

## Low-Income Housing Tax Credit Program

### What is the Low-Income Housing Tax Credit program?

The Low-Income Housing Tax Credit (LIHTC) program was established by the Tax Reform Act of 1986 (Internal Revenue Code Section 42) to create market incentives for the acquisition and development or rehabilitation of affordable rental housing. It is the federal government's primary program for encouraging the investment of private equity in the development of affordable rental housing.

### How does the program work?

The LIHTC program authorizes state housing credit agencies (HCAs) to award 9 percent and 4 percent federal tax credits to developers of affordable rental housing. The tax credits are used by developers to raise equity financing for their projects.

The equity capital generated from the tax credits lowers the debt burden on LIHTC properties, making it easier for owners to offer lower, more affordable rents; while investors, such as banks, obtain a dollar-for-dollar reduction in their federal tax liability.

National banks can invest in LIHTC projects by making direct investments in affordable housing projects and investments in funds comprised of multiple projects. These investments will receive a stream of tax credits during the initial 10 years of a 15-year tax compliance period. Such

investments are typically structured as real estate limited partnerships or limited-liability companies. Thus, a national bank, as a limited partner or limited-liability member, can generate additional returns with the pass through of depreciation and cash flow in these real estate investments.

### How are tax credits awarded?

Under the authority of the Internal Revenue Service (IRS), state HCAs administer the LIHTC program through qualified allocation plans (QAPs). States are allowed to set specific allocation criteria for awarding tax credits and must develop QAPs that identify and prioritize housing needs, especially for low-income renter households. Criteria used to guide the selection of projects awarded tax credits must also be included in a state's QAP. HCAs award tax credits to developers based on the housing needs identified and selection criteria established.

At the state level, the annual volume cap for the 9 percent tax credit is equal to the state population multiplied by a fixed per capita rate. The 4 percent tax credit allocation is based on the state's volume cap for private activity bonds, which is equal to the state population multiplied by a per capita rate. Nonprofit and for-profit developers apply for the tax credits to build and rehabilitate affordable rental housing. Tax credits are available only to help cover the cost of units within qualified projects reserved for rental to low-income households.

## **How can LIHTCs benefit a bank?**

Banks choose to invest in LIHTC projects for several reasons. When properly managed, investments in LIHTCs can earn attractive rates of return, with yields above the 10-year U.S. Treasury bond rate. They also can spur on additional commercial lending opportunities with existing customers and newly established banking relationships.

### ***Community Reinvestment Act (CRA)***

Banks may receive positive CRA consideration for community development activities related to LIHTC projects and funds, provided the activities benefit a bank's assessment area or a broader statewide or regional area that includes the bank's assessment area(s) (AA). The bank's AA(s) need not receive an immediate or direct benefit from the bank's participation in the activity, provided the purpose, mandate, or function of the activity includes serving geographies or individuals located within the institution's AA(s). Examiners will consider these activities even if they will not benefit the bank's AA(s), as long as the bank has been responsive to community development needs and opportunities in its AA(s).

Examples of activities that may be eligible for CRA consideration include direct investments in LIHTC projects, predevelopment financing or construction/permanent financing to LIHTC projects, investments in funds that specialize in funding and managing LIHTC projects, and technical assistance to nonprofit organizations that help identify and counsel potential low- or moderate-income residents.

Investments in LIHTC projects (or a fund consisting of several projects) are eligible investments for national banks under the OCC's Part 24 authority. Federal savings

associations may make public welfare investments under specific authorities that are described on the [OCC's Public Welfare Investments Web Resource Directory](#)

## **What are the risks to bank investors?**

A bank should consider the compliance, tax planning, underwriting and credit, liquidity, and operational/reputation risk of any investment it may make.

To take full advantage of the tax credits under the LIHTC program, a bank should have taxable income projected for the term of the investment and evaluate its exposure to the alternative minimum tax. LIHTCs are subject to recapture if a project fails to house income-qualified tenants at affordable rents for a 15-year compliance period.

Bank investors typically underwrite LIHTC investments as commercial real estate transactions. A bank investor must perform front-end due diligence to ensure satisfaction with the financial capacity, performance, management capacity, and expertise of the project developer and general or managing partner.

As an investor in a multifamily property operating for a minimum of 15 years, a bank must be comfortable with projected reserves, debt service coverage, and guarantees. Once a transaction meets a bank's underwriting criteria, the bank can evaluate the transaction from an investment perspective.

Banks should consult their own tax advisors about the tax treatments and consequences that may apply to their own transactions.

## For More Information

### Office of the Comptroller of the Currency

- [Low-Income Housing Tax Credits: Affordable Housing Investment Opportunities for Banks](#) *Community Developments Insights Report*, March 2014.
- [Investing in Low-Income Housing Tax Credits: A Sound Opportunity for Community Banks](#), *Community Developments Investments*, Spring 2006.
- [The Low-Income Housing Tax Credit Program: Community Banks Reaps More than Monetary Returns](#), *Community Developments Online News Articles*, Spring 2000.
- [Tax Credits 101](#), *Community Developments Online News Articles*, Spring 2000.
- [Tax Credit Resource Guide](#) is a directory that provides easy access to information for a sampling of organizations that can provide resources to banks interested in investing and lending to federal Low-Income Housing Tax Credit projects.
- Community Affairs - [Community development resources](#) are available to national banks, government agencies, and community organizations
- [District Community Affairs Officers contact information](#)

### U.S. Department of Housing and Urban Development

- [LIHTC Database](#)

### Industry Sources

- [Affordable Housing Investors Council \(AHIC\)](#) provides information about the benefits of investing in affordable housing tax credit properties, educates corporate investors on all aspects of affordable housing, and discusses issues

of importance to investors in the industry.

- [National Association of Local Housing Finance Agencies \(NALHFA\)](#) is a national association of professionals, including city and county agencies, non-profit organizations, underwriters, consultants, financial advisors, bond counsels, and rating agencies, who help finance affordable housing in the broader community development context at the local level.
- [National Association of State and Local Equity Funds \(NASLEF\)](#) promotes the efficient management of state and local equity funds to create or rehabilitate affordable rental housing throughout the United States.
- [National Council of State Housing Agencies \(NCSHA\)](#) was created by the nation's state Housing Finance Agencies (HFAs) as a nonprofit affordable housing advocacy organization that represents state HFAs, the District of Columbia, Puerto Rico and the Virgin Islands, two (non-HFA) state agencies that allocate LIHTCs, and for profit and nonprofit firms in the affordable housing field.

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The Tax Cuts and Jobs Act (Pub. L. No. 115-97), signed into law on December 22, 2017, made numerous changes to the Internal Revenue Code. This document has NOT been updated to reflect these changes. Banks or other entities considering a tax credit equity transaction should consult with a tax professional with knowledge of how the changes in the tax code may affect specific tax credit equity transactions.