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# Preserving Long-Term Affordability in LIHTC Housing

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The Low-Income Housing Tax Credit (LIHTC) is the nation's largest and most significant affordable rental production program. Since its inception in 1987, the LIHTC has *supported* [https://www.urban.org/sites/default/files/publication/98761/lithc_past_achievements_future_challenges_final_0.pdf] the construction or rehabilitation of about 110,000 affordable rental homes per year, financing more than *3.7 million* [https://www.taxcreditcoalition.org/the-housing-credit/#:~:text=The%20Low-Income%20Housing%20Tax%20Credit%20%28Housing%20Credit%29%20is,to%20the%20National%20Council%20of%20State%20Housing%20Agencies.] affordable homes in total. By leveraging private capital to meet the critical housing needs of vulnerable populations, the LIHTC is one of the federal government's primary policy tools for addressing the shortage of affordable housing in the United States.

Despite the LIHTC's centrality in the country's affordable housing landscape, its time-bound affordability requirements pose a challenge to sustaining a sufficient affordable housing stock over the long term. Recent studies have warned that thousands of affordable LIHTC units have started phasing out of these affordability requirements and point to the need for greater resources to maintain and expand the number of affordable homes available to low-income renters. This blog provides context on LIHTC affordability periods, discusses strategies to preserve affordable units for longer or in perpetuity, and highlights bipartisan proposals to strengthen the policy.

**The Basics of LIHTC Affordability Periods**

The LIHTC incentivizes developers to build and maintain affordable housing for low-income households by leveraging tax credits to lower their costs. Unlike other federal affordable housing programs, the LIHTC is not funded through congressional appropriations. Rather, Congress provides the Internal Revenue Service (IRS) with the authority to issue tax credits to each state based on its population size, with a minimum for states with small populations. States receive a fixed number of tax credits annually, which state housing finance agencies (HFAs) then allocate to developers through a competitive process. Developers sell these credits to investors who, in turn, use them to offset their federal income taxes, raising capital for affordable housing properties.

In exchange for the tax credits, developers agree to provide and maintain a certain number of affordable homes for a specified period. LIHTC developers must abide by affordability requirements *laid out* [https://www.federalregister.gov/documents/2022/10/12/2022-22070/section-42-low-income-housing-credit-average-income-test-regulations] in the so-called 20-50 test, in which at least 20% of units must be occupied by tenants earning no more than 50% of area median income (AMI), or the 40-60 test, in which at least 40% of the units must be occupied by residents earning no more than 60% of AMI. As of 2018, *new income averaging provisions* [https://www.congress.gov/bill/115th-congress/house-bill/1625] allow LIHTC owners to serve households earning as much as 80% of AMI as long as the average income limit in the property does not exceed 60% of AMI.

There are two types of LIHTCs available to developers: the 9% credit and 4% credit. The former is typically reserved for new construction, while the latter is reserved for rehabilitation or construction financed using other subsidies, particularly federally tax-exempt bonds called private activity bonds (PABs).

From 1986 to 1989, federal LIHTC provisions included a 15-year compliance period. Beginning in 1990, Congress created an “extended use period” of an additional 15 years, for a total of 30 years. Though LIHTC property owners are still able to opt out of affordability requirements after the first 15 years through a regulatory relief process, *res earch* [https://www.huduser.gov/portal/publications/hsgfin/lihtc_report2012.html] has shown that most LIHTC developments remain affordable past the 15-year initial compliance period.

### LIHTC Preservation After Year 30

As LIHTC developments built after 1990 begin to age out of the 30-year extended use period, the question of whether affordable units could be lost has become pertinent. *Est imates* [https://nlihc.org/sites/default/files/Balancing-Priorities.pdf] find that nearly 500,000 current LIHTC units—representing nearly a quarter of the total stock—will reach their 30-year mark by the end of this decade. Some states mitigate this concern by requiring *extended affordability periods* [https://www.housingfinance.com/news/the-next-preservation-challenge-expiring-lihtc-properties_o] for LIHTC-financed properties. California and Nevada, for example, have 50-year affordability requirements. Others go even further: Utah requires 99 years of affordability, while Vermont has incorporated an "in perpetuity" standard in its state LIHTC program. LIHTC developments that receive capital from other federal housing programs, such as HUD's HOME Investment Partnerships Program and the new *Green and Resilient Retrofit Pro gram* [https://www.nixonpeabody.com/-/media/files/alerts/2023/05/hud-publishes-new-green-and-resilient-retrofit-program-funding-opportunities.pdf#:~:text=All%20properties%20assisted%20with%20GRRP%20funding%20shall%20be,regarding%20affordability%20running%20in%20favor%20of%20HUD%20or], must also maintain additional affordability periods.

However, with the extended use period ending for hundreds of thousands of LIHTC units in the coming years, the question of how to recapitalize and rehabilitate these units in ways that sustain or even enhance their affordability should be a central concern of federal housing policymakers.

Once the extended use period ends, LIHTC owners generally have *four options* [https://www.novoco.com/podcast/april-25-2023-year-30-and-beyond-what-lihtc-owners-need-know-about-end-extended-use-period]:

- Convert subsidized units to market rate rents
- Apply for additional tax credits that would establish new affordability requirements

Voluntarily maintain their affordable homes

Sell the property

The ease of converting units to market rate depends on many factors. Many of the federal and local financing sources that LIHTC developers rely on can have additional requirements—such as extended affordability periods, transition periods for rent increases, and tenant rights provisions. However, a *recent analysis from Freddie Mac* [https://mf.freddiemac.com/docs/DTS-LIHTC-at-risk.pdf] found that LIHTC properties that left the program generally had higher rents when compared with LIHTC properties. While many of these homes are still rented for less than conventional market rate units, the increase can still lead to unaffordable rents for the lowest-income households. Properties in high-value markets are especially vulnerable to market rate conversion, as owners could significantly increase their revenue by matching the rising rents around them.

In contrast to market rate conversions, incentivizing owners to apply for new credits at the end of an affordability period—referred to as resyndication—is one way to preserve affordability. To acquire a new LIHTC allocation, owners must commit to a new affordability period. This is mostly done with 4% credits, which finance new construction and rehabilitation and require the use of private activity bonds for financing. To that end, policies that make it easier for owners of existing LHITC properties to rehabilitate under new affordability requirements can help halt the loss of affordable homes.

**Policy Proposals for Preserving Affordable LIHTC Units**

Preserving affordable homes in LIHTC properties will likely require reckoning with affordability periods, expanding the resources available to support preservation, and better targeting those resources to support families most in need and properties most at risk.

To strengthen the housing credit and the preservation toolkit, Congress could consider the following reforms:

1. Extend the federal LITHC affordability period in perpetuity

To address concerns over the phase-out of units from the federally mandated 30-year period, Congress can establish an "in perpetuity" affordability standard for new LIHTC units, while ensuring that there is sufficient funding available to recapitalize and resyndicate properties as needed.

State-level LIHTC policy can be instructive on this point. Policymakers in many states have employed strategies such as offering additional tax incentives or financial assistance for property rehabilitation for developers who commit to extended affordability periods. *Research* [https://escholarship.org/content/qt9fs1m0tt/qt9fs1m0tt_noSplash_d2119cd7a2815706b327a55fb40d07dd.pdf?t=q7cj6c] on California's 50-year affordability period has shown that lengthening the affordability standard had a negligible impact on investor interest in participating in the LIHTC program.

This recommendation was included in BPC's *American Housing Act* [https://bpcaction.org/wp-content/uploads/BPC-Action-Housing-Legislative-Brief.pdf], which also proposes additional, timely reforms to strengthen the LIHTC and unlock its potential to serve more extremely low-income families.

2. Increase federal housing credit allocations

The ability of the LIHTC program to produce affordable housing is limited by the amount of tax credits that states and territories receive. An increase in the amount of housing credit resources would address the significant unmet demand for LIHTC development—in a typical year, developers request *three times* [https://rentalhousingaction.org/wp-content/uploads/2023/05/AHCIA-Detailed-Bill-Summary-May-2023-1.pdf] the amount of available credits.

This recommendation is included in the recently reintroduced *Affordable Housing Credit Improvement Act* [https://www.congress.gov/bill/118th-congress/house-bill/3238]

(AHCIA), which would restore the 12.5% cap increase that expired in 2021 and further increase annual housing credit allocations by 50% over the next two years.

In the next decade, the additional allocation is *estimated* [https://rentalhousingaction.org/wp-content/uploads/2023/05/AHCIA-Detailed-Bill-Summary-May-2023-1.pdf] to increase affordable rental housing production and preservation by up to 232,500 more homes than would otherwise be financed under current law.

3. Reduce the amount of bond financing needed to access credits.

Due to the PAB requirement involved for 4% LIHTC allocations, many states have more demand for affordable housing than they are able to finance with their existing PAB volume cap authority. By lowering the threshold for the so-called "50% test," which requires developers to finance half of a project with PABs to qualify for 4% LIHTCs, Congress would give HFAs greater flexibility to finance rehabilitation needs.

The AHCIA also addresses this recommendation by lowering the bond financing threshold to 25%, allowing states to produce and preserve more bond-financed developments.

Beyond these three recommendations, two additional provisions in the AHCIA would further incentivize rehabilitation and preservation:

- Including tenant relocation expenses in rehabilitation expenditures, which would allow these costs to be capitalized as part of the cost of rehabilitation.
- Providing flexibility for existing tenants' income eligibility if they met income requirements upon initial occupancy, which would resolve the tension between adopting new affordability requirements as part of a recapitalization and allowing tenants who have experienced income growth (within a reasonable limit) to stay in their homes.

### Conclusion

The LIHTC is a critical tool for addressing the affordable housing crisis in the United States, facilitating the development and preservation of millions of affordable rental units for low-income households. Given the increasing demand for affordable housing and the looming challenges facing LIHTC developments as more units phase out of the current federal affordability requirement, it is crucial for policymakers to act swiftly in implementing reforms.

By adopting the policy proposals outlined above, policymakers can strengthen the LIHTC and help secure affordable housing for millions of low-income Americans for generations to come.



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