early.
- Program Integration (HOME)
- Applicability to 4% TEB Projects – VHDA?
- Tracking MSA and NAURA in a Mixed-Income Building / Project

(MRI, RealPage, Other software, spreadsheet?)

Frequently Asked Questions

1. If the NAUR is triggered, is that by building?

2. Wouldn't putting all the 80% units in a separate building violate fair housing laws? True or False

3. Can owners elect to designate the larger LIHTC units for higher-income households, i.e., the 70% and 80% AMI units as shown in the 40-unit project in the table? For example….

NO!

	20% AMI	60% AMI	70% AMI	80% AMI
1 BR	5			
2 BR		5		
3 BR			15	15
Total	5	5	15	15

Designation Average 60.0%

EQUAL HOUSING OPPORTUNITY

4. What's the best practice for property management to track over-income households and next available unit in mixed income AI projects?

Q & A

----------Thank You for Attending Our Session ----------

Presenter Bios

Erica Etterling has been the Compliance Support Manager for the Compliance and Asset Management Department in the Rental Housing Division at VHDA since September 2017 and assists the Director by providing guidance on statutory requirements and evaluating internal operations, policies, and procedures for monitoring the affordable housing programs in the VHDA multifamily portfolio. She has been in the Affordable Housing industry for more than 20 years, and was the Compliance Manager at the Georgia Department of Community Affairs for four years before her current position with VHDA. She began her career as a receptionist for a real estate developer in TN entering into the world of Tax Credits, and has held increasing roles in all areas of development, leasing, management, and monitoring of Federal, State, and local housing programs in several states. She loves all the moving parts in working with affordable housing programs and takes every advantage to gain new knowledge and share her knowledge and experiences with others.

Marie Peace, HCCP, C6P, NCP, FHS, is Vice President of Compliance at the Franklin Johnston Group, located in Virginia Beach, VA. Marie multifamily career began in 1995 as a Community Manager in Central Virginia. By 1996, Marie completed a new community lease up before the project even opened; soon after, she was promoted to Director of Compliance. This role included implementing policies and procedures relating to tax credit housing. Marie spent thirteen subsequent years working with A.J. Johnson Consulting Services completing asset management reviews and auditing files to determine compliance with LIHTC, HUD, HOME Funds, USDA-RD and other state or local housing programs. She also conducted physical inspections to ensure properties were well maintained and in compliance with ADA requirements. Her role with A.J. Johnson Consulting included reviewing files to determine if households would be deemed eligible under Section 42 or other housing programs. In doing so she typically reviewed between 8,000 and 10,000 files annually.

Vinnie Viola, MPA, HCCP, is Principal and Founder of Birch Island Real Estate Consulting, LLC. His company provides asset management consulting services and web-based and private trainings to owners, developers, operators and investors of multifamily housing funded with LIHTC equity. With over 25 years' experience, Vinnie has worked in for-profit, government and not-for-profit organizations that invest in, manage and regulate affordable housing. His career includes ten years in various leadership roles at Boston Financial Investment Management and Boston Capital, through which he gained expertise with asset management best practices. In these roles, Vinnie participated in hundreds of investment committee meetings for prospective tax credit investments. He proactively managed thousands of rental units in hundreds of investment partnerships, comprising over $1 billion in investor contributed equity. Vinnie received his Bachelor of Arts in Geography with concentration in urban planning from the University of Massachusetts Boston and Master of Public Affairs from the University of Texas Dallas. He is an active member of NH & RA's Asset Management Council, a unique peer network that convenes affordable housing executives from multifamily development firms as well as syndicators, tax credit investors and lenders, to develop operational best practices.

Disclaimer

This panel presentation is for training purposes only and should not be construed otherwise. The panelists are not proving LIHTC compliance, legal or tax advice. Please consult with your attorney, accountant or tax advisor for specific advice or information about your LIHTC project circumstances. Similarly, speak with your state housing finance agency representatives about how the new Average Income Set-Aside may apply to your awarded projects and / or future tax credit applications.

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