

Managing Compliance

Presented by
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Internal Revenue Service
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Introduction



Hello!

The word "Hello!" is rendered in a large, bold, 3D font. Each letter is filled with a different color from a rainbow spectrum: 'H' is purple, 'e' is red, 'l' is orange, 'l' is yellow, 'o' is green, and '!' is blue. The letters have a slight shadow cast to the right, giving them a three-dimensional appearance.

Objectives

- **Guide for Completing Form 8823:
Summary of Revisions**
- **Prioritize for Day-to-Day Operations**

Priority Topics

- Income Certifications (Chapter 4)
- Gross Rents (Chapter 11)
- General Public Use (Chapter 12)
- Tenant Protections (Chapter 26)
- Student Households (Chapter 17)

1: Determining Income

“Maximum benefits and annualized payments should not be used unless the source of funds is expected to continue throughout the certification period or for an indeterminable length of time.”

Page 4-8: Annualizing Payments

Example 1: Indefinite Time Period

John works as a telemarketer for \$9 an hour, 40 hours a week. He does not work overtime, has no other source of income, and is not planning to leave his job. His anticipated income is computed as:

$$\text{\$9/hr} \times 40 \text{ hrs/wk} \times 52 \text{ wks/yr} = \text{\$18,720/yr}$$

Example 2: Definite Time Period

A teacher works nine months annually and receives \$1,300 per month. During the summer recess, the teacher works for the Parks and Recreation Department for \$600 a month. The teacher's income is computed as:

$$(\$1,300 \times 9 \text{ m}) + (\$600 \times 3 \text{ m}) = \$13,500/\text{year}$$

Example 3: Anticipated Changes

At the time an unemployed plumber applies for housing in May, he is receiving unemployment benefits of \$250 per month. Beginning in October, he will be employed at \$1,000/month.

Unemployment Ins. = \$250 x 5 months

Wages = \$1,000 x 7 months

Annual Income = \$8,250/year

Why aren't unemployment benefits annualized per 4350.3 Manual?

For IRC §42, annualizing the unemployment benefits will *overstate* the actual income received. Low-income housing will not be made available to truly income-qualified households.

For Section 8, annualizing the unemployment benefits is necessary so that when dividing by 12, an accurate current monthly income is calculated and used for determining the rent subsidy. Otherwise, monthly income is *understated*.

Example 4: Sporadic Income

Justine is disabled and worked about six months last year, but now has more medical problems and doesn't know when or how much she will be able to work.

Since actual income from her sporadic employment cannot be reasonably determined, income earned during the prior year should be used, *but* only if circumstances are similar.

“Anticipated” means:

1. prior year (historical), or
2. current income (extrapolate), or
3. anticipated future earning

Method is a matter of ***judgment***
applied to the ***facts***,
to compute ***best estimate***.

To what extent should Handbook 4350.3 be relied upon?

1. Generally, HUD definitions determine whether funds are included in income based on source and characteristics, except for military housing allowances in some cases
2. Computation of annual income may differ
3. Documentation standards will differ; state agency requirements will govern



Deployment of Military Personnel to Active Duty

1. Allow guardian to move in
2. Allow tenant to care for dependents of military personnel on active duty
3. Allow lease to remain in effect

Page 4-11: Accommodations for military personnel called to active duty will be temporary or for a reasonable period: i.e.,

“for as long as needed.”

When determining income, consider:

- Whether project is mixed-use or 100% low-income housing (increasing household size or moving within project).
- Military housing allowances (includable?)
- Self-Employed Tenants (documentation)
- Office in the Home (commercial use)
- Scholarships and Grants (Section 8)
- Previously certified low-income households (extended use agreements)

#2: Rent Limits

Because HUD determines a tenant's rent on a monthly basis, state agencies must determine whether the owner is in compliance with the gross rent limits *each month of the owner's current tax year*.

Page 11-2: Determining Rent Limits on a Monthly Basis

In Compliance: the rent does not exceed the gross rent limitations on a monthly basis

Out of Compliance:

1. the rent exceeds the rent limit on a monthly basis
2. the rent exceeds the rent limit on a tax year basis
3. impermissible fees are charged

Back in Compliance:

- Once a unit is determined to be out of compliance with the rent limits, the unit ceases to be a low-income unit for the remainder of the owner's tax year
- An owner cannot avoid disallowance of the credit by rebating excess rent or fees to the affected tenants
- A unit is back in compliance on the first day of the owner's *next taxable year* if the rent charged on a monthly basis does not exceed the limit

#3: General Public Use

“Owner must make reasonable attempts to make vacant low-income units available to the public for rent. Owners should advertise the availability of vacant units using advertising methods designed to be accessible to *all* prospective tenants.”

Page 12-2: Marketing

#4: Tenant Protections

Eviction: legally dispossessing a person of land or rental property. (page 26-3)

Failure to Renew Lease: not renewing a lease or entering into a new lease allowing a tenant to continue occupying a low-income unit. (page 26-4)

Termination of Tenancy: has no legal definition and is a term of art specific to IRC §42. (Footnote #26-1)

1. Owner wishing to evict a tenant must comply with applicable state and/or local laws governing evictions
2. Owner wishing to nonrenew a lease must provide tenant with timely notice that lease will not be renewed as required under state law
3. Owner must demonstrate if challenged in state court that good cause exists to support eviction, nonrenewal of lease, or termination of tenancy (document file)

In Compliance:

1. Extended Use Agreement includes prohibitions against terminations of tenancy without good cause and increases in rent not otherwise allowable
2. Annual certification to state agency that owner is in compliance
3. No terminations of tenancy without good cause
4. No increases in rent unless permitted by IRC §42

#5: Student Households

1. “Student” during each of five months during calendar months during the calendar year
2. New exception for former “foster care” children: “former” defined by state agencies
3. Verification of student status is separate from income (re)certifications
4. “Verification” not “certification” of student status
5. Separate annual verification requirement for “continuous” compliance

Qualifying Married Student Households

Question: Is a married couple required to actually file a joint return in order to qualify for the exception under IRC §42(i)(3)(D)(ii)(II)?

No. The couple need only be *entitled* to file a joint return.

Who is *entitled* to file a joint return?

A couple is considered married for the whole taxable year if, on the last day of the tax year, the couple meets any one of the following tests:

1. Married and living together as husband and wife,
2. Living together in a common law marriage that is recognized in the state where they now live or in the state where the common law marriage began,
3. The couple is married and living apart, but not legally separated or divorced, or
4. The couple is separated under an inter-locutory (not final) decree of divorce.

For more information, refer to IRS Publication 501.

“Other” Really Important Priorities

Chapter 1: Authority of Guide

- Guide is not a legal authority
- Reference of current legal authorities
- Cannot be cited
- Scope is limited
- Guide is obsoleted as of the effective date of revised legal authority

Chapter 5: Income Recerts

- Exception for housing financed by the Rural Housing Service under Section 515 and buildings financed with tax-exempt bonds
- Annual income recertifications not required for tax years ending after July 30, 2008, if all low-income buildings in the project are 100% low-income buildings
- State housing agencies may impose recert requirement

Chapter 6: Physical Suitability

- Vacant low-income units must be suitable for occupancy

Chapter 8:

Eligible Basis and Grants

- If building was *placed in service* on or before July 30, 2008, then federally-funded grants made with respect to the building *or its operation* reduces the eligible basis
- If building was *placed in service* after July 30, 2008, the federally-sourced grants used for the operation of the building do not require a reduction of eligible basis
- Rental assistance from specific sources not considered federal grants

Chapter 8: 40/50 Rule

- For buildings *placed in service* before July 31, 2009, assistance provided under HOME or NAHASDA is not treated as a below market Federal loan if 40% or more of the units in the building are occupied by individuals whose income is 50% or less than the AMGI

- For buildings *placed in service* after July 30, 2008, below market loans under HOME or NAHASDA are not considered federal subsidies, and are not subject to the 40/50 rule

Chapter 14: NAUR

- Application to 100% low-income buildings where annual income certifications are not required
- See Newsletter #32
- Comparable units have the same number of bedrooms and comparable amenities
- Noncompliance trigger by renting to nonqualified household or renting units at market rates

Chapter 15: Vacant Unit Rule

- Project-based rule
- Violated when market rate units are rented before making reasonable attempts to rent vacant low-income units
- Failure to market vacant low-income units is a violation of the general public use rule

Chapter 16: Extended Use

- Guidelines for documenting the beginning of the 1-year correction period

Chapter 23:

Other Noncompliance Issues

- Nonperformance of Extended Use Agreements
- Owner of 100% LIHC project fails to complete annual income recerts

Chapter 24: Exhibit 1

- No longer required to place surety bond upon disposition of a LIHC building (or interest there) to avoid credit recapture if a building was reasonably expected to continue to be operated as low-income housing
- Elections to no longer maintain bonds or Treasury Direct Accounts in place on July 30, 2008. (Rev. Proc. 2008-60)

Chapter 25: Tenant Fraud

- Updated procedures for reporting to the Whistleblower's Office
- Same Form 211, same information
- Different office

Contact Information

- Telephone: 202-283-2516
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- E-Mail: Grace.F.Robertson@irs.gov
(E-Mail preferred)

Thanks

Thanks

Thanks

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Thanks Thanks

Thanks Thanks

Top 10 Most Challenging Compliance Issues

Referencing the “Guide for Completing Form 8823
Low-Income Housing Credit Agencies Report on
Noncompliance or Building Disposition
(Revised October 2009)



#1 – Utility Allowances

- For RHS assisted buildings or RHS Resident assistance units:
 - Use RHS Utility Allowance for all rent restricted units in a building.
- If no RHS but building is HUD regulated:
 - Use HUD Utility Allowance for all rent restricted unit in a building.
- If neither of the above:
 - Use PHA Utility Allowance or an estimate.

#1 – Utility Allowances

- Pre (07-28-08) Local Utility Allowance Election is permanent with one exception:
 - The State Agency approves a switch back to the PHA Utility Allowance.
- Post 07-28-09 – May now use:
 - State Agency or private contractor
 - HUD Utility Schedule Model
 - PHA or Utility Company estimate.
- Sub-metering is OK.

#2 – Transfers

- When a Resident, whose income is less than 140% of the income limit, transfers to a new unit in the project, the units switch status.
- The vacated unit assumes the status the newly occupied unit had immediately before it was occupied by the current resident and the newly occupied unit adopts the status of the vacated unit.

#2 – Transfers

- Transfers between Buildings:
 - Residents can transfer between buildings within the project (as defined by owner's election on Form 8609).
 - Residents with income exceeding 140% of the income limit cannot transfer between buildings because the Next Available Unit Rule is a building-based rule.

#2 – Transfers

- Transfers in the same Building:
 - Does not matter whether the household has income exceeding 140% of the income limit.

#3 – Resident Manager Units

- The 8823 Audit Guide indicates that charging rent for a Manager's Unit may take away the exempt status of the unit.

#3 – Resident Manager Units

- If an Owner is charging rent for the Manager Unit, the IRS may determine that the unit is not reasonably required by the project. Such a determination would be made based on the Owner not requiring the Manager to occupy the units as a condition of employment.

#4 – Gross Rent Exceeds Tax Credit Limits

- Overcharging Residents for rent in the first year of the Compliance Period can disqualify the Owner from claiming any credits.
- The 8823 Audit Guide indicates that an Owner cannot avoid the disallowance of the Low Income Housing Credit by rebating excess rent to the affected Residents in any year of the Compliance Period.

#4 – Gross Rent Exceeds Tax Credit Limits

- Rent Computation:
 - Units may be residential rental property notwithstanding the fact that services *other than housing* are provided.
 - However, any charges to low-income residents for services that are not optional generally must be included in Gross Rent.

#4 – Gross Rent Exceeds Tax Credit Limits

- Examples of non-optional fees, included in Gross Rent:
 - Renter's Insurance
 - Built in storage shed
 - Washer / Dryer hook ups
- Optional fees, not included in Gross Rent:
 - Laundry room equipment fees
 - Pet fees

#5 – Verifying Income / Assets

- Acceptable methods of verifying information include Third Party Verifications, Review of Documents submitted by the resident (i.e. check stubs), and the Resident Certifications made under penalties of perjury.
- Third Party Verifications are the most preferred form of documentation.

#5 – Verifying Income / Assets

- Footnote 16:
 - Third party contacts are considered impossible if an employer does not respond, third party charges a fee, or no third party is available. Generally a third party contract is considered delayed if a response will not be received within two weeks, but can be less if it is determined that the third party will not respond.

#5 – Verifying Income / Assets

- Child Support:
 - When no documentation is available, the Owner may require the family to sign a certification stating the amount received. The certification must be notarized.
 - A signed, sworn self-certification by a resident is sufficient documentation to show that a resident is not receiving Child Support.
 - A State Agency may require that an Owner obtain documentation, other than the statement described above, to support a resident's Annual Certification.

#6 – Full Time Students

- IRC151(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 at an educational organization, or is pursuing a full-time course of institutional on-farm training under the supervision of an accredited agent of an educational organization or of a State or political subdivision of a state. Treas. Reg. further provides that the five calendar months need not be consecutive.

#6 – Full Time Students

- The term “educational organization” includes:
 - Elementary schools;
 - Junior / Middle schools;
 - Senior High schools;
 - Colleges and Universities;
 - Technical, Trade & Mechanical schools.

#6 – Full Time Students

- Revisions to the qualified exceptions:
 - Single parents with children all of who are students and such parents and children are not dependents of another individual (none of the household members are dependents of a third party).
 - The children can be dependents of a parent outside of the household.
 - A married couple that is entitled to file a joint tax return, but has not filed one, still satisfies the exception under IRC 42(i)(3)(D)(ii)(II).

#7 – Recertifications

- Changes in Family Size:
 - The addition of new member(s) to an existing low-income household requires the income certification for the new member(s), including third party verification. Treatment will depend on if the property is mixed use or 100% Tax Credit.
 - Mixed property – the new member’s income is added to the income of the existing household’s “most recent” Tenant Income Certification.
 - For a mixed property, the income of the new member is taken into consideration with the income of the existing household for purpose of the Available Unit Rule.
 - 100% Tax Credit property – the income is added to the Original Certification.

#7 – Recertifications

- Non-compliance with Annual Income Recertification requirements that are identified and corrected by the Owner prior to notification of a compliance review by the State Agency need not be reported to the IRS.

#7 – Recertifications

- A retroactive certification can be performed which completely and clearly documents the sources of Income and Assets that were in place at the time the certification should have been effective, and applies income limits that were in effect on that date.
- The Resident should date the document with the current date of signature with a statement that says the information is true and correct as of the effective date of the certification.
- Assuming the Owner can document that the household was income eligible at the time of move-in, the unit should not be considered out of compliance.

#8 – Non-performance of the Extended Use Agreement (EUA)

- Under IRC 42(h)(6), taxpayers receiving credits must execute an Extended Use Agreement, which is recorded as a restrictive covenant against the property, as provided by state law.
- The Extended Use Period end on the later of the date specified in the agreement or 15 years after the close of the Compliance Period. At a minimum, the property must be maintained as low income housing for 30 years beginning with the first day of the Compliance Period.

#8 – Non-performance of the Extended Use Agreement (EUA)

- The 8823 Guide states that violations of the Extended Use Agreement (EUA) are *not* to be reported to the IRS.
- However, violations of the EUA will be tracked by the State, and Owners will be notified of errors.

#9 – Physical Inspection Standards

- Violations of the Uniform Physical Conditions Standards (UPCS) or Local Inspection Standards.

#9 – Physical Inspection Standards

- State Agencies must inspect Low-Income Housing Credit properties to ensure that the building and units are suitable of occupancy.
- Inspections by the State Agency must be made at least once every three years.

#9 – Physical Inspection Standards

- A building is in compliance if it meets the requirements of either HUD's Uniform Physical Condition Standards (UPCS) or local standards.
- The UPCS does not supersede or preempt local health, safety and/or building codes.
 - When conflicts are presented, the local code will be evaluated by the State Agency in determining whether the project or unit is in compliance.

#9 – Physical Inspection Standards

- Exhibit 6-1 (pages 6-9 and 6-10) – Checklist for the Physical Inspection of Low Income Housing Credit Properties and Summary of Findings.
 - New forms being used by many State Agencies during the property inspections.

#9 – Physical Inspection Standards

- Exhibit 6-4 (page 6-13) – Notification Letter – Critical Violations.
 - Violations involving life threatening problems requiring correction within 72 hours of notification.

#10 – Guidelines for Determining Noncompliance

- The State Agency is responsible for determining whether Owner are compliant with IRC 42 and its regulations.
- At least once every three years, a minimum of 20% of all Low Income Housing Credit Resident files and units must be reviewed by the State Agency.
- In the event that extensive noncompliance is identified, State Agencies should consider expanding the number of units inspected & files reviewed beyond the 20%.

#10 – Guidelines for Determining Noncompliance

- In many instances, the Form 8823 Guide states that if noncompliance is discovered and corrections are made prior to notification of the State Agency's audit, it will not be considered noncompliance.
- Audits should be done periodically to discover and correct noncompliance items.

Question and
Answer
Session with
the Experts!