CALIFORNIA TAX CREDIT ALLOCATION COMMITTEE

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DATE: June 25, 2020

TO: Low Income Housing Tax Credit Project Owners and Applicants

FROM: California Tax Credit Allocation Committee – Development Section

RE: Average Income Test Federal Election

To qualify for low income housing tax credits (LIHTCs), multifamily rental housing must have a minimum percentage of low income units, which is based on county-level area median income (AMI). In January 2018 as part of the Consolidated Appropriations Act of 2018, a change was made to the LIHTC program, increasing the maximum income and rent limits from 60% AMI to 80% AMI. As a result, the three options provided or "elected" pursuant to Internal Revenue Code (IRC) §42(g)(1) are:

- at least 20% of the units restricted to rent levels that do not exceed 50% AMI ("20/50"),
- at least 40% of the units restricted to rent levels that do not exceed 60% AMI ("40/60"), or
- at least 40% of the units restricted to rent levels that do not exceed 80% AMI, with the average of all restricted units no more than 60% AMI (the Average Income Test or "AIT"). Restrictions must be designated in 10% AMI increments (20%, 30%, 40%, 50%, 60%, 70% or 80%).

California Tax Credit Allocation Committee (TCAC) has receive guidance from the IRS regarding the Average Income Test and a project's first year of credit as follows. The effective date of the law was March 23, 2018, and thus the first tax year in which an owner could meet this election is 2018. Therefore, any project electing the AIT must have a first year credit beginning no earlier than 2018.

The IRS cited the Form 8823 Guide, which states that a building is in compliance if the elected minimum set aside requirement is met by the end of the first year of the owner's credit and compliance period (and continues to be met each year throughout the compliance period). The tax credit units must also be rent restricted.

The applicable IRC section is §42(g)(3)(A), which states as follows:

(3) Date for meeting requirements.

(A) In general.--Except as otherwise provided in this paragraph, a building shall be treated as a qualified low-income building only if the project (of which such building is a part) meets the

requirements of paragraph (1) not later than the close of the 1st year of the credit period for such building.
(B)...

In May 2018, TCAC adopted regulations that allowed projects with an existing tax credit reservation to elect the Average Income Test and make changes to the application's housing unit designations, increasing some to 80% AMI. Effectively this permitted projects under construction and some projects nearing completion at the time of the legislation enactment to increase their maximums from 60% AMI to 80% AMI. TCAC is now providing additional guidance, consistent with IRS direction, that to be considered a 100% LIHTC project (not mixed income), all buildings in these projects must have a first year credit no earlier than 2018.

As a reminder, TCAC Regulation §10325 (f)(13) and §10326(g)(9) require a project with low income units targeted at greater than 60% AMI to make the "Yes" election on line 8b of the IRS Form 8609. Given than the AIT is calculated at the project level, a project with a "No" election would have to calculate average income at the building level. A "No" election would require complicated calculations which may cause project owners errors jeopardizing tax credits for all project units, not just any over-income units. As a result, projects must select "Yes" on line 8b of the IRS Form 8609.