

# 4% Low Income Housing Tax Credits: The Basics

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# Overview

- ▶ Owner of LIHTC project receives federal tax credits
- ▶ Credits received each year for 10 years after rent-up
- ▶ Project units subject to 20-50/40-60 income limits and rent-restricted
- ▶ Income limits (and use limits) apply for 15 years (and if violated tax credits subject to recapture)
- ▶ Rent charged to LIHTC tenants is to be no more than 30% of tenant's imputed income
- ▶ Unlike 9% LIHTCs, 4% LIHTCs are not included in the State's per capita allocation
- ▶ Arizona Department of Housing (ADOH) awards the 4% LIHTCs
- ▶ 4% LIHTCs must use an allocation of the State's tax-exempt Private Activity Bonds (Arizona Finance Authority)

# LIHTC Calculation Basics

- Step 1 - Only “eligible basis” of project qualifies, which is (1) cost of new construction and any rehabilitation (sticks, bricks, materials and labor) and (2) cost of acquisition of existing buildings; excluded are land, site preparation, soft costs not project related (e.g., syndication costs), reserves, marketing and management. EXAMPLE: \$5,000,000.
- Step 2 - Eligible basis may be boosted by 30% if project in (1) a HUD designated qualified census tract (QCT) or (2) a HUD designated difficult development area (DDA). EXAMPLE: \$6,500,000.
- Step 3 - Multiply eligible basis by percentage of LIHTC units in the project (other units are “market rate”); the product is called “qualified basis.” EXAMPLE:  $80\% \times \$5,000,000 = \$4,000,000$ .
- Step 4 - Multiply qualified basis by 4%; this is maximum amount of annual tax credits. EXAMPLE:  $4\% \text{ OF } \$4,000,000 = \$160,000$ .

# LIHTC Example

Example - (\$500,000 land; \$5,000,000 construction)

Eligible Basis	\$5,000,000	
Boost	none	no QCT/DDA
Applicable Fraction	80%	20% market rate
Qualified Basis	\$4,000,000	
Tax Credit %	4%	
Tax Credits (annual)	\$160,000	maximum
Tax Credits (10 years)	\$1,600,000	

# Tax Credit Pricing

- ▶ Primary LIHTC purchasers are banks (or funds with banks as investors).
- ▶ Price quoted based on percentage of all future LIHTCs (by xx cents per dollar amount of LIHTCs, such as 95 cents).
- ▶ Price based on time value of LIHTCs (that is, “yield” to investor of taxes saved) and project tax losses.
- ▶ Other pricing factors
  - ▶ Community Reinvestment Act benefits
  - ▶ alternative investment interest rates
  - ▶ corporate and personal relationships
  - ▶ size of the investment/project (bigger is better)
  - ▶ when the LIHTCs will be available
  - ▶ when purchase price of LIHTCs will be paid (usually rentup)
  - ▶ characteristics of the project/developer/investor
  - ▶ other deal terms (e.g., reserves, guarantees, etc.)
  - ▶ debt structure and subsidies
  - ▶ location, location, location

Questions?

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