



# Housing Tax Credit Compliance Manual

July 2019

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## Preface

This manual is a training and reference guide for the administration of the Housing Tax Credit (HTC) Program for South Dakota. It is intended to answer questions regarding procedures, rules, and regulations that govern the HTC developments. The manual should be used in conjunction with, and as a supplement to, Section 42 of the Internal Revenue Code. If a determination is made that any provision of this manual is in conflict with Section 42 of the Internal Revenue Code, the Internal Revenue Code will govern.

The laws and regulations governing the Housing Tax Credit (HTC) program as well as the interpretation of these laws can and do change. Owners and Managers should keep current on all changes in the Internal Revenue Code and the Code of Federal Regulations that may affect their properties. This may require consulting qualified legal and tax professionals for advice.

Compliance monitoring by South Dakota Housing Development Authority (SDHDA) will be administered through the Rental Housing Management division.

This Housing Tax Credit Compliance Manual can be accessed at [www.sdhda.org](http://www.sdhda.org).

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In 1986, the Tax Reform Act enacted by Congress 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 Housing Tax Credit (HTC) program which began in 1987 and received permanent authorization with the Omnibus Budget Reconciliation Act of 1993. HTCs provide incentive 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. Housing Tax Credits are not considered a Federal subsidy.

### **The Owner**

The owner is responsible for compliance with the IRS code. Any and all financial consequences to the owner as a result of noncompliance, whether identified by SDHDA or by the IRS, will be the responsibility of the owner.

The owner is responsible for ensuring that the development is in compliance with Section 42 and all pertinent procedures, rules and regulations that apply to rental housing. This includes all site staff located at the property level.

### **South Dakota Housing Development Authority (SDHDA)**

SDHDA is assigned the responsibility of compliance monitoring under Section 42 (m)(1)(B)(iii) of the IRS code.

The initial inspection is due by the end of the calendar year following the year the last building is placed in service. The initial Housing Tax Credit (HTC) review consists of a review of the tenant files and physical inspection of the property and units.

After the initial review, once every three years SDHDA will conduct an on-site physical inspection and review the tenant files that are within the extended use period. On February 26, 2019, 26 CFR 2019-03388 changed the sample size from at least 20 percent of the low income units to an on-site review and low-income certification review of not fewer than the minimum number of low-income units for the corresponding number of low-income units in the low-income housing project set forth in the table to paragraph (c)(2)(iii) that is listed below.

Number of low-income units in the low-income housing project	Number of low-income units selected for inspection or for low-income certification review (minimum unit sample size)
1	1
2	2
3	3
4	4
5-6	5
7	6
8-9	7
10-11	8
12-13	9
14-16	10
17-18	11
19-21	12
22-25	13
26-29	14
30-34	15
35-40	16
41-47	17
48-56	18
57-67	19
68-81	20
82-101	21
102-130	22
131-175	23
176-257	24
258-449	25
450-1,461	26
1,462-9,999	27

The selection of units is a random sample chosen at the time of the site review. No advance notice may be given as far as unit selection or tenant file selection. If a review of the tenant files is conducted one day and the physical inspection is conducted on another, different units are to be chosen, if possible. Notice is to be given only 15 days in advance of the review. Low income units that are within the extended use period and have completed the compliance period will be subject to a review of 20% of the low-income units and 20% of the tenant files, both randomly selected. In the event extensive non-compliance is found, the sample size may be expanded.

SDHDA is to notify the owner and management agent within 30 days if SDHDA discovers during an audit, inspection or review that the development is not in compliance with the Code.

The owner has an opportunity to correct noncompliance within 90 days from the date of the letter or email sent to the owner. An extension of up to six months may be granted by SDHDA for good cause as determined by SDHDA.

SDHDA is required to notify the IRS of an owner's potential noncompliance no later than 45 days after the end of the allowed time for correction, whether or not the noncompliance is corrected. SDHDA will notify the IRS by filing Form 8823, explaining the nature of the noncompliance and indicating whether the owner has corrected the noncompliance.

The IRS released the Guide for Completing Form 8823, Low-Income Housing Credit Agencies Report of Noncompliance or Building Disposition in January of 2007. It was updated in September of 2009 and in January of 2011. The 8823 Guide gives guidance on what is considered noncompliance and what steps need to be taken to correct noncompliance.

### *Record Retention*

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Records are to be retained for each building for a minimum of six years after the due date for that year's federal income tax return. In the event an extension is filed, the starting period is when the return is actually filed with the IRS.

The records for the first year of the credit period must be retained for at least 21 years. The compliance period runs 15 years and tax returns must be retained for every year of the compliance period plus at least 6 years after the due date for filing the tax return for the last year of the compliance period.

Electronic storage systems may be used instead of paper records. You must have a way to access the records. For example if a computer disc is used, a machine to read the disc must be available.

SDHDA recommends a duplicate set of the original files be stored at a location other than where the original records are stored.

Owners must maintain applicant and tenant information in a way to ensure confidentiality, such as locked doors and file cabinets. Records must be disposed of in a way that personal information is safeguarded, such as shredding or pulverizing.

## ***Program Elections***

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IRS Form 8609 – Please pay particular attention to the elections that were selected under Part II of the 8609, as the elections are used to determine how the property is monitored.

### **Minimum Set Aside Election**

Owners elect one of three options. They are:

1. 20/50 – 20% of the units must be occupied by tenants whose incomes are 50% or less of area median income (AMI).
2. 40/60 – 40% of the units must be occupied by tenants whose incomes are 60% or less of area median income (AMI).
3. Average Income Test – At least 40% of the units are rent restricted and occupied by individuals whose income does not exceed the imputed income limitation designated by the taxpayer with respect to the respective unit. The designated percentage may be 20, 30, 40, 50, 60, 70 or 80 percent. Further, the average of the designated income limits of the respective units cannot be greater than 60%, which is called the Average Test.

Each building is considered a separate project under IRC Section 42(g)(3)(D). The minimum set-aside election applies to each building separately unless the owner elects to treat the building as a multiple-building project. That election is noted on the 8609, Part II, line 8b. The election once made, is irrevocable.

### **Rent and Income Limits**

The Housing Economic Recovery Act of 2008 (HERA) uses the Multifamily Tax Subsidy Income Limits Summary (MTSP Income Limits). They are published annually by the United States Department of Housing and Urban Development (HUD). The income limits are posted under the HUD data sets. The placed in service date determines the correct income limit table that should be utilized.

All buildings within a multiple building project (line 8b on the 8609 is checked “yes”) use the earliest placed in service date.

Each building uses a separate placed in service date if the project is not a multiple building project (line 8b on the 8609 is checked “no”).

As a resource, the *Novogradac* website under the income and rent calculator is a great tool to check to see if you have the correct income and rent limits for your property.

### **Compliance Period**

This is a 15 year period that the IRS monitors for compliance. The first year that credits are claimed start the compliance period. The end of the 15<sup>th</sup> year runs until December 31<sup>st</sup>.

### **Extended Use**

Beginning with 1990 allocations, extended low income housing commitments, also known as restrictive covenants detailed in the Declaration of Land Use Restrictive Covenants became a requirement of the HTC program. The restrictive covenants are recorded at the Register of Deeds in the county the development is physically located. The extended use provision runs at least an additional 15 years after the end of the compliance period. Every Declaration of Land Use Restrictive covenant is project specific, based on the owner's elections at application.

### **Eligible Basis x Applicable Fraction = Qualified Basis**

Generally, eligible basis is the dollar amount spent on the construction or acquisition costs of a building minus items such as land, federal grants and soft costs.

The cost of depreciable property used in common areas or provided as comparable amenities to all residential units is generally included in eligible basis.

An example of this would be carpeting in the common area. The cost of tenant facilities may be included in eligible basis if there is not a separate charge for the use of the facility and they are made available on a comparable basis to all tenants in the project. An example of this is a swimming pool or garages.

Other factors in determining eligible basis are the qualified census tract and difficult development areas.

The applicable fraction is the lesser of the unit fraction or the floor space fraction.

The unit fraction is the number of HTC units in the building divided by the total number of residential units in the building.

The floor space fraction is the total floor space of the HTC units in the building divided by the total floor space of the residential rental units in the building.

The applicable fraction after the first year should remain constant. Year one is prorated based on the applicable fraction at the end of the month starting after the first full month the building is placed in service.

## ***Compliance Requirements***

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It is a requirement to keep separate records for each qualified low income building in the development. These records need to be maintained for each year in the compliance period and extended use period showing the following information:

- Total number of residential rental units in the building, including the number of bedrooms and square footage for each residential rental unit;
- Percentage and number of residential rental units in the building that are low income units;
- Rent charges for each residential rental unit in the building, including utility allowances and any additional optional and non-optional charges to the tenant;
- Number of occupants in each low income unit;
- Low income unit vacancies in the building and information that shows when, and to whom, the next available units were rented;
- Initial low income certification for each low income tenant;
- Documentation to support each tenant's initial income and student status;
- Annual re-certifications or Annual Household Certification Updates including student status for each low income household;
- Eligible basis and qualified basis of the building at the end of the first year of the credit period and each year of the credit period; and
- Character and use of the nonresidential portion of the building included in the building's eligible basis under the Code (e.g. tenant facilities that are available on a comparable basis to all tenants and for which no separate fee is charged for use of the facilities, or facilities reasonably required by the development).

### *Web Compliance Management System*

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In order to begin using the Web Compliance Management System (WCMS), the Owner or Management Agent will need to request a WCMS Authorization Form from SDHDA. After the WCMS Authorization Form is completed and returned, a message will be sent notifying the Owner/Management Agent that they can log into WCMS to register. Once the user has registered they should notify SDHDA and the approval process can be completed. SDHDA will notify the user when the approval process is complete and the user can begin using the system.

Please do not share passwords as this is a secure system. In addition, please notify SDHDA if a staff member that had access to WCMS leaves your employment or changes

jobs. The employee will continue to have access to the system and your data until we are notified that user should be removed from the system.

## *Annual Reporting Information*

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The following is to be submitted to SDHDA annually:

- Annual Owner Certificate of Continuing Program Compliance;
- Tenant data for the year; via Web Compliance Management System (WCMS)
- Authorized Representative Designation (if applicable);
- Utility allowance(s) applicable for the reporting year.

Certification provisions of the Code require the owner of a low income housing project to certify at least annually to SDHDA that the property meets the following criteria for the preceding 12 month period. This is accomplished through the submission of the Annual Owner Certificate of Continuing Program Compliance. E-mail submissions are accepted.

The following questions are verified annually by the Owner.

- The minimum set-aside of 20-50, 40-60 or Average Income Test;
  - At least 20 percent or more of the residential units in the development are both rent-restricted and occupied by individuals whose income is 50 percent or less of area median income;
  - At least 40 percent or more of the residential units in the development are both rent-restricted and occupied by individuals whose income is 60 percent or less of area median income; or
  - Average Income Test where at least 40% of the units are rent restricted and occupied by individuals whose income does not exceed the imputed income limitation designated percentage may be 20, 30, 40, 50, 60, 70 or 80 percent. Further the average of the designated income limits of the respective units cannot be greater than 60%.
- Did the applicable fraction of any building in the development change? If a change occurred, a description of the change is needed;
- Did the owner have an annual low income certification or Annual Household Certification Update from each low income tenant and documentation to support that certification?

- Were the designated low income units rent-restricted as defined in the Code?
- Were all units in the development for use by the general public and used on a non-transient basis?
- Were there any findings of discrimination under the Fair Housing Act?
- Were all units in the development suitable for occupancy taking into account local health, safety, and building codes?
- Is there a change in the eligible basis? If there has been a change, an explanation of the change is needed;
- Are all tenant facilities included in the eligible basis provided on a comparable basis without a separate fee to all tenants residing in the development?
- Are reasonable attempts made to rent a unit of comparable or smaller size to qualifying tenants after a unit is vacated prior to renting to a non-qualified household?
- As the tenant income increases above the maximum income limit, is the next available unit of comparable or smaller size rented to tenants having a qualifying income?
- Did the owner refuse to lease a unit in the development to an applicant because the applicant holds a voucher under Section 8?
- Did the qualified non-profit organization and its non-profit entity materially participate in the operation of the development?
- Has the ownership changed? If yes, please provide an explanation;
- Did the development receive a health/safety violation from a local government entity?
- Were any tenants evicted for other than good cause?

All tenant data for January-December of the prior year must be submitted through WCMS. The due date for the reporting is the first Friday in March.

A copy of the utility allowance that was in effect for January-December of the reporting year must be submitted.

In the event the reports are not received by the due date, after the owner is notified and there is no response, an IRS form 8823 will be filed with IRS, as required by the Code.

At recertification if a household's income increases over 140% of the current qualifying income limit, the unit becomes "over income." Credits can continue to be claimed on a unit as long as the next available unit of equal or smaller size in the same building is rented to a qualified applicant. Units over 140% must remain rent restricted until the next available unit is rented. If the rule is violated, all 140% units fall out of the applicable fraction and minimum set-asides.

Only units that have been previously occupied by an eligible household and are suitable for occupancy may be included for compliance purposes. If a unit has never been occupied by an eligible household, or was a market rate unit, neither are counted as qualifying households.

### **Rent Requirements**

Units in developments receiving HTC allocations must be rent-restricted to comply with the low income set-aside requirements. A residential unit is rent-restricted if the gross rent with respect to such unit does not exceed 30 percent of the imputed income limitation applicable to such unit. The gross rent must include an allowance for tenant-paid utilities. The Declaration of Land Use Restrictive Covenant spells out development specific rent restrictions.

Because the Declaration of Land Use Restrictive Covenants are project specific and the rent/income limits are project specific, based on the placed in service dates, we recommend using the Novogradac Income and Rent Calculator. Rent changes based on updated rent limits are to be made only at move-in or at time of annual recertification.

The rent calculation after January 1, 1990, is based on the number of bedrooms in the unit as opposed to the actual family size.

The maximum rent for a one bedroom unit is determined by using the average of the one and two person income limits. One bedroom units are assumed to be occupied by 1.5 persons. The average would be multiplied by 30% and divided by 12 to get the monthly rent.

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, cable television or internet. Whenever the tenant directly pays utility costs, a utility allowance must be used to determine the maximum unit rent that may be charged.

In the event that the rent charged is greater than the maximum HTC rent and is determined to be out of compliance, the unit ceases to be a low income unit for the remainder of the owner's tax year. A unit is back in compliance on the first day of the owner's next tax year if the rent charged on a monthly basis does not exceed the limit. An owner cannot avoid the disallowance of the tax credit by rebating the excess rent or fees to the affected tenants.

The initial rents established at reservation and recorded in the Declaration of Land Use Restrictive Covenants must be utilized until the earlier of one year measured from the date the unit is occupied or the period of initial occupancy. Please review your Declaration of Land Use Restrictive Covenants as the document is project specific and in some instances limits the rent increase.

### **Utility Allowances**

The IRS requires that utility allowances be set according to 26 CFR 1.42-10 (April 24, 1994), effective May 2, 1994, and amended July 29, 2008.

A building owner must review at least once during each calendar year the basis on which utility allowances have been established and must update the applicable utility allowance. The review must take into account any changes to the building such as any energy conservation measures that affect energy consumption and changes in utility rates. The owner has 90 days from the effective date of the new allowance to implement the utility allowance.

The building owner must retain any utility consumption estimates and supporting data as part of the taxpayer's records.

If a utility (other than telephone, cable television or internet) is paid directly by the tenant, the gross rent includes a utility allowance. If all utilities are paid by the owner the utility allowance is zero.

The building owner is not required to review the utility allowances, or implement new utility allowances, until the building has achieved 90 percent occupancy for a period of 90 consecutive days or the end of the first year of the credit period, whichever is earlier.

#### **Building Assisted by Rural Development**

If a building receives assistance from Rural Development (RD), the applicable utility allowance for all rent-restricted units in the building is the RD utility allowance. In the event a tenant received other state or federal assistance, the RD utility allowance is used.

If any tenant in a building receives Rural Development rental assistance, the applicable utility allowance for all rent-restricted units is the applicable Rural Development utility allowance, including any tenants receiving rental assistance payments from HUD.

#### **Building regulated by the Department of Housing and Urban Development**

If the rents and utility allowances of the building are reviewed by HUD on an annual basis (HUD-regulated building), the applicable utility allowance for all rent-restricted units in the building is the applicable HUD utility allowance.

If a tenant in a building receives tenant-based Section 8 assistance, owners must use the utility allowance from the Public Housing Authority (PHA) administering the assistance. The PHA utility allowance would only be for the unit that was occupied by the resident receiving the Section 8 assistance.

For building owners that do not receive RD or Section 8 Assistance, the following options may be used to calculate utility allowances.

#### **Public Housing Agency - PHA**

A building owner may obtain a utility estimate for each unit in the building from the PHA that has jurisdiction over the building, provided the PHA agrees to provide the estimate. The estimate is obtained when the building owner receives, in writing, information from the PHA providing the estimated per-unit cost of the utilities for units of similar size and construction for the geographic area in which the building is located. The PHA estimate may be obtained by a building owner at any time during the building's extended use period. Costs incurred in obtaining the estimate are paid for by the building owner.

#### **HUD Utility Schedule Model**

A building owner may calculate a utility estimate using the "HUD Utility Schedule Model" that can be found on the Low Income Housing Tax Credits page at <http://www.huduser.org/portal/resources/utimodel.html>. Utility rates used for the HUD Utility Schedule Model must be no older than the rates in place 60 days prior to the effective date of the utility allowance.

#### **Utility Company Estimate**

Any interested party, including a tenant, building owner or agency may request the utility company estimate of utility consumption in the building's geographic area. The estimate is obtained when the interested party receives, in writing, information from a local utility company providing the estimated cost of that utility for a unit of similar size and construction for that geographic area. Costs are the responsibility of the person requesting the estimate. The party that obtains the estimate must retain the original of the utility company estimate and must furnish a copy to the owner and the monitoring agency. The owner of the building must make copies available to all tenants in the building. In the case of the deregulated utility services, the interested party is required to obtain an estimate only from one utility company even if multiple companies can provide the same utility service to a unit. The utility company must offer services to the building in order for that company's rate to be used.

#### **Energy Consumption Model**

A building owner may calculate utility estimates using an energy, water and sewage consumption analysis model (energy consumption model). The energy consumption model must, at minimum, take into account specific factors including, but not limited to unit size, building orientation, design and materials, mechanical

systems, appliances and characteristics of the building location. The utility consumption estimates must be calculated by either a properly licensed engineer or a qualified professional approved by SDHDA that has jurisdiction over the building. Use of the energy consumption model is limited to the building's consumption data for the twelve-month period ending no earlier than 60 days prior to the beginning of the 90-day period, and utility rates used for the energy consumption model must be no older than the rates in place 60 days prior to the effective date of the utility allowance. In the case of newly constructed or renovated buildings with less than 12 months of consumption data, the qualified professional may use consumption data for the 12 month period of units of similar size and construction in the geographic area in which the building containing the units is located.

### **Agency Estimate**

This method is not offered by SDHDA.

### **Owner's Average of Actual Consumption Utility Allowance Procedure**

A building owner may calculate utility estimates using actual consumption data. The method to calculate the estimate is:

- 1) Request utility data from either the utility company or the tenant household for at least the number of units determined by the sample size methodology detailed below. This must be done for each bedroom size at the property. If the property consists of multiple identical buildings, then the sampling can be performed at the property level for each bedroom size. If the buildings are different, sampling must be done for each building.

A unit should be excluded from the sample if it:

- a) Is receiving an increased utility allowance as a reasonable accommodation;
  - b) Has been vacant for more than 2 months. Units included in the sample should have at least 10 months of occupancy; or
  - c) Is receiving a flat utility rate as part of a low-income rate assistance program.
- 2) Determine the average utility cost for each bedroom size without removing any units from the analysis beyond those excluded from the same sample size as indicated in (1) above.

Do not remove the highest or lowest utility cost household when determining the average.

#### **Recommended Sample Size**

1-20 Units – All

21-61 Units – 20

62-71 Units – 21

72-83 Units – 22  
84-99 Units – 23  
100-120 Units – 24

Failure to maintain or provide the utility allowance and supporting documentation annually is considered noncompliance. Without proof of the allowance amount, the rent cannot be correctly calculated. An incorrect utility allowance may result in noncompliance for rents that exceed the tax credit rent limits.

### **Submetered Utilities**

Submetering is when a building owner purchases a utility from a utility company and then separately charges the tenants for the utility. In those situations, if the utility costs paid by a tenant based on actual consumption in a submetered, rent-restricted unit and if certain other requirements are satisfied, then the charges for the utility are treated as paid by the tenant directly to the utility company, even though the payment passes through the building owner. This also applies to situations in which a building owner sells to tenant's energy that is produced from a renewable source and that the owner did not purchase from or through a local utility company. The submetered utility charge does not count against the maximum rent that the building owner can charge. The rent that the owner may require from the tenant is reduced by the utility allowance.

### **Leasing**

The initial HTC lease is required to be for a duration of six months or greater. "Transient" is not defined in Section 42 or other IRS regulations, but the legislative history of Section 42 describes a "safe harbor" which states that leases within the initial term of six months which can then revert to a month-to-month tenancy are considered "non-Transient." Section 42 specifically provides that a single-room occupancy (SRO) unit may be rented on a month-by-month basis without it being considered "Transient."

All adults 18 years and over are required to sign the lease. SDHDA recommends student status, good cause evictions and required annual reporting be addressed in the HTC lease.

### **Fees**

Fees as a condition of occupancy or non-optional charges are included in the cost of services that are required as a condition of occupancy must be included in gross rent. (Treasury Regulation 1.42-11(a) (3)).

Application fees may be charged to cover the actual cost of the application processing, credit and criminal history checks and landlord references. The fee is limited to recovery of the actual out-of-pocket costs.

Security deposits and pet deposits may be charged. A monthly pet fee may be charged for pets. You may not charge a fee or deposit for a service animal.

### **Number of Persons Per Unit**

There is no HTC regulation governing the number of persons allowed to occupy a unit based on size. It is important to be consistent when accepting or rejecting applications. It is recommended the owner determine the minimum and maximum number of people that will be allowed to occupy each size unit and document it in writing as part of the Management Plan and Tenant Selection Plan.

### **Households and Family Size**

As a general rule, a “household” consists of all individuals (or tenants) residing in a unit. To determine the household income limit, all applicable income standards are adjusted for family size.

For Tax Credit purposes the following occupants are not considered part of the household: live-in aids, foster children, foster adults and guests.

For HTC purposes the following are included in the household: Children temporarily absent due to placement in a foster home, children in joint custody who are present in the household 50% or more of the time, children who are away at school but live with the family during recesses, unborn children of pregnant women, children who are in the process of being adopted, temporarily absent family members who are still considered family members, family members in the hospital, or a rehabilitation facility for periods of limited or fixed duration.

The family decides if persons permanently confined to a nursing home or hospital are included when determining family size for income limits.

## *Qualification of Applicants*

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Applicants for low income, rent-restricted units should be advised early in their initial visit to the development that there are maximum income limits and student status restrictions that apply to the units. Management should explain to prospective tenants that the anticipated income of all persons expecting to occupy the unit must be verified prior to occupancy and financial and student status will be reviewed annually.

### **Initial Certification**

SDHDA recommends the use of the Tenant Income Certification form. If the property is a Section 8/HTC property, a Tenant Income Certification form for the initial certification is required by SDHDA. The owner must verify all income and assets to determine if the household is income eligible. The income of every prospective household member must be verified.

The Tenant Income Certification effective date should be the date the household moves into the unit.

### **Annual Recertification**

### **100% Tax Credit building**

Effective January 1, 2009, if all the low income units in the development are 100% low income, the owner is not required to complete an annual tenant income recertification for each household. However, the owner is required to have each household complete a self-certification form called the "Annual Household Recertification Update." The form must be completed any time prior to 120 days of the anniversary date of move-in. Please include a student verification form with each annual update to document student status each year. It is very important to review the form and make sure that it is fully completed, signed and dated.

### **Mixed Use Buildings**

Buildings that have both market rate units and HTC units must have a complete recertification packet on file for the HTC units to determine if the Available Unit has been applied correctly.

Upon the anniversary date of the tenant's move-in or anytime within 120 days prior to the anniversary, a subsequent Tenant Income Certification must be completed and all resident income/assets/student status verified.

A unit does not lose its status as a low income unit solely because of an increase in the household's income. Once a unit qualifies as a low income unit it continues to qualify as such until the tenant's income exceeds 140 percent of the applicable income limit. Even then, the unit remains a low income unit as long as the owner continues to fill vacancies in comparable or smaller units with tenants who qualify as low income tenants and the units continue to be rent restricted. Tenants whose income exceeds 140 percent of median income are not allowed to relocate to another unit within the same development.

### **Students**

A unit is not considered an eligible HTC unit if all the occupants of such unit are full time students.

IRC 151 (c)(4) defines, in part, a "student" as an individual, who during each of 5 calendar months during the calendar year in which the taxable year of the taxpayer begins, is a full-time student of an educational organization described in IRC 170(b)(1)(A)(ii). Treasury Regulation 1.151-3(b) further provides that the five calendar months need not be consecutive.

The determination of student status as full or part-time should be based on the criteria used by the educational institution the student is attending. Part-time student status should be verified with the educational institution. If one household member is a part-time student and all other household members are full-time students, the household is eligible.

An educational organization, as defined by IRC 170(b)(1)(A)(ii), is one that normally maintains a regular faculty and curriculum, and normally has an enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. The term "educational organization" includes elementary schools, junior and senior

high schools, colleges, universities and technical, trade and mechanical schools. It does not include on-the-job training courses.

There are exceptions to the full-time student status outlined in IRC 42(i)(3)(D). The section provides that a unit shall not fail to be treated as a low income unit merely because it is occupied by either an individual who is:

- A student receiving assistance under Title IV of the Social Security Act, (TANF). Verification would be a TANF award letter.
- A student enrolled in a job training program receiving assistance under the Job Training Partnership Act, (Workforce Investment Act replaced the Job Training Partnership Act), or under other similar Federal, State or local laws. Verification would be a copy of the assistance award letter.

Or entirely by full-time students if such students are:

- Single parents with children all of whom are students and such parents and children are not dependents (as defined in IRC 152) of another individual and are not dependents of another individual other than a parent of such children. Verification would be a copy of the tax return or divorce decree.
- Married and filing a joint return or are entitled to file a joint return. Verification would be a copy of their tax return or marriage certificate.

Effective for verifications after July 30, 2007, a full-time student would qualify if one of the members of the household included a member who formerly received foster care assistance. Verification would be foster care paperwork from social services.

Revenue Ruling 2013-17 – Recognizes same-sex marriages (married in any state) that would meet the married and filing a joint return exception.

If a previously qualified household becomes a full-time student household and does not meet any of the exceptions, the household will not be in compliance and is not a qualified student household.

### **Change in Household Composition**

SDHDA recommends not adding additional household members for six months after the initial household moves into the unit.

Addition of new member(s) to an existing low income household requires the income certification for the new member(s) of the household, including the third-party verification. The new member's income is added to the income disclosed on the existing Tenant Income Certification. The household continues to be income-qualified, and the income of the new member plus the existing household's income is taken into account for purposes of the Available Unit Rule under IRC 42(g)(2)(D).

Decrease in household size does not trigger the immediate completion of a new Tenant Income Certification. The next Tenant Income Certification completed will show the household size decreased and their income/assets will be removed.

A household may continue to add members as long as at least one member of the original low income household continues to live in the unit. Once all the original tenants have moved out of the unit, the remaining tenants must be certified as a new income-qualified household.

### **Unit Transfers**

Unit transfers are handled differently depending upon whether the transfer is within the same building or it is to a different building.

- **Transfer within the same building**

The household moves to a different unit in the same building, the newly occupied unit adopts the status of the vacated unit.

- **Transfer to a different building**

It depends on the household's area median income and the election made on the 8609, part b. The household cannot transfer if the household income is over 140% of the income limit. Households under 140% of the income limit residing in 100% HTC developments, can transfer between buildings in the development.

Please note – If on the 8609, part 8b, the election was “no,” you cannot transfer the tenants without first going through the initial income eligibility process and qualifying the household.

The recertification will be due on the anniversary of the original move-in date.

### **Manager/Security Unit**

The adjusted basis of the unit occupied by a manager is includable in the Eligible Basis of the building under IRC 42(d)(1) as a facility reasonably required for the benefit of the development. However, the unit is excluded from the Applicable Fraction of the building under IRC 42(c)(1)(B).

The manager is not required to be income qualified. The manager position is required to be full-time. The number of hours worked does not define full-time.

Typically, a security officer provides on-site presence during the evening and nighttime hours to respond to any emergencies and disturbances, and to respond to residents' requests for assistance, including complaints, unauthorized visitors, improper parking and unauthorized use of community facilities. Other encouraged activities may include conducting resident background investigations, neighborhood watch programs and educational activities for primary school-age residents.

Conversion of the unit from a manager's unit to a HTC unit must have prior written approval from SDHDA before the unit is converted, as does converting a HTC unit to a manager's unit.

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### *General Income and Asset Verification Requirements*

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All income sources, including asset income, must be verified. Annual income includes all amounts that are not specifically excluded by regulation. Exhibit 5-1 of HUD Handbook 4350.3, Income Inclusions and Exclusions provide a complete listing of income inclusions and exclusions.

Acceptable methods of verifying information include the following:

#### **Written**

Written documentation sent directly by a third-party source is the preferred method of verification. It is assumed that third-party sources will send written verification to the owner through the mail or via email.

The applicant or tenant should not hand-carry the verification to or from the third-party source. If the verification does not contain an original signature or is delivered by the applicant or tenant, the owner should examine the documents for evidence of tampering. In these situations the owner may, but does not have to accept the document as acceptable verification.

If the information is not complete the owner must follow up with the source to obtain complete information.

#### **Oral**

Oral verification, by telephone, from a reliable third-party source is an acceptable verification method, mostly used for clarification. Owners frequently use this method when the third party does not respond to a written verification request. When verifying information over the telephone, it is important to be certain that the person on the telephone is the party he or she claims to be. Generally, it is best to telephone the verification source rather than to accept the verification from a source calling the development management office. When verifying information by phone, the owner must record and include the following information.

- Third-party's name, position and contact information;
- Information reported by the third party;
- Name of the person who conducted the telephone interview; and
- Date and time of telephone call.

## **Electronic**

The owner may obtain accurate third-party written verification by facsimile, e-mail or internet, if adequate effort is made to ensure that the sender is a valid third-party source.

Fax - Information sent by fax is most reliable if the owner and the verification source agree to use this method in advance during a telephone conversation. The fax should include the company name and fax number of the verification source.

E-mail - Similar to faxed information, information verified by e-mail is more reliable when preceded by a telephone conversation and/or when the e-mail address includes the name of an appropriate individual and firm.

Internet - Information verified on the internet is considered third-party verification if the owner is able to view web-based information from a reputable source on the computer screen. Use of the print-out is also acceptable.

When third-party documentation is not available, owner must document in the file efforts made to obtain the required verification and the reason the verification was not obtained.

The owner must include the following documents in the tenant file:

- A written note to the file explaining why third-party verification is not possible; or
- A copy of the date-stamped original request that was sent to the third-party;
- Written notes or documentation indicating follow-up efforts to reach the third-party to obtain verification; and
- A written note to the file indicating the request has been outstanding without a response from the third-party.

Management should give the applicant the opportunity to explain any significant differences between the amounts reported on the application and amounts reported on third-party verification in order to determine actual income. The file must be documented to explain the difference.

## **Effective Term of Verification**

Verifications are valid 120 days from the date of receipt, not the effective date of the Tenant Income Certification. If verifications are more than 120 old, new verifications must be obtained.

## **Section 8 Tenant Income and Asset Verification**

The annual income for a household receiving housing assistance payments under Section 8 Choice Voucher may be verified by obtaining a statement from the Public Housing Authority (PHA). The owner must submit the Section 8 Eligibility Verification to the PHA for completion. If the form shows that the tenant's income does not exceed the applicable income limit, the household is eligible to occupy a rent-restricted unit. However, SDHDA requires for the first year rent-up files, actual Tenant Income Certifications and corresponding third-party documentation are to be used to document the first year tenant files.

### **Calculating Annual Income**

Annual income is the gross income the household anticipates it will receive from all sources, including earned and unearned income and income from assets.

Examples of earned/unearned income includes, but is not limited to gross wages, salaries, tips, overtime, social security, welfare, unemployment compensation and worker's compensation.

Examples of asset income include bank accounts, retirement accounts, real estate and other investments (not including personal items).

Please refer to HUD Handbook 4350.3 for a complete listing and discussion of earned/unearned income and asset income.

Income determination is based on the annual gross income a household anticipates it will receive for the 12-month certification period. Verification of all sources of current and anticipated income for all household members age 18 and older, person under the age of 18 who are treated as adults because they are the head, co-head or spouse (emancipated minors) and unearned income of minor children must be obtained in order to establish that the income limit is not exceeded.

Owners must convert all verified incomes to annual amounts. To annualize full-time employment, multiply:

- Hourly wages by 2080 hours;
- Weekly wages by 52;
- Bi-weekly amounts by 26;
- Semi-monthly amounts by 24; and
- Monthly amounts by 12.

To annualize income from other than full-time employment, multiply:

- Hourly wages by the number of hours the family expects to work annually;

- Average weekly amounts by the number of weeks the family expects to work;
- Other periodic amounts (monthly, bi-weekly, etc.) by the number of periods the family expects to work.

SDHDA recommends using the greater of the year-to-date income calculation and hourly calculation if both are provided for HTC purposes.

If an applicant is currently unemployed with no verifiable income from any source and claiming zero income, he/she must complete a Certification of Zero Income form.

If periodic payments are received from annuities, insurance policies, retirement funds, pensions, disability or death benefits and other similar types of periodic receipts, they should be counted as income. If benefits are received through periodic payments, do not count remaining amounts as an asset.

### *Specific Criteria for Verifying Income and Assets*

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Potential tenants should be advised during the application process the units are rent-restricted. Before a household takes occupancy, all documentation must be received and the Tenant Income Certification must be complete, including date and signature.

Owners and managers should use current circumstances to project income, unless verification forms or other verifiable documentation indicate that an imminent change will occur.

EIV (Earned Income Verification) cannot be used to verify income for Section 42.

Please see HUD 4350.3, Chapter 5 for specific information on verifying income and assets. Following are areas SDHDA has had specific and recurring questions.

#### **Educational Scholarships and Grants**

The treatment of educational scholarships or grants is dependent on whether the student is receiving Section 8 assistance.

##### Not Receiving Section 8 Assistance

- All forms of student financial assistance, no matter how it is used, are excluded from annual income. Financial assistance includes grants, scholarships, educational entitlements, work study programs, and financial aid packages. It does not matter whether the assistance is paid to the student or directly to the educational institution. The financial assistance that comes from the parent to the child is excluded from annual income.

##### Receiving Section 8 Assistance

All financial assistance received from the following sources in excess of tuition is included in income.

- All financial assistance received from the Higher Education Act Assistance under the Higher Education Act of 1965 including Pell Grants, Federal Supplemental Opportunity Grants, Academic Achievement Incentive Scholarships State assistance Partnership Program, the Robert G. Byrd Honors Scholarship Program and the Federal Work Study program.
- Private sources (nongovernmental) of assistance, including assistance provided by a parent, guardian or other family member, whether residing within the family in the Section 8 assisted unit or not, or from other persons not residing in the unit.
- Institutions of higher education, when the specific institution and scholarship amount are referenced.

Financial assistance received from one of the sources above, in excess of tuition, is not included in income if either of the two following exceptions is applicable:

- The student is over the age of 23 with dependent children, or
- The student is living with his/her parents who are applying for or receiving Section 8 assistance.

Financial assistance does not include loan proceeds.

### **Alimony or Child Support**

Alimony or child support that is court-ordered or supported by a written agreement should be included in income unless the recipient certifies the funds were not received and reasonable efforts have been made to collect the amount due, including filing with the courts or agencies responsible for enforcing payments.

Documentation would include a verification form completed by the Department of Social Services or the person paying the support. A separation or settlement agreement or copy of a divorce decree stating the amount and type of support and payment schedule.

If the documentation listed above is not available, a signed sworn self-certification by a tenant is sufficient documentation under Treas. Reg. 1.42-5(b)(1)(vii) to show that a tenant is not receiving child support payments. In addition, to stating a tenant is not receiving any child support payments, an annual signed, sworn self-certification should indicate whether the tenant will be seeking or expects to receive child support payments within the next 12 months. If a tenant possesses a child support agreement, but is not presently receiving any child support payments, the tenant should include an explanation of this and all supporting documentation; i.e., a divorce decree or court documents. Also, the self-certification should indicate that the tenant will notify the owner of any changes in the status of child support. Documentation of the collection efforts may be requested.

### **Recurring Gifts**

This may include rent, utility and other payments made on behalf of the household and other cash contributions provided on a regular basis. Documentation would include a document showing the purpose, dates and value of the contribution or gift.

Groceries provided to the household and/or payments made directly to the child care provider by a person not living in the unit are excluded from annual income.

### **Income from a Business**

The net income from the operation of a business, profession, or sole proprietorship business is included in income. Net income is gross income less business expenses, interest on loans, and depreciation computed on a straight-line basis. Salaries paid to the applicant or other household members from the business must also be identified and included in income. In addition, cash and assets withdrawn by family members must be included in income except when the withdrawal is a reimbursement of cash or assets invested in the business.

Business expenses do not include principal payments on loans, interest on loans for business expansion or capital improvements, or other expenses for business expansion or outlays for capital improvements.

If the net income from a business is negative, it must be counted as zero income. A negative amount cannot be used to offset other family income.

Appropriate documentation could include the following:

- Copy of individual federal income tax return (1040) including any:
  - Schedule C (Small Business)
  - Schedule E (Rental Property Income)
  - Schedule F (Farm Income)
- Copy of Corporate or Partnership Tax return (if applicable)
- Copy of the profit and loss statement from financial statements
- Applicant's notarized statement or affidavit as to net income from the business during the previous year.

### **Social Security**

At move-in, the award or benefit statement must be within 120 days prior to the effective date of the Tenant Income Certification. Annual award letters are acceptable for any recertification and for any property that has completed the compliance period.

## **Unemployment Applicants**

If the household is unemployed and intends to live off of income from assets only, a Certification of Zero Income must be completed. If there are two adult members and one is not working, the non-working household member must complete a Certification of Zero Income. The asset income must be verified as described below.

Unemployment Compensation can be verified through the Unemployment Compensation office. The amount must be annualized unless there is clear documentation showing a beginning and end date.

## **Assets**

Assets, other than necessary personal items, are considered along with verified income in determining the eligibility of a household. There is no limit on the amount of assets a household may hold and a household is not required to convert an asset to cash. Assets include bank accounts; saving accounts; trusts; certificates of deposit; money market; stocks and bonds; the surrender value of life insurance policies and cash kept in safety deposit boxes or at home. Assets held in foreign countries are considered assets. Assets over \$5,000 must be third-party verified.

Assets do not include necessary personal items such as clothes, furniture, cars, wedding rings, or vehicles. Assets used in business are not assets included in the computation of the tenant's income. If an asset is held in the tenant's name but the income generated by the asset accrues to someone who is not a member of the household and the other person is responsible for income taxes on the accrued income, then the asset is not included in the tenant's income.

In computing assets, owners must use the cash value of the asset. Cash value is the market value of the asset less reasonable costs that were or would be incurred in selling or converting the asset to cash. SDHDA considers 10% as a reasonable basis for the costs of conversion.

After calculating the total value of assets, if the asset value is \$5,000 or less, add the actual amount of asset income to the other verified household income. When assets exceed \$5,000, add the greater of the actual asset income, or the imputed income using the passbook interest rate (currently set at 0.06%) to the total verified household income. The household's combined total income cannot exceed the applicable low income limits at move-in.

If the value of the assets does not exceed \$5,000, the "Under \$5,000 Asset Verification" form maybe used. This form is only applicable to the HTC program. If you have a mixture of other types of funding in the development, such as HOME, Section 8 or RD, you may NOT use this form.

Equity in rental property or other capital investments include the current market value less any unpaid balance on any loans secured by the property, and reasonable costs that would be incurred in selling the asset, penalties, broker fees, etc;

Example – An applicant owns a home with a market value of \$30,000 and a loan against the home of \$18,000. The cash value of the asset would be shown as \$9,000 (\$30,000 less 10% less \$18,000).

**Checking and Savings Accounts** – Checking accounts utilize a six month average balance. Savings accounts utilize the current balance.

**Debit Card** is considered an asset and verified like a savings account. Savings accounts use the current balance.

**Stocks/bonds** - Interest or dividends are counted as income, even if the earnings are reinvested. The value of stocks and other assets vary from one day to another. Use the quarterly statement or quotes from the broker to determine value.

**Retirement and pension funds** – If employed, only include amounts that can be withdrawn without retiring or terminating. Count the whole amount less any penalties. After retirement, the amount received as a lump sum is considered an asset. Any retirement benefits received as periodic payments are included in annual income.

**IRA, 401(k) or Keogh Accounts** - If the holder has access or periodic payments are being made this is counted as income. If the holder has access to the funds and there are no periodic payments, count as an asset.

**Annuities** – If a member of the household is receiving annuity payments and is not able to withdraw the balance as a lump sum of cash, the payments are treated as income. If the balance of the annuity can be withdrawn, the annuity is treated as an asset.

**Insurance Policies** Cash value of life insurance policies available to the individual before death are considered an asset (e.g., the surrender value of a whole life policy or a universal life policy). Term life insurance has no cash value prior to death.

**Lump sum receipts or one-time receipts** these include inheritances, capital gains, one-time lottery winnings, victim's restitution, settlements on insurance and other claims are counted as assets (including health and accident insurance, worker's compensation, and personal or property losses), and any other amount that are not intended as periodic payments;

**Personal property held as an investment** includes gems, jewelry, coin collections, or antique cars held as an investment are counted as an asset. An applicant's wedding ring and other personal jewelry are not counted as an asset;

**Assets disposed of within two years before effective date of certification/recertification** - If the cash value of the disposed assets exceeds the actual amount the family received by more than \$1,000, include the whole difference between the cash value and the amounts received. Do not include if the differences is less than \$1,000.

*Example:* A couple gave \$2,000 to each of their three grandchildren and deeded a home to their son. The home had a cash value of \$40,000 and the son paid his parents \$12,000

for the home. \$34,000 (\$40,000 less \$12,000 plus \$2,000 x 3) is counted as an asset until such time as the household can certify on a Tenant Income Certification form that they did not dispose of any assets during the two years preceding the certification date. (The \$12,000 paid by the son may also be counted as an asset, depending on what was done with the payment).

Do not count assets disposed of for less than fair market value as a result of a foreclosure, bankruptcy, or a divorce or separation agreement.

### **Asset Ownership Guidelines**

If assets are owned by more than one person, prorate the assets according to their percentage of ownership. If no percentage is specified, prorate the assets evenly among all owners.

## ***Acquisition and/or Rehab of Existing Buildings***

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Income Qualifying Households before the beginning of the 10-year credit period:

Under Rev. Proc. 2003-82, a unit occupied before the beginning of the credit period will be considered a low income unit at the beginning of the credit period, even if the household's income exceeds the income limit at the beginning of the first year of the credit period, if two conditions related to the income qualifications are met, and the unit must be rent restricted.

1. For households occupying a unit at the time of acquisition by the owner, the initial Tenant Income Certification is completed within 120 days after the date of acquisition using the income limits in effect on the day of acquisition. The effective date of the Tenant Income Certification is the date of acquisition since there is no move-in date.
2. In the event that the household occupies a unit at the time of acquisition, but the Tenant Income Certification is completed more than 120 after the date of acquisition, the household is treated as a new move-in. Owners use the income limits in effect at the time of the Tenant Income Certification and the effective date is the date the last adult household member of the household signed the certification (this is an exception to the general rule for the effective dates because there is no move-in date).
3. When the household moves into a unit after the building is acquired but before the beginning of the first year of the compliance period, the Tenant Income Certification is completed using the income limits in effect at the time of the certification and the effective date is the date the household moves into the unit.

For purposes of Rev. Proc. 2003-82, the income of the individuals occupying a unit before the beginning of the first credit year are first tested for purposes of the Next Available Unit Rule under IRC 42(g)(2)(D)(ii) and Treas. Reg. 1.42-15 at the beginning of the first year of the building's credit period.

1. The test must be completed within 120 days before the beginning of the first year of the credit period.

2. The “test” consists of confirming with the household that sources and amounts of anticipated income included on the Tenant Income Certification are still current. If additional sources or amounts of income are identified, the Tenant Income Certification will be updated based on the household’s documentation. It is not necessary to complete the third-party verifications.
3. If the household is over-income based on current income limits, the Next Available Unit Rule is applied.

If the effective date of the initial Tenant Income Certifications is 120 days or less before the required “test,” it is not necessary to “test” for purposes of the Next Available Unit Rule because the time period for completing the initial Tenant Income Certification and the time period for completing the “test” is the same. The annual Tenant Income Certification will be completed each year on the anniversary of the original Tenant Income Certification’s effective date.

*Example 1:* The Effective Date of Initial Tenant Income Certifications is 120 Days or Less Before the Test Date.

An owner purchased an existing building on September 1, 2014, and anticipated beginning the credit period on January 1, 2015. Household A occupied a unit at the time of the purchase and was determined to be income qualified on September 22, 2014. Because the household was determined to be income-qualified within 120 days of January 1, 2015, it is not necessary to “test” for the purposes of the next available unit rule.

If the effective date of the original Tenant Income Certifications is more than 120 days before the required “test,” the household’s income must be tested within 120 days before the beginning of the first year of the credit period.

*Example 2:* The Effective Date of Original Tenant Income Certification is More than 120 Days Before the Beginning of the First Year of the Credit Period.

An owner purchased an existing building on March 1, 2014, and anticipated beginning the credit period on January 1, 2015. Household A, an income qualified household, moved into the rent-restricted unit on April 1, 2014. Because the household was determined to be income-qualified more than 120 days before the beginning of the credit period on January 1, 2015, the household’s income must be tested no earlier than 120 days before January 1, 2015, to determine whether the Next Applicable Unit Rule should be applied.

Beginning with allocations of credit after 1989, owners of HTC buildings are required to enter into extended agreements with the state agency allocating the credit. Owners make a long-term commitment to maintain the buildings as low income housing for at least 30 years beginning with the first day of the 15-year compliance period. The owner must maintain the specified number of low income units (Applicable Fraction) based on the income limit elected under IRS 42(g)(1).

Households determined to be income-qualified for purposes of the IRC 42 credit during the 15-year compliance period are concurrently income-qualified households for purposes of the extended use agreement. As a result, any household is determined to be income qualified at the time of move-in for purposes of the extended use agreement is a qualified low income household for any subsequent allocation of IRC 42 credit.

Example 1: Owner Receives Additional Credit for Rehabilitation

An owner received IRC 42 credits to construct new low income housing. The owner placed the buildings in service in 1996 and started claiming credits the same year. The 15-year compliance period ended December 31, 2010. In 2012, the owner applied for and received an allocation of credit to rehabilitate the existing low income buildings. The rehabilitation is completed and the owner starts claiming the credit in 2014.

On February 1, 2009, John and Mary are determined to be income-qualified and move into a low income property. John and Mary timely complete their income certification for each year 2010 through 2013. The unit has always qualified as a low income unit, except when the unit was not suitable for occupancy during the rehabilitation period.

The unit is a low income unit on January 1, 2014, when the owner (a calendar year taxpayer) begins claiming the credit. If the unit was determined to be an over-income unit under IRC 42(g)(2)(D) at the time of the household's last income recertification in January of 2008, the owner is subject to the Available Unit Rule.

Example 2: New Owner Receives Credit for Acquisition and Rehabilitation

Owner ABC received IRC 42 credits to construct new low income housing. ABC placed the buildings in service in 1996 and started claiming credits the same year. The 15-year compliance period ended December 31, 2010. In 2011, ABC sold the development to XYZ, who simultaneously received an allocation of acquisition and rehabilitation credit. The rehabilitation was completed and XYZ started claiming the credit in 2013. From the time of acquisition until a new extended use agreement is recorded, XYZ is subject to the extended use agreement between ABC and the state agency.

On February 1, 2009, John and Mary are determined to be income-qualified and move into a low income unit. John and Mary timely complete their income re-certifications each year 2010 through 2012. The unit has always qualified as a low income unit, except when the unit was not suitable for occupancy during the rehabilitation period.

Based on the 2012 annual income recertification, the unit is a low income unit at the beginning of XYZ's credit period on January 1, 2013, when XYZ (a calendar year taxpayer) begins claiming the credit. XYZ should follow the procedures under Rev. Proc. 2003-82 to test income at the beginning of the credit period.

*Compliance Monitoring Fee*

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SDHDA will charge an annual fee of \$50.00 per development plus \$30.00 per low income unit all developments during the compliance period and extended use period. This fee will be reviewed on an annual basis to reassess its reasonableness and will continue in effect until further notice. Fees are billed one (1) year in arrears.

Annual fees will be imposed after the first full year in service which is measured from the month the last building in the project is placed in service.

SDHDA will directly invoice each development and all fees are to be paid directly to SDHDA.

*Available to the General Public*

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HTC properties are subject to the Fair Housing Act (Title VII of the Civil Rights Act of 1968) which makes it unlawful to discriminate in any aspect relating to rental of dwellings, in the availability of transactions related to residential real estate, or in the provision of services and facilities in connection therewith because of race, color, religion, sex, disability, familial status or national origin.

Treasury, HUD and Department of Justice (DOJ) entered into a Memorandum of Understanding (MOU) in a cooperative effort to promote enhanced compliance with the Fair Housing Act for the benefit of the residents of HTC properties and the general public. The MOU includes coordinated procedures for notifying the state agencies and IRS of charges, lawsuits, or other actions under the Fair Housing Act involved in the HTC properties.

HUD or DOJ will notify a state agency of:

- A charge by the Secretary of HUD for a Violation of the Fair Housing Act,
- A probable cause finding under a substantially equivalent fair housing state law or local ordinance by a substantially equivalent state or local agency,
- A lawsuit under the Fair Housing Act filed by the DOJ, or
- A settlement agreement or consent decree entered into between HUD or DOJ and the owner of a Tax Credit property.
- A form 8823 will be filed with the IRS for a notification as reference above received from HUD or DOJ.

Other non-FHA civil rights actions and lawsuits, such as section 504 Rehabilitation Act lawsuits or administrative actions, are not covered under the terms of the MOU and will not be reported to the IRS.

A General Public Use Rule was clarified on July 30, 2008, to allow occupancy restrictions or preferences that favor tenant with special needs, involved in artistic or literary activities and who are members of a specified group under a federal or state program or policy that supports housing for such specified group.

**Violence Against Women Act - (VAWA)**

While not a compliance requirement of section 42, the Violence Against Women Reauthorization Act of 2013 (VAWA 2013) was extended to include the Low Income Housing Tax Credit program in 2013. Owner must comply with the lease requirements found in Section 601 of VAWA 2013.

Lack of compliance with VAWA does not cause the loss of Tax Credits. Therefore, SDHDA does not monitor for VAWA compliance. However, educating staff on VAWA requirements is recommended. Violations of victims' rights can lead to discrimination under the Fair Housing Act.

## *Compliance Reviews*

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### **Tenant File Review**

Properties within the compliance period will be reviewed based on the chart located on page 5 as of February 26, 2019. Properties past the compliance period in the extended use period will be reviewed based on 20% of the multi-family units. If there are serious non-compliance issues the sample size will may increase. One hundred percent of all single family homes will be reviewed.

The following items will be reviewed during the on-site review:

- Application
- Tenant Questionnaire
- Lease
- Consent and Release forms
- Credit Report (if in the file)
- Criminal Background Check (if in the file)
- Tenant Income Certification and supporting documentation
- Affirmative Fair Housing
  - Advertising
  - Equal Opportunity Posters
- Current Rent Roll
- Copy of Replacement Reserve Account Balance
- Copy of the last HTC Training Certificate
- Waiting List of prospective tenants
- Lead Based Paint Disclosure (if applicable)
- Completed and signed copy of the 8609
- Utility Allowances and supporting documentation

Corrections should be made to documents with a line drawn through the incorrect item, write in the correct item and have both parties initial and date the change. White out is not acceptable.

The selection of the files and units will be a random sample that is not available prior to the review. Approximately 15 days prior to the inspection the owner will be contacted and an agreeable time will be set up and a confirmation letter will be sent to the owner/agent of the property. Any violations corrected prior to the date of the confirmation letter will not be reported to the IRS in the form of an 8823.

### **Physical Review of Units**

The first physical review of the property will be no later than the end of the second year after the last building is placed in service. The review of the tenant files and physical review of the units will be conducted in the year required.

SDHDA utilizes the Uniform Physical Conditions Standards (UPCS) as the physical inspection criteria for HTC developments. All units must be safe, decent and sanitary.

The manager is required to notify all households at least 24 hours in advance of the physical inspection. The selection of the units is random and at the discretion of the inspector.

UPCS have five areas to be inspected:

- Site
- Building Exterior
- Building Systems
- Dwelling Units
- Common Areas

Site – This includes fencing and gates, grounds, walkways and steps, storm drainage, retaining walls, signs and refuse disposal.

Building Exterior – This includes doors, main entrance, accessibility to main entrance, fire escapes, foundations, lighting, roofs, walls and windows.

Building Systems – This includes domestic water, electrical system, elevators, emergency power, exhaust system, fire protection, HVAC and sanitary system.

Common Areas – This includes, but is not limited to basement/garage/carport, closet/utility/mechanical, community room, daycare, interior hallways, kitchen, laundry room, lobby, office, patio/porch/balcony, pools, restrooms, storage, trash collection areas, call for aid, ceiling, doors, electrical system, interior hallways and outside areas, floors, HVAC system, stairs, walls, windows, lighting and graffiti.

Dwelling Units – This includes, but is not limited to bathrooms, call-for-aid, ceiling, doors, electrical system, floors, hot water heater, HVAC system, kitchen, laundry area, lighting, outlets/switches, patio/porch/balcony, smoke detector, stairs, walls and windows.

If any Health and Safety issues were found during the physical review, a formal Life/Safety Citation will be issued at the end of the review. There is a 72 hour correction period for any Life/Safety issues.

Some of the most common Life/Safety findings include: tripping hazards, inoperable emergency lights, inoperable smoke detectors, GFI's that do not trip, no access to the breaker box, missing spacers from the breaker box, housekeeping negligence to the degree it poses a health/safety issue, egress windows are blocked, combustible items stored near the furnace or water heater, water heater pressure relief valve pipe missing, inoperable exterior locks and expired fire extinguishers tags.

SDHDA recommends using preventative maintenance and maintaining a maintenance schedule at all developments.

### **Noncompliance**

If SDHDA does not receive the required certifications by the due date or if SDHDA discovers on audit, inspection, or review, or in some other manner that the development is not in compliance with the Code, SDHDA will notify the owner within 30 days.

The owner will have an opportunity to supply missing certifications or to correct noncompliance within a specified correction period, not to exceed 90 days from the date of the notice to the owner. At the sole discretion of SDHDA, the correction period may be extended for a period of up to six (6) months if there is good cause for granting an extension.

SDHDA is required to notify the IRS of an owner's failure to file the Annual Owner Certification on a timely basis, or any other noncompliance issues no later than 45 days after the end of the allowed time for correction, whether or not the noncompliance or failure to certify has been corrected.

The IRS published a "Guide for Completing Form 8823". Commonly called the 8823 Guide, it provides instructions for monitoring agencies to determine noncompliance, what constitutes correction, and how and when noncompliance and property dispositions are reported. Owners and managers are encouraged to use the Guide as a reference tool.

If uncorrected noncompliance is reported to the IRS, a corrective 8823 cannot be filed until all instances of noncompliance are corrected for that building.

### **Casualty Loss**

SDHDA must be notified within 10 days of a casualty loss and the owner will then have 30 days to submit a plan. An 8823 will be filed with the IRS noting the building is out of compliance within 90 days. After the casualty loss has been remedied, a corrected 8823 will be filed with the IRS.

### **Liability**

Compliance under the requirements of the Code is the responsibility of the owner of the development. SDHDA's obligation to monitor for compliance with the requirements of the Code does not make SDHDA liable for an owner's noncompliance. SDHDA will not make any representation other than to the IRS that a development is in compliance.

### **Lead Based Paint**

SDHDA uses HUD's Uniform Physical Conditions Standards (UPCS) when physically reviewing the development. Therefore, the Lead Based Paint Safe Housing Rule applies to the HTC program.

### **Sale, Transfer or Disposition of the Project after the Placed in Service Date**

When a sale or transfer occurs after the placed in service date, the owner must submit a completed Notice of Intent to Transfer Ownership or Change Owner Name or Status form.

The IRS has suggested in Regulation 1.42-5 that, if a building is sold or otherwise transferred by the owner, the new owner should obtain all information regarding the first year of the credit period.

## ***Extended Use - Year 15 and Beyond***

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### **Extended Use**

Beginning with 1990 allocations, the extended low income housing commitments, also known as restrictive covenants (Declaration of Land Use Restrictive Covenants) became a requirement of the HTC program. The restrictive covenants are recorded at the Register of Deeds in the county the development is physically located. SDHDA established a set of monitoring procedures for qualified HTC properties after year fifteen. The procedures are designed to lessen reporting burdens for owners and preserve the long-term affordability of developments.

Owners who elect to stay in the HTC program at the end of the 15 year period will follow modified monitoring criteria, which will be in effect for the extended use period. The following criteria will apply:

- An initial Tenant Income Certification including third party documentation will be completed at move-in.
- The Annual Household Update form must be completed by the tenant at annual recertification to ensure the annual reporting information is collected.
- Student status will no longer be a consideration. Full-time students may live in a HTC unit. However, if you plan to come in for a competitive HTC allocation round and a full-time student household occupies the unit, the household would not be student eligible and therefore ineligible for new credits.
- The Available Unit Rule will be revised to provide that if a household's income goes over 140% of the applicable AMI, a currently vacant unit or the next unit in the same building must be rented to a qualified household. This would be a one for one replacement.

- The building's applicable fraction will be determined by the unit fraction. The square footage of the unit will not be used to determine the lesser of fraction.

The following monitoring procedures would continue:

- Annual Owner Certificate of Continuing Program Compliance;
- Tenant data for the year, via Web Compliance Management System (WCMS);
- Authorized Representative Designation (if applicable);
- Utility allowance(s) for the reporting period submitted;
- Every three years, a file review of the tenant files will be completed. Twenty percent (20%) of the files will be examined. More files may be reviewed at the discretion of SDHDA. After completing the compliance period, reviewing the same unit and corresponding file is not a requirement.
- Physical review of the property will include a minimum of five units, all public areas and utility rooms. If SDHDA has a completed a physical review of the development under a different housing program within the last two years, that physical review may be utilized.

At the end of the extended use period, an owner is prohibited from evicting existing tenants for other than good cause, and from raising their rents beyond the HTC maximum rents, for a period of three (3) years. A letter will be sent to each tenant that currently resides in the unit informing them of this requirement. As the current HTC tenants move out of the units, the tenants that move into the units can be market rate tenants with market rate rents. At the end of each year, for the three year period, a report shall be submitted to SDHDA verifying the HTC tenants that remain in the units and the rent amounts.

After year 15 and the end of the compliance period, an IRS form 8823 will not be filed with the IRS to notify them of noncompliance. The tax benefit to the owner is exhausted and the IRS can no longer capture or disallow credits.

Compliance fees are to be paid to SDHDA through the extended use period.

Throughout the extended use period, if noncompliance occurs, SDHDA will work with the owner to bring the property back into compliance and reserves the right to sue for specific performance. If compliance is not attained, that information is shared with our Development team. If the owner comes in for a competitive allocation of Tax Credits, negative points may be awarded, which may cause the application to fail in the competitive process.

### **Qualified Contracts**

Each Declaration of Land Use Restrictive Covenant is project specific. The elections made by the owner at the time of application may allow or disallow the owner from coming

in to request a Qualified Contract. If allowed, owners who are no longer interested in owning and/or retaining the low income use restrictions on the development can pursue the Qualified Contract option. During, or any time after the 14<sup>th</sup> year of the compliance period, the owner may request that SDHDA find a buyer for the low income portion of the development. If SDHDA is unable to find a purchaser pursuant to a Qualified Contract within a one year period, the development may be converted to market-rate use. For more information, please visit the website at [www.sdhda.org](http://www.sdhda.org) and review the “Housing Tax Credit Program – Year 15 Plan and Application.” The 2002-2003 Qualified Allocation Plan offered additional competitive points for electing additional extended use years beyond 30 and the owner is prohibited from requesting a Qualified Contract.