


Section 42 Non- Compliance: How it Happens and How to Repair


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Form 8823: Low Income Housing Credit Agencies Report of Noncompliance or Building Disposition



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Following the Compliance Review


State sends summary of findings to Owner.
Section 42 says the Owner has 90 days to respond & prove:

- They were always in compliance; **or**
- The noncompliance has been corrected; **or**
- Ask for an extension (up to 6 months)

Caution:
The state may set a shorter time frame.

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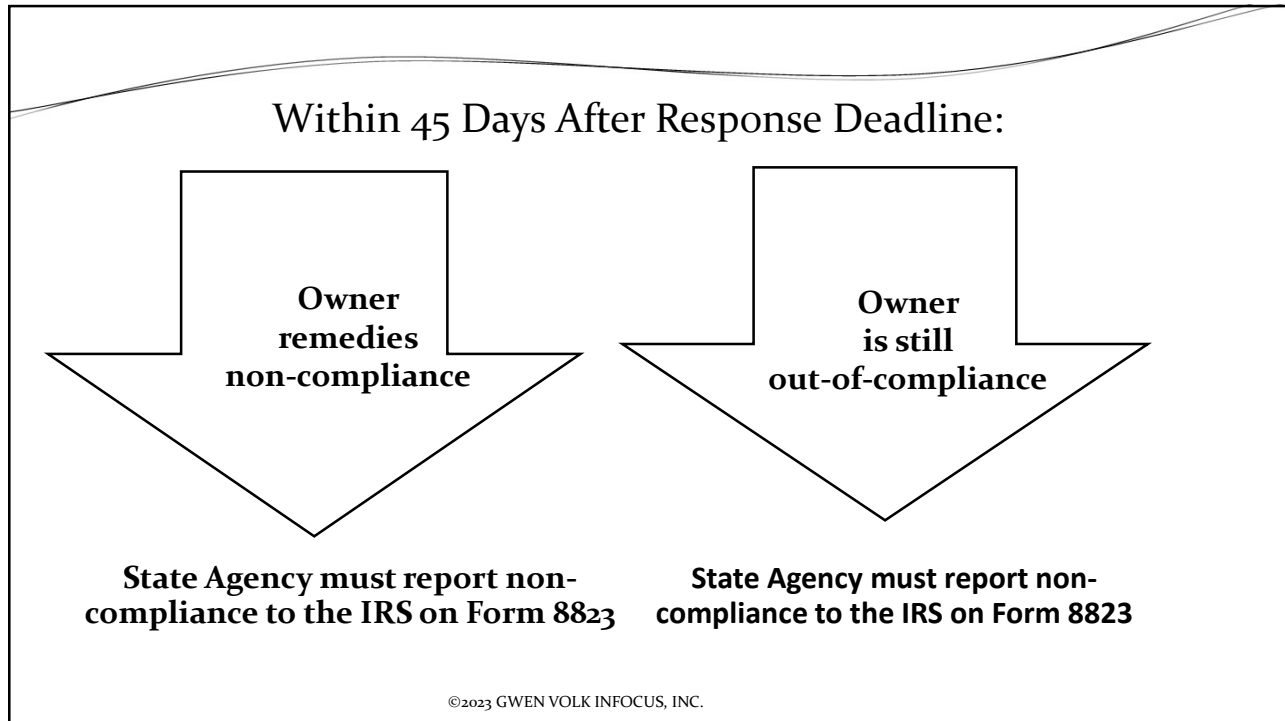


“The Commission will generally provide up to 30 days to correct documentation or reporting errors. However, the correction period is not to exceed 90 days from the date of the notice to the Owner. Any additional correction time granted by the Commission is granted solely at the Commission's discretion.”

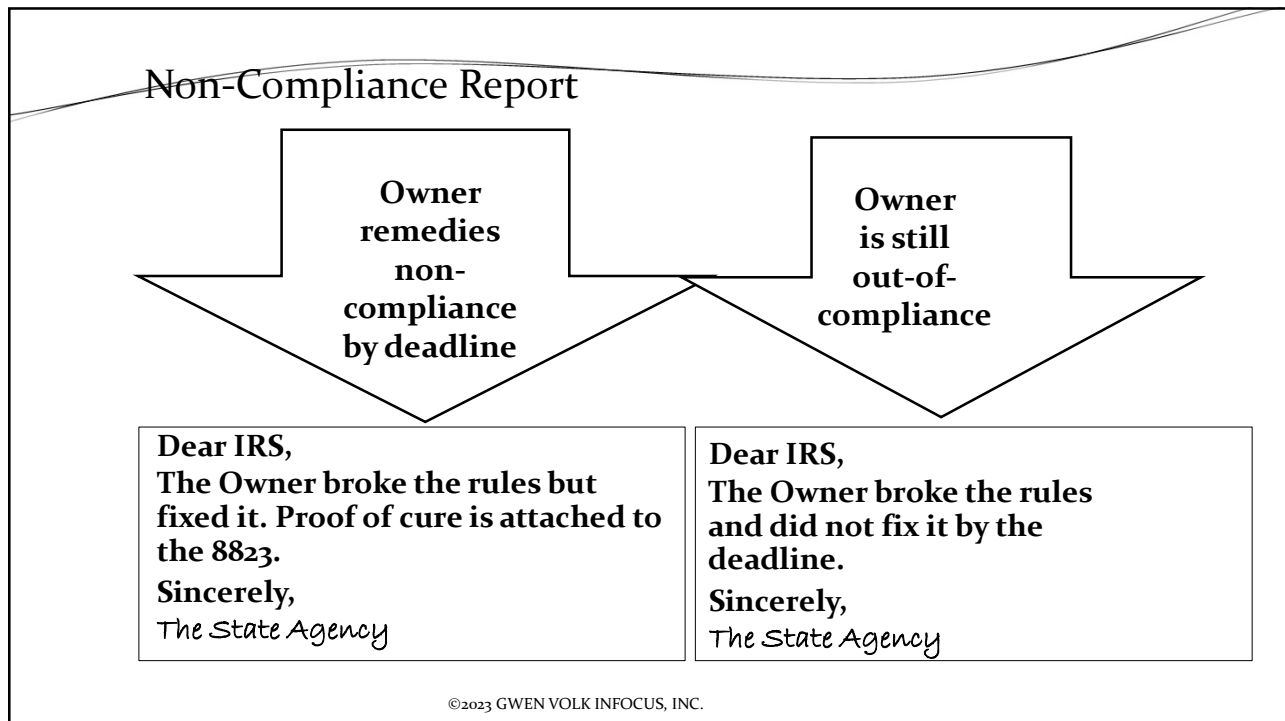
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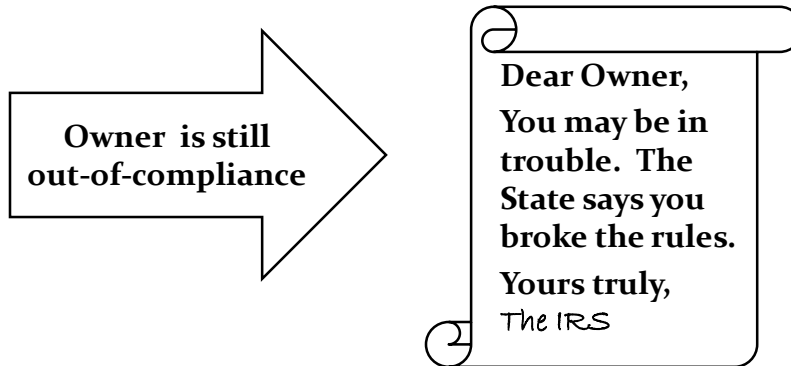
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Non-Compliance Reporting Nuances

- After the IRS receives the 8823 form:

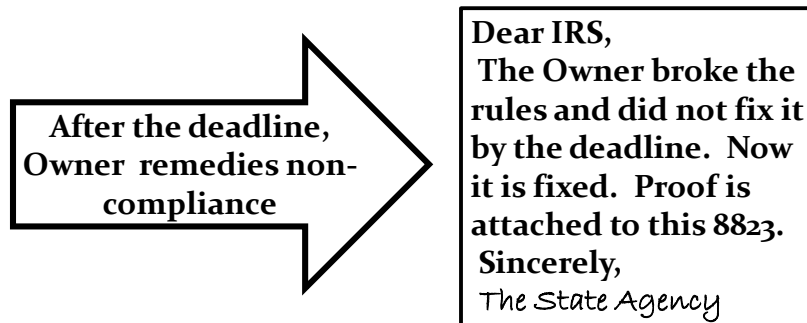


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Back in Compliance 8823

- State files another 8823 with the IRS



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WSHFC's list of Common Reasons for Non-Compliance

1. Failure to properly income-qualify a Resident at the time of initial move-in.
2. Failure to charge correct rent.
3. Failure to keep units suitable for occupancy at all times.
4. Failure to properly implement changes in utility allowances.
5. Violations of Uniform Physical Conditions Standards.
6. Failure to satisfy Special-Needs Commitments or additional affordable housing set-asides.
7. Failure to recertify Residents within 12 months or annually certify student status for every Resident.

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17 Types of Noncompliance

- A. Household Above Income Limit on Initial Occupancy
- B. Annual Recertification Incorrect, Incomplete, Undocumented
- C. Violations of UPC or Local Inspection Standards
- D. Owner's Annual Certification Incomplete, Incorrect or not Submitted
- E. Changes in Eligible Basis
- F. Failure to Meet Minimum Set-Aside
- G. Gross Rents Exceed Tax Credit Limit
- H. Project Not Available to General Public/Violations of Fair Housing Act
- I. Violations of Available Unit (140%) Rule

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17 Types of Noncompliance (Cont.)

- J. Violations of Unit Vacancy Rule
- K. Extended Use Agreement not Executed
- L. Low Income Units Leased to Non-Qualified Student Households
- M. Utility Allowance not Properly Calculated
- N. Failure to Respond to Requests for Monitoring Reviews
- O. HC Units Used on a Transient Basis
- P. Project no Longer in Compliance/Participating in the LIHC Program
- Q. Qualified Nonprofit Organization Failed to Materially Participate (when applicable)

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A. Household Above Income Limit on Initial Occupancy:

How it Happens

- Used wrong income limit
- Miscalculated household size
- Didn't count an income source
- Didn't consider future income changes
- Miscalculated income

How to Repair

- Treat household as a new tenant with current income limit
 - If qualified, non-compliance is corrected. Out of compliance from date of move-in TIC until date of new initial TIC.
 - If still not income-eligible, the unit is considered back in compliance when a new income-qualified household moves in.

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A. Household Above Income Limit on Initial Occupancy:

Penalties

- If the owner did not exercise “due diligence” :
 - The unit may not be counted towards
 - the minimum set-aside;
 - the applicable fraction;
 - May be issued an 8823 and subject to recapture of credits.
- Failing to meet the minimum set-aside:
 - 1st year of credit period, Owner is prohibited from ever claiming credits.
 - Subsequent taxable year, Owner loses all the credits for that year.

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G. Gross Rents Exceed Tax Credit Limit

How it Happens

- Failed to reduce tenant rent due to a UA increase
- Charged resident for a non-optional service
- Raised over-income resident’s rent to market before following the available unit rule.

How to Repair

- Reduce rent to at or below the maximum tax credit limit.

Penalties

- Credits are lost for the entire taxable year on all units for which rent was overcharged
- If happened first year of credit period and caused the minimum set-aside not to be met, the building does not qualify for the program.
- Rebating excess rent to the tenants will not remove the penalty

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L. Low Income Units Leased to Non-Qualified Student Households

How it Happens

- The owner rents to a household consisting of all full-time students who don't meet one of the exceptions, or
- Fails to document that a household qualifies for an exception.
- Household is determined to be a non-qualified student household at annual recertification.

How to Repair

The unit is back in compliance when is no longer occupied entirely by full-time students or the tenant qualifies under one of the exceptions. May need to offer the household an incentive to move out.

Penalties

The unit is disqualified for tax credits. The out of compliance date is the first day of the fifth month during the calendar year that the full-time student attended a qualifying educational organization.

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M. Utility Allowance Not Properly Calculated

How it Happens

- Wrong utility allowance used
- UA is not properly calculated, or
- Rents are not reduced when increase in UA puts them over maximum
- No annual written documentation of utility allowances

How to Repair

- Reduce rent charged to correctly reflect the utility allowance.
- Prove that property was not overcharging rent, despite paperwork negligence.

Penalties

- See slide on Gross Rents being overcharged.
- Lack of documentation could result in recapture of previously claimed credits.

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C. Violations of UPC or Local Inspection Standards

How it Happens

- State agency inspection or owner’s disclosure on the annual certification reveals ---
 - Property is not decent, safe and sanitary and in good repair
- Owner falsely certifies units are habitable on Owner’s Annual Certification

How to Repair

- Submit evidence of the corrected violations and/or
- State agency visual inspection.

Penalties

“Down” units are not eligible for credits until back in compliance.

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B. Annual Certification Incorrect, Incomplete, Undocumented

How it Happens

- Owner fails to complete on time or to document or completes incorrectly
- Household is nonresponsive to notices, rescinds move-out notice, or eviction is delayed

How to Repair

- Complete late certification either currently or retroactively
 - Unit is back in compliance the date the tenant signs TIC.
 - Retroactive certification helps to avoid violating the Available Unit Rule.
- If resident did not cooperate, document that notices were sent timely:
 - If they then give notice and vacate, there is no noncompliance;
 - If they fail to vacate, must recertify within 120 days;
 - If still non-cooperative, take action to remove the household.

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I. Violations of Available Unit (140%) Rule

How it Happens

- Owner recertifies a household as over 140% of MTSP or
- Owner fails to accurately calculate household's income at annual and does not realize household exceeds 140% of MTSP and
- Thereafter, Owner rents a vacant unit of comparable or smaller size **in the same building** to a non-qualified household.

How to Repair

- Restore the applicable fraction in one or more of the following ways:
 - Rent any combination of market rate, over-income, and out of compliance low-income units to qualified households, and/or
 - Re-certify an over-income tenant whose income decreases to below 140% of the current income limit, and/or
 - Re-certify an over-income tenant when the MTSP increases to an amount, such that 140 percent of the income limit is more than the tenant's income

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I. Violations of Available Unit (140%) Rule*

Penalties

- If any comparable or smaller unit that is available or that becomes available is rented to a nonqualified resident, all over-income units within the same building for which the available unit is comparable or *larger* lose their status as low income units.
- The date of the noncompliance is the date the market unit household moves in or the date the unit was pre-leased to them, whichever is earlier.

*A Building (BIN) Rule

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B. Annual Certification Incorrect, Incomplete, Undocumented

Penalties

- Corrected *prior to notification* of the compliance review by the state agency -- need not be reported;
- State may report a pattern of late recertifications
- Credits may be in jeopardy if owner is not demonstrating due diligence – notices sent, action taken, etc.

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E. Changes in Eligible Basis

How it Happens

- Eligible Basis is reduced when:
 - Space designated for tenant use is converted to space that is no longer available to them;
 - Owner charges fees for facilities included in the Eligible Basis.
- Noncompliance starts the date space is converted or when a fee is charged.

How to Repair

- Stop charging the fee.
- For converted space, state agency should not report the building back in compliance.
 - Instead should contact the IRS

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D. Owner's Annual Certification Incomplete, Incorrect or Not Submitted

How it Happens

Owner fails to complete or submit one or more of the certification items

How to Repair

- Submit a perfected annual certification (and any other required documentation)
- Back in compliance date received by state agency

Penalties

State agency can treat the project as out of compliance.

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H. Project Not Available to General Public & Fair Housing Act Violations

How to Repair

- All units are made available to the general public.
- Owner provides documentation that he/she has complied with court order and/or HUD's requirements and that the violation has been corrected.

Penalties

- Denial of credits on a per-unit basis from date of triggering event
- Loss and/or recapture of credits if the problem is systemic and/or Owner has therefore failed to meet the minimum set-aside
- Loss of credits for failure to enter into a settlement agreement with HUD, the DOJ, or a state or local fair housing agency

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K. Extended Use Agreement Not Executed

How it Happens

- The owner fails to sign and/or record such an agreement, or
- The agreement doesn't contain necessary provisions such as:
 - 30 year minimum
 - No eviction or termination of tenancy other than for good cause
 - No raising the gross rent unless otherwise permitted

How to Repair

Owner executes and records an extended use agreement within one year after the finding. The noncompliance is corrected and taxpayer can claim the low-income housing credit for past taxable years.

Penalties

No credit is allowable if the extended use agreement is not in effect as of the end of a taxable year in the credit period.

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F. Failure to Meet Minimum Set-Aside

How it Happens

- Rent-up did not go well
- Misunderstood or incorrectly listed Minimum Set-Aside
- Miscalculated income and household was never income-eligible.
- Violated the vacant unit rule or the 140% rule.
- Overcharged the rent.

How to Repair

Prove the state was wrong (not likely).

Penalties

- First year of the credit period, taxpayer is prohibited from ever claiming credits;
- At close of the taxable year for a subsequent year in the compliance period, entire credit is lost for that year.

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H. Project Not Available to General Public & Fair Housing Act Violations

How it Happens

- Units are
 - designated for or preference given to a single occupational group*
 - provided only for a member of a social org. or by an employer for its employees, or
 - part of a hospital, nursing home, sanitarium, life care facility, retirement home, or
 - in a dormitory, trailer park, or intermediate care facility.
- The owner
 - refuses to make reasonable accommodations or to allow reasonable modifications to the unit or common area
 - fails to comply with accessibility design requirements when built after March 13, 1991, or
 - otherwise discriminates under the Fair Housing Act

*Exception for certain artistic/literary focused projects

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J. Violations of the Unit Vacancy Rule*

How it Happens

Owner does not make reasonable attempts to rent vacant, low-income units before renting vacant market units of comparable or smaller size to non-qualifying tenants.**

How to Repair

Restore the applicable fraction by renting a sufficient number of vacant units to qualified low-income households.

Penalties

All vacant units **in the property** that were previously occupied by qualified households lose their status as low-income units.

*A Project Rule

**Owner must be able to prove reasonable attempts were/are being made.

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N. Failure to Respond to Requests for Monitoring Reviews

How it Happens

- Owner refuses to allow a monitoring agent to visit a site or inspect tenant files, or
- Owner repeatedly delays monitoring from taking place.

How to Repair

The owner is back in compliance when the agency performs the site visit and/or reviews the tenants' files.

Penalties

State agencies may remove a LIHC property from the program if the owner fails to respond to repeated notices for monitoring reviews.

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O. Housing Credit Units used on a Transient Basis

How it Happens

- No lease is on file for the tenant, or
- The tenant's initial lease term is not at least six months*

How to Repair

Execute a lease with a term of at least six months

Penalties

- The units are out of compliance as of the effective date of the initial certification until the new lease is executed.
- If the property is actually being used as transient housing, it does not qualify for the program.

*exceptions for certain transitional housing for the homeless.

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P. Project No Longer in Compliance/Participating in the LIHC Program

How it Happens

Including but not limited to:

- The building wasn't Placed in Service in time or failed to meet the Minimum Set-Aside.
- The building did not comply with what the state agency required at allocation.
- State and Owner both agreed to cancel the allocation.
- Owner chooses to stop treating the building as an LIHC property.

Penalties

Recapture may occur and no credits would be allowed in the remaining years of the credit period.

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Q. Qualified Nonprofit Organization Failed to Materially Participate

How it Happens

- Other areas of non-compliance under IRC §42(h)(5):
 - Non-profit loses its exempt status.
 - Non-profit does not have an ownership interest in the project.
 - Non-profit fails to "materially" be involved in development or operations.

How to Repair

Noncompliance is restored in the taxable year when the Owner:

- Reinstates a qualified nonprofit as an owner of the project and/or
- Satisfies the material participation test set forth in IRC §469(h)(1) for that taxable year.

Penalties

The State should file an 8823 with the IRS

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In addition to IRS Consequences . . .

- There are State consequences for non-compliance

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Noncompliance with State Requirements


The Commission takes noncompliance with State requirements very seriously. Potential areas of noncompliance with Commission requirements include but are not limited to:

- Failure to maintain Additional Low-Income Set-Asides
- Failure to properly restrict rents on such units
- Failure to pay annual compliance fees
- Failure to maintain Special-Needs Commitments
- Failure to restrict upfront rental charges
- Failure to advertise and provide notice of affordable housing vacancies to the extent such commitments were made

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- Note that failure to comply with Commission state requirements can jeopardize an Owner's ability to make future credit allocation requests.
- Serious and/or ongoing federal or state noncompliance may compel the Commission to pursue other remedies as allowed under the terms of the Regulatory Agreement, such as requiring the Owner to use a Commission approved property management company, imposition of rent garnishment or other legal action.

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- If the Commission discovers that Residents at a 100% low-income property are not being properly initially qualified, the Commission may require that the Owner re-instate third-party recertifications for all Residents, every year, until the Owner can prove that all Residents are income-qualified.
- The Commission also has the right to require re-instatement of third-party recertifications for any property that fails to abide by any and all program requirements, including but not limited to:
 - Preventing adult members from being added to Residents within the first six months of the initial lease without re-qualifying the entire household
 - Completing the first year third-party recertification for all Residents
 - Following the Next Available Unit Rule
 - Abiding by other Commission requirements

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Section 42 Non-Compliance

Q & A


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**Section 42 Non- Compliance:
How it Happens and How to Repair**

Thank you for your time and participation!

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