

Introduction to the Low-Income Housing Tax Credit (“LIHTC”)

WIGGIN AND DANA

Counsellors at Law

Created as part of the Tax Reform Act of 1986 and made permanent in 1993, the LIHTC is an indirect federal subsidy used to finance the construction and rehabilitation of affordable rental housing throughout the United States. This indirect subsidy comes in the form of a federal income tax credit under Section 42 of the Internal Revenue Code (the “Code”), which generally offsets an investor’s federal income tax liability dollar-for-dollar for each LIHTC generated by a project and allocated to such investor. In the absence of the LIHTC program, Congress believed that private developers and investors would not provide a sufficient stock of affordable housing to meet the needs of low-income persons since these types of projects typically do not generate enough profit to warrant the investment. In addition to providing tax credits to subsidize a project, the LIHTC program provides numerous economic and social benefits to the low-income community and facilitates the productive use of abandoned or unused land in both urban and rural communities.

LIHTCs are allocated by the federal government to each state based generally on the state’s total population. In the aggregate, the LIHTC provides state agencies with approximately four billion dollars in annual budget authority that they may use to leverage the vast amount of capital required to fill the affordable rental housing needs of the low-income community. Taxpayers must apply directly to the state or responsible state agency where the project is located for an allocation of LIHTCs

and each state is given the authority to establish their own allocation process and criteria within the limitations set by Code Section 42. In Connecticut, the state agency responsible for administering the LIHTC program is the Connecticut Housing Finance Authority (“CHFA”). Due to the limited number of LIHTCs allocated to each state, the application process is very competitive and most states, including Connecticut, give a preference to project’s with a non-profit sponsor.

The LIHTC can be used in connection with both newly constructed and renovated qualified residential rental buildings and may generally be used in conjunction with historic rehabilitation tax credits and tax-exempt bonds. In order to qualify for LIHTCs, a project must maintain a minimum number of “low-income units” (as defined in Code Section 42) occupied by persons at or below certain area median income thresholds. The amount of LIHTCs allocated to a project is generally based on: (i) the costs of constructing new buildings or acquiring and rehabilitating existing structures; (ii) the types and sources of financing and other funds provided to the project; (iii) the portion of the residential units qualifying as “low-income units”; and (iv) the applicable tax credit percentage as announced by the Internal Revenue Service. Once a project is placed in service, it is generally eligible for LIHTCs every year over a 10-year period. However, in order to continue generating LIHTCs and to avoid having to recapture into income previously taken

Introduction to the Low-Income Housing Credit (“LIHTC”)

WIGGIN AND DANA

Counsellors at Law

LIHTCs, a project must satisfy specific low-income housing guidelines for a full 15-year compliance period. Additionally, as part of the allocation process, state agencies require that a project owner enter into an “extended use agreement” obligating the owner to satisfy certain tax credit compliance rules for a 30-year (and often longer) period. A LIHTC project is also subject to annual reporting requirements, state monitoring, audits and inspections. The specific LIHTC rules under Code Section 42 are extremely technical and often cumbersome in nature. Rest assured, the Wiggin and Dana Affordable Housing, Community Development and Tax Credits Practice Group has substantial experience and expertise in counseling a diverse range of clients in connection with all aspects of LIHTC projects, including structuring transactions, real estate and tax due diligence, and negotiating and preparing documents at all levels and stages of development. Please feel free to contact any member of our team to schedule an appointment.

This advisory is designed to inform clients about recent developments in the fields of real estate law. Nothing in this advisory constitutes legal advice, which can only be obtained as the result of personal consultation with an attorney. The information published here is believed accurate at the time of publication but is subject to change and does not purport to be a complete statement of all relevant issues.

One Century Tower
P.O. Box 1832
New Haven CT
06508-1832
Telephone 203.498.4400
Telefax 203.782.2889

400 Atlantic Street
Stamford CT
06911-0325
Telephone 203.363.7600
Telefax 203.363.7676

450 Lexington Avenue
Suite 3800
New York NY
10017-3913
Telephone 212.490.1700
Telefax 212.490.0536

One CityPlace
185 Asylum Street
Hartford CT
06103-3402
Telephone 860.297.3700
Telefax 860.525.9380

Quaker Park
1001 Hector Street, Ste. 240
Conshohocken PA
19428-2395
Telephone 610.834.2400
Telefax 610.834.3055