Minnesota Housing Finance Agency

HOUSING TAX CREDIT PROGRAM

COMPLIANCE MANUAL

Minnesota Housing finances and advances affordable housing opportunities for low and moderate income Minnesotans to enhance quality of life and foster strong communities.

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Introduction

The Minnesota Housing Finance Agency has been designated by the Minnesota Legislature as the primary apportionment Agency of Housing Tax Credits in Minnesota. Qualified local cities and counties have also been designated by the Legislature as suballocators of the tax credit: the cities of Duluth, Rochester, St. Cloud, St. Paul and Minneapolis, and Washington County and Dakota County.

The purpose of the Minnesota Housing Finance Agency (Minnesota Housing) is to ensure the availability of decent, safe, energy efficient, and affordable housing to low and moderate-income households. In order to achieve its purpose, Minnesota Housing is active in: lending and financing, allocating housing grants and subsidies, advocating for affordable housing, establishing state housing policies and providing technical assistance to housing sponsors.

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Foreword

Minnesota Housing shall be under no obligation to undertake an investigation of the accuracy of the information submitted for Compliance Monitoring. Minnesota Housing's review shall not constitute a warranty of the accuracy of the information, nor of the quality or marketability of the housing to be purchased, constructed, or rehabilitated pursuant to the program. Developers, potential investors and interested parties should undertake their own independent evaluation of the feasibility, suitability and risk of the project. If any information submitted by building owners to the Minnesota Housing is later found to be incorrect in any material respect, it is the responsibility of the building owners to inform Minnesota Housing and to request a reexamination of the information. Interested parties should consult with a knowledgeable tax professional prior to entering into any commitment concerning the use and claim of housing tax credits.

In January 2007 the Internal Revenue Service (IRS) released its *Guide for Completing Form 8823, Low-Income Housing Credit Agencies Report of Noncompliance or Building Disposition* (8823 Guide), and updated it in September, 2009. The 8823 Guide was not intended to change any Section 42 rules or policies, but to provide definitions of what IRS considers "in compliance" and for consistency in reporting "out of compliance," and "back in compliance," on IRS Form 8823. IRS did not include an effective date for state agencies to make any needed adjustments to policies and procedures to the extent existing policy and procedure do not conform to the instructions in the 8823 Guide.

Most of Minnesota Housing's compliance, monitoring, and reporting policy and procedure are already reflective of instructions in the 8823 Guide. However, some adjustments needed to be made and this manual is reflective of those adjustments. Owners are required to comply with the new policy and procedure by 1/1/2008.

This manual has not been reviewed or approved by the Internal Revenue Service (IRS) and should not be relied upon for interpretation of federal income tax legislation or regulations.

Background and Overview

Section 42 (m)(i)(B)(iii) of the Internal Revenue Code requires housing credit agencies to include in their Housing Tax Credit Allocation Plan a procedure to monitor all tax credit projects for compliance with the requirements of Section 42, the Housing Tax Credit Program (HTC), throughout the compliance period.

An allocating agency must have a procedure for monitoring compliance with the provisions of the Code and notifying the Internal Revenue Service (IRS) of any noncompliance of which it becomes aware whether or not it is corrected. The monitoring requirements became effective on January 1, 1992, were amended on January 14, 2000, and apply to all tax credit projects, even if the projects received an allocation prior to 1992. Minnesota Housing, as the state allocating agency, is authorized by the Code to charge a reasonable fee to cover the costs of compliance monitoring. The IRS has issued final regulations, Income Tax Regulation 1.42-5 ("1.42-5"), relating to the requirements for compliance monitoring.

The purpose of this manual is to set forth the procedures to be followed by Minnesota Housing and the owners of tax credit projects in order to comply with the requirements of Section 42. The compliance monitoring requirements are subject to modification by the IRS and income determination requirements are subject to modification by HUD. Minnesota Housing will revise this manual annually.

Owners should be aware that section 1.42-5 explicitly provides that the credit agency monitoring procedures only address the requirements for housing credit agency monitoring, and do not address forms and other records that may be required by the IRS on examination or audit.

Projects with Allocations from Multiple Allocators

Some tax credit projects receive tax credits from both Minnesota Housing and a suballocator. Tax credit compliance monitoring for those projects will be done by the entity which first allocated credits to the project, unless the allocators make other arrangements regarding the project.

Tax Exempt Bond Projects

Some tax credit properties receive their allocation of credits through the use of tax-exempt bonds. Minnesota Housing will monitor developments that received an allocation through the issuance of tax-exempt bonds, except where the bonds were issued in a suballocator jurisdiction. In those cases, the suballocator will be responsible for compliance monitoring unless other arrangements are made. Tax-exempt bond developments must comply with the same IRS requirements and HTC compliance monitoring procedures as non-tax exempt bond developments.

Chapter 1 – Program Summary

The following is a brief summary of the requirements of the tax credit program. It is not intended to be detailed or comprehensive:

A. Minimum Set Aside Election

Two options are available for the minimum set aside requirement:

1. No less than 20% of the housing units must be set aside for tenants whose incomes are 50% or less of the area median income; or
2. No less than 40% of the housing units must be set aside for tenants whose income are 60% or less of the area median income.

Each building is considered a separate project under IRC Section 42(g)(3)(D), and the minimum set-aside applies separately to each building, unless the owner elects to treat buildings as a multiple-building project, in which case the minimum set-aside and other project rules apply to the identified project. Owners identify the building(s) in a multiple-building project by attaching a statement to the owner's first-year tax return. See instructions for Form 8609, line 8b for details.

Rental agents or managers should confirm the set-aside that was established by the building owner at the time the set-aside option was made (the election is made on form 8609 for the first year of the credit period), to ensure continued compliance. Once selected, the option cannot be changed. Note that this is only the minimum set-aside. All low-income units must comply with the respective minimum set-aside income and rent election. For example, for 20/50 minimum set-aside, if building applicable fraction is 100%, all tax credit units must have an income and rent restriction of 50% AMI.

Owners may elect additional state-established set-aside requirements (such as additional rent restrictions, serving certain targeted populations, etc.) as a condition of obtaining credits. These will be reflected in the allocation documents, which include the Carryover Agreement and Declaration of Land Use Restrictive Covenants. If such additional set-asides are elected, they must be maintained throughout the compliance period and extended use period, and will be monitored at the same time as, and in a manner similar to, the Section 42 requirements.

If a property is financed using NAHASDA or HOME funds which 1) have not been subtracted from the basis calculation or 2) have an interest rate below the Applicable Federal Rate, and the owner receives tax credits at the seventy percent (70%) present value rate (i.e., 9 percent credits), then owner must rent forty percent (40%) of the units **in each building** to households whose income is fifty percent (50%) or less of area median income. There is not a corresponding rent restriction with this HOME income limit set-aside. Rent limits are set according to the elected tax credit set-aside and/or any additional rent

restrictions under which the allocation was made. Note: Buildings placed in service after 7/30/2008, are not subject to this provision.

B. Rent and Income Requirements

The income necessary to be eligible to rent a unit is based on the household income limits adjusted for family size for the area in which the project is located. Income determination is similar to Section 8 income qualifications as described in 24 Code of Federal Regulations (CFR) 813.106.

The formula for computing gross rent is based on 1.5 persons per bedroom not to exceed 30% of the corresponding income election.

C. Rent and Income Figures

The U.S. Department of Housing and Urban Development annually publishes median income figures for all Minnesota counties. Minnesota Housing uses these figures to calculate the maximum allowable rents and tenant incomes for rental units receiving the tax credit. Minnesota Housing publishes income and rent limits, based on area median income, for projects receiving an HTC allocation and sends out the updated limits as they become available.

Due to the Housing and Economic Recovery Act of 2008 (HERA), income limits for projects funded with tax credits and/or financed with tax exempt housing bonds (TE Bonds) are now calculated and presented separately from the Section 8 income limits. Beginning with the publication of FY2009 Median Family Income estimates and Income Limits, the section 8 income limits CAN NO LONGER be used for tax credit or TE Bond properties.

To avoid noncompliance, be sure you are using the correct limits table. In 2010, there are three sets of income and rent limit tables and, according to HERA, the Placed in Service (PIS) date for a project determines which set of limits to use.

- **Table A** is for properties placed in service before 1/1/2009
- **Table B** is for properties placed in service from 1/1/2009 to 5/13/2010.
- **Table C** is for properties placed in service on or after 5/14/2010.

Each year, when new limits are released, there will likely be an additional table.

When determining which table to use for properties with placed in service dates both before and after the income limit effective dates, consider the following:

- The earliest PIS date for a building governs, so if a building has acquisition credits with a PIS date prior to 1/1/2009, it uses Table A even if rehab is PIS after 1/1/2009.
- Under Section 42 each building is considered a separate project unless the owner elects to treat buildings as a multiple-building project. The multiple-building election is made by the owner on line 8b in Part II of form 8609. However, since form 8609 is typically issued well after the placed in service date, owners of properties with buildings placed in service both before and after

1/1/2009 must determine what this election will be and which buildings are part of the project. Owner must document this determination in the property's records, and when completing Part II of form 8609, the election must be consistent.

- If the earliest PIS date for any building that is part of a multiple-building project (line 8b is or will be checked "yes" and owner has identified the buildings that are part of the multiple-building project) is 12/31/2008 or earlier, then all buildings that are part of that multiple-building project use Table A. If the earliest PIS date is on or after 1/1/2009 but before 5/14/2010, then all buildings that are part of that multiple-building project use Table B. If the earliest PIS date is on or after 5/14/2010, then all buildings that are part of that multiple-building project use Table C.
- If buildings are not part of a multiple-building project (line 8b is or will be checked "no"), then buildings PIS before 1/1/2009 use Table A, buildings PIS on or after 1/1/2009 but before 5/14/2010 use Table B, and buildings PIS on or after 5/14/2010 use Table C.

D. Building Regulations

The credit amount allocated to each building in a project is partially calculated on the following factors:

1. Eligible Basis:

   In general, the Eligible Basis of a building is equal to the building's adjusted basis for acquisition, rehabilitation or construction costs for the entire building, subject to certain conditions and modifications set forth in Section 42 (d). As a general rule, the adjusted basis rules of Section 1016 apply, with the exception that no adjustments are made for depreciation. Some of the special provisions for determining eligible basis under Section 42 (d) are:

   Buildings located in areas designated as a "qualified census tract" or "difficult development area" may be eligible for an increase in allowable basis.

   If non-HTC units are of a quality standard greater than that of HTC units in the building, the costs of non-HTC units generally are not included in eligible basis.

   The cost of depreciable property used in common areas or provided as comparable amenities to all residential units (e.g. carpeting and appliances) is included in determining eligible basis. The cost of tenant facilities (e.g. parking, garages, and swimming pools) may be included in eligible basis if there is no separate charge for use of the facilities and they are made available on a comparable basis to all tenants in the project.

   Eligible Basis is reduced by federal grants, residential rental units which are above the average quality standard of the low-income units, any historic rehabilitation credits, and nonresidential rental property.

The Eligible Basis, as of the end of the first year of the credit period, is reported to the IRS on Part II of the form 8609, and does not change from year to year.

2. Applicable Fraction

The applicable fraction is the lesser of:

- The unit fraction, which is the number of HTC units in a building divided by the total number of residential rental units; or
- The floor space fraction, which is the total floor space of the HTC units in the building divided by the total floor space of the residential rental units in the building.

When determining which units to include in the numerator (low-income units), and in the denominator (total units) of the applicable fraction, please note:

- Units that have never been occupied or are occupied by a nonqualified household cannot be included in the numerator, but must be included in the denominator;
- Vacant units that were last occupied by a nonqualified household cannot be included in the numerator, but must be included in the denominator.
- Units not suitable for occupancy, including tax credit units being rehabilitated in the first year of the credit period, cannot be included in the numerator, but must be included in the denominator.
- Common space units (units for FT manager, FT maintenance or security – see par. E, below), are not included in either the numerator or denominator.

E. Full Time Resident Manager's Unit

The full time resident or on-site manager's unit may or may not be included in determining the applicable fraction depending on the circumstances. According to IRS Revenue Ruling 92-61, the ways in which the on-site manager's unit may be considered are:

1. For buildings that have been placed in service after September 9, 1992, the full time manager's unit must be treated as common space (i.e., it would not be included in either the numerator or denominator of the applicable fraction).

2. For buildings that were place in service prior to September 9, 1992, the full time manager's unit may be treated as follows:

   a. The full time manager's unit is considered a qualified low-income unit (the rent is restricted to a qualifying amount and the resident manager is a certified low-income tenant); or

b. The full time manager's unit is considered common space. As common space, the unit would not be included in either the numerator or the denominator of the applicable fraction.

Example: A building contains 24 units and the applicable fraction is 100%. Credits were allocated on 23 units. This means that the manager's unit was treated as common space when the credit was allocated. The applicable fraction would be 23/23 or 100%.

A full time manager or maintenance person must occupy a resident manager's unit. The number of hours worked does not define full-time; rather it is defined that the manager's presence on site is reasonably required for the development. Some things to consider are: what is warranted by the type, size and/or location of the development, as well as what is needed in terms of the resident population. Some developments may not need to employ a resident manager for what is normally considered full-time and other developments may need to employ more than one on-site manager or maintenance person. Full-time is considered to be whatever is reasonably required to make operations run smoothly at the development. As a general guide, a manager who performs management functions such as leasing units, preparing certification paperwork, cleaning, general maintenance, preparing turnovers, collecting rent, etc., and is available to the site on an on-call basis to respond to emergencies may be considered a full-time manager under this ruling. According to Revenue Ruling 2004-82, dated August 30, 2004, a unit may also be occupied by a full-time security officer and be treated as common space, if reasonably required.

All developments, especially those that are new allocations, need to notify Minnesota Housing of the status of common space unit(s) and which method is being used. When notifying Minnesota Housing, it is necessary to include the project name and HTC number, the building address and BIN number, the unit number, the number of bedrooms in the unit, the square footage, the current resident manager, maintenance person, or security personnel's name and a description of duties and time involved. If not previously considered as part of the allocation process, Minnesota Housing will issue a letter acknowledging such common space unit. For the most part, Minnesota Housing will rely on the owner's determination of whether a full time unit is reasonably required by the development. However, if Minnesota Housing becomes aware that the unit is not occupied by a full time manager, maintenance, or security personnel, as represented by the owner, it may become a noncompliance issue.

Note: If the owner is charging rent for the unit, the Internal Revenue Service may determine that the unit is not reasonably required by the project because the owner is not requiring the manager, maintenance or security personnel to occupy the unit as a condition of employment.

A unit occupied by a part time manager, caretaker, or maintenance person must either be treated as a qualified low-income unit or as a market rate unit. If the unit is treated as a qualified low-income unit, then the household must meet all tax credit eligibility criteria. Please note that any reduction in rent in exchange for services must be considered as income.

F. Calculating the First Year Applicable Fraction

To determine the applicable fraction for the first year, find the low-income portion as of the end of each full month that the building was in service during the year. Add these percentages together and divide by 12 (per instructions on IRS Form 8609 and 8609- A). Note that the applicable fraction must be calculated for both the unit and floor space fraction.

Assume that a low-income building was placed in service on January 15, and has the following lease-up schedule during the first year of the credit period:

Month	Low-Income Units	Total Units	Monthly Unit Fraction	Low Income Sq Ft	Total Square Feet	Monthly Square Foot Fraction
January	1	10	0%	1000	12000	*0.00%
February	2	10	20%	2000	12000	16%
March	4	10	40%	3800	12000	31.66%
April	6	10	60%	5400	12000	45%
May	7	10	70%	6300	12000	52.5 %
June	7	10	70%	6300	12000	52.5 %
July	7	10	70%	6300	12000	52.5 %
August	8	10	80%	7200	12000	60%
September	9	10	90%	8400	12000	70%
October	10	10	100%	12000	12000	100%
November	10	10	100%	12000	12000	100%
December	10	10	100%	12000	12000	100%
	Sum of monthly Unit Fraction/12		66.66%	Sum of monthly Sq Ft Fraction /12		56.68%

*The owner may **not** count the unit occupied in January toward the first-year applicable fraction since the building was not placed in service the full month. For all other months, even if a resident moved in to a unit on the last day of the month, that unit is considered occupied at the end of the month. The first year applicable fraction for this building would be 56.68% based on this lease-up schedule.

G. Qualified Basis

Qualified basis is the portion of the eligible basis applicable to Housing Tax Credit units in a building. Qualified Basis is the product of a project's Eligible Basis multiplied by the Applicable Fraction. The original qualified basis is determined as of the last day of the first year of the credit period and is reported to the IRS on Part II of Form 8609.

H. Claiming Credits

The credits may be taken annually for 10 years and are based on a percentage of the qualified costs of the building. For 1987, the applicable rates were 9 percent for new construction and substantial rehabilitation and 4 percent for

buildings with federal subsidies and for acquisition and rehabilitation of existing buildings. (In order for an existing building to qualify for the credit in connection with substantial rehabilitation, there must be a period of at least 10 years between the date of acquisition and the date the building was last placed in service.)

I. Compliance Period

All developments receiving a credit allocation must comply with eligibility requirements for a period of 15 years beginning with the first taxable year of a building's credit period. This is typically referred to as the "compliance period". All developments receiving a credit allocation after December 31, 1989, must enter into a Declaration of Land Use Restrictive Covenants for Housing Tax Credits with Minnesota Housing at the time a final allocation of credit is issued, which requires developments to comply with eligibility requirements for a minimum additional 15 years beyond the 15-year compliance period for a total of 30 years. This is typically referred to as the "extended use period". The Declaration of Land Use Restrictive Covenants is a recorded covenant which runs with the land. See Section 9, *Compliance and Monitoring After Year 15* for details on requirements in the extended use period.

J. Outline of Minnesota Housing Compliance Process

1. All tax credit projects that claim the tax credit in the jurisdiction of Minnesota Housing must submit a complete certification and annual report to Minnesota Housing by February 15th or the next business day of each calendar year (see Chapter 4 for further details):

2. Minnesota Housing will conduct a compliance inspection of each development at least once every three years and will perform a file review and physical inspection on 20% of the low-income units.

3. For new projects, Minnesota Housing will conduct a monitoring inspection no later than the end of the second year of the credit period.

4. If changes in equity ownership are planned or have occurred, owner must submit a Notice to Transfer Ownership or Change Owner Name or Status (HTC 27), and other necessary documentation. (See Chapter 7 of this manual for detailed information.)

5. In the event that Minnesota Housing (i) does not receive certification or documentation, or (ii) is not permitted to inspect tenant files, or (iii) upon inspection or review, Minnesota Housing becomes aware of an aspect of the project, which is not in compliance:

    a. Minnesota Housing will provide written notice to the owner of the lack of certification, inspection, or other non-compliance;

b. The owner will be given a time period, to be determined by Minnesota Housing but not to exceed 90 days, to correct the non-compliance.

Minnesota Housing will file IRS Form 8823 "Report of Noncompliance" no later than 45 days after the end of the correction period whether or not the non-compliance has been corrected. See Chapter 8.

K. Owner's Responsibility

Each owner has chosen to utilize the HTC Program to take advantage of the tax benefits provided. In exchange for these tax benefits, certain requirements must be met.

Prior to issuance of a final tax credit allocation, the owner must certify to the total project costs. The owner must also certify that all Program requirements have been met. Any violation of the requirements of the Program could result in the loss of tax credits to the owner.

The owner is responsible for compliance with the Code. Owner must take any lawful action to comply fully with the Code and with all applicable rules, rulings, policies, procedures, regulations or other official statements promulgated or proposed by the United States Department of the Treasury, or the Internal Revenue Service, or the Department of Housing and Urban Development from time to time pertaining to Owner's obligations under Section 42 of the Code. Minnesota Housing is assigned the responsibility for monitoring compliance. Any and all financial consequences to the owner as a result of noncompliance, whether identified by Minnesota Housing or the IRS, will be the responsibility of the owner.

Successful operation of a HTC development is management intensive; the owner is responsible for ensuring that the project is properly administered. Thorough understanding of HTC requirements and compliance monitoring procedures requires training of owners and managers. This training should occur before a development is occupied and should be provided to the on-site property management staff. At a minimum, such training should cover key compliance terms, qualified basis rules, determination of rents, tenant eligibility, file documentation, available unit procedures and unit vacancy rules, agency reporting and record retention requirements, and site visits. Continuing education each year or at a minimum every other year is strongly recommended in order to keep up with regulatory and procedural changes.

L. Noncompliance

If the management agent and/or the owner determines that a building or entire project is not in compliance with program requirements, Minnesota Housing must be notified immediately. The management agent and/or the owner must formulate a plan to bring the project back into compliance, and advise Minnesota Housing in writing of such a plan.

Chapter 2 – IRS Reporting Requirements

The IRS and Minnesota Housing require owners to file specific forms for compliance and reporting purposes. Failure to submit required forms as outlined in this manual to either the IRS or Minnesota Housing as appropriate will constitute non-compliance and may make the owner subject to recapture or ineligible for credit.

A. Low Income Housing Allocation Certification (IRS Form 8609)

One IRS Form 8609, Low Income Housing Allocation Certification ("8609") will be issued by Minnesota Housing for each building within a project.

Note: If allocations were issued in multiple years, a separate 8609 will be issued for each year's allocation. If rehabilitation and acquisition credits are issued on the same building, the "acquisition" and "rehabilitation" will receive separate 8609 forms.

Part I of the form 8609 will be completed by Minnesota Housing and sent to the owner after the project is placed in service and all documentation required by Minnesota Housing is reviewed and approved. Minnesota Housing files the original with the IRS for their records to compare with the taxpayer's return.

The owner completes Part II and files the Form(s) 8609 with the IRS at the Philadelphia Service Center, with an original signature in Part II, for the first Taxable Year in which the credit was claimed. See the instructions on IRS Form 8609 and 8609-A for details.

Owners should consult with their legal and/or tax advisors for advice on completing and filing the IRS tax forms. Minnesota Housing cannot give legal or tax advice on the filing or completion of tax forms since that area is out of its jurisdiction.

Part I of form 8609 is to be prepared **by Minnesota Housing only**. If Minnesota Housing becomes aware that an owner or its agent has filed a self-prepared 8609 with the Internal Revenue Service, Minnesota Housing reserves the right to determine that all parties involved will not be eligible for future participation in Minnesota's HTC Program for a period of ten (10) years.

B. Low Income Housing Credit (IRS Form 8586)

One Low Income Housing Credit (IRS Form 8586) form must be completed to claim credits for the first Taxable Year in which credit is taken and every year thereafter in the Compliance Period.

If the owner is claiming credits on IRS Form 8586 from a flow-through entity, (such as a partnership, S corporation, estate or trust) the individual investor must complete only Part I of Form 8586.

C. Declaration of Land Use Restrictive Covenants

The building owner must record an approved Minnesota Housing Declaration of Land Use Restrictive Covenants (extended use commitment) which must be in effect on or before the end of the first taxable year credits are claimed 42(h)(6)(A). Failure to timely and properly record this instrument is an event of noncompliance and will be reported to the Internal Revenue Service.

D. Recapture of Low Income Housing Credit Form 8611

IRS Form 8611 is used by taxpayers who must recapture tax credits claimed in previous years. A copy of Form 8611 must be filed with the IRS upon completion by the owner.

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Chapter 3 – Record Keeping and Record Retention Requirements

A. Record Keeping

Under the record keeping provision of Reg. 1.42-5, the owner must keep records for each building in the project for each year in the compliance period showing:

- The total number of residential rental units in the building (including the number of bedrooms and the size in square feet of each residential rental unit);
- The number of occupants in each HTC unit and the household's student status.
- The number and percentage of residential rental units in the building that are HTC units, offices, and management units;
- The rent charged on each residential rental unit in the building (including utility allowance) as well as any additional charges to tenants. Documentation must include tenant ledgers, leases, and utility allowances as required by Internal Revenue Service;
- The HTC unit vacancies in the building, marketing information, and information which shows when and to whom each of the next available units were rented;
- The annual income certification of each HTC household;
- Documentation to support each HTC Tenant's Income Certification including application/recertification questionnaire, and verifications. Anticipated income of all adult persons expecting to occupy the unit must be verified and included on a Tenant Income Certification prior to occupancy and recertified annually for continued eligibility. Income verifications (written, third party verification is always preferred) are sent directly to and returned by the source to management, not through the applicant.
- The character and use of the nonresidential portion of the building included in the building's eligible basis under Section 42(d) (e.g. tenant facilities that are available on a comparable basis to all tenants and for which no separate fee is charged for use of the facilities, or facilities reasonably required by the project);
- The eligible basis and qualified basis of the building at the end of the first year of the credit period.
- Records demonstrating that any state established set-aside elected by the owner has been complied with for each year of the compliance period.

B. Record Retention

The owner must retain the records described above for at least six years after the due date (with extensions) for filing the federal income tax return for that year. The records for the first year of the credit period, however, must be retained for at least six years beyond the due date (with extensions) for filing the federal income tax return for the last year of the compliance period of the building.

See Revenue Ruling 2004-82, published August 30, 2004, which clarifies that owners may comply with the record retention provisions under IRC Section 1.42-5(b) by using an electronic storage system instead of maintaining hardcopy (paper) books and records, provided that the electronic storage system satisfies the requirements of Revenue Procedure 97-22.

Owners must maintain applicant and tenant information in a way to ensure confidentiality. Any applicant or tenant affected by negligent disclosure or improper use of information may bring civil action for damages and seek other relief, as appropriate. Owners must dispose of records in a manner that will prevent any unauthorized access to personal information, e.g., burn, pulverize, shred, etc.

Chapter 4 – Monitoring – Certification and Review

A. Annual Certification

The owner must certify to Minnesota Housing, under penalty of perjury, at least annually for each year of the 15 year compliance period on MHFA Form HTC 12 Owner's Certification of Continuing Program Compliance, or other forms designated, that the project is in compliance with the requirements of Reg. 1.42-5 paragraph (c)(1), certification and review provisions. The owner's certification requires the owner to certify that the project meets the following for the preceding 12-month period:

1. The project met the minimum requirements of the 20/50 test under Section 42(g)(1)(A) of the Code; the 40/60 test under Section 42(g)(1)(B) of the Code; or the 15/40 test for "deep rent-skewed" projects under Section 42(g)(4) and 142(d)(4)(B) of the Code, whichever applies to the project.

2. There has been no change in the applicable fraction (as defined in Section 42(c)(1)(B) of the Code) for any building in the project.

3. <u>At initial occupancy the owner has received a Tenant Income Certification with supporting documentation and an Annual Student Certification from each low-income household. At annual recertification owner has received an Annual Student Certification and, where applicable, a Tenant Income Certification with supporting documentation from each low-income household.</u>

4. Each low-income unit in the project has been rent-restricted under Section 42(g)(2) of the Code.

5. No tenants in low-income units were evicted or had their tenancies terminated other than for good cause and no tenants had an increase in the gross rent with respect to a low-income unit not otherwise permitted under Section 42.

6. All units in the project are and have been for use by the general public and used on a non-transient basis (except for transitional housing for the homeless provided under Section 42 (i)(3)(B)(iii) of the Code).

7. No finding of discrimination under the Fair Housing Act, 42 U.S.C 3601-3619, has occurred for this project. A finding of discrimination includes an adverse final decision by the Secretary of Housing and Urban Development (HUD), 24 CFR 180.680, an adverse final decision by a substantially equivalent state or local fair housing agency, 42 U.S.C 3616a(a)(1), or an adverse judgment from a federal court.

8. Each building in the project is and has been suitable for occupancy, taking into account local health, safety, and building codes (or other habitability

standards), and the state or local government unit responsible for making building code inspections did not issue a report of a violation for any building or low income unit in the project.

9. There has been no change in the eligible basis (as defined in Section 42(d) of the Code) of any building in the project since last certification submission.

10. All tenant facilities included in the eligible basis under Section 42(d) of the Code of any building in the project, such as swimming pools, other recreational facilities, parking areas, washer/dryer hookups, and appliances were provided on a comparable basis without charge to all tenants in the buildings.

11. If a low-income unit in the project has been vacant during the year, reasonable attempts were or are being made to rent that unit or the next available unit of comparable or smaller size to tenants having a qualifying income before any units were or will be rented to tenants not having a qualifying income.

12. If the income of tenants of a low-income unit in the project increased above the limit allowed in Section 42(g)(2)(D)(ii) of the Code, the next available unit of comparable or smaller size was or will be rented to residents having a qualifying income.

13. An extended low-income housing commitment as described in section 42(h)(6) was in effect, including the requirement under section 42(h)(6)(B)(iv) that an owner cannot refuse to lease a unit in the project to an applicant because the applicant holds a voucher or certificate of eligibility under section 8 of the United States Housing Act of 1937, 42 U.S.C. 1437f. Owner has not refused to lease a unit to an applicant based solely on their status as a holder of a section 8 voucher and the project otherwise meets the provisions, including any special provisions, as outlined in the extended low-income housing commitment (not applicable to buildings with tax credits from years 1987-1989).

14. The owner received its credit allocation from the portion of the state ceiling set-aside for a project involving "qualified non-profit organizations" under Section 42(h)(5) of the code and its non-profit entity materially participated in the operation of the development within the meaning of Section 469(h) of the Code.

15. There has been no change in the ownership or management of the project.

B. Annual Submission Requirements

The owner's certification must be submitted to Minnesota Housing by February 15, or the next business day, of each calendar year. The Owner's Certification of Continuing Program Compliance (form HTC 12) must be submitted to Minnesota Housing by the owner of any and all projects, including those which have received a carryover allocation of tax credits or a preliminary

determination letter in the case of tax exempt bond allocations (even if the project has not yet been placed in service).

If the property is not yet in the first year of the credit period, submit:

- Owner's Certification of Continuing Program Compliance with appropriate designation of not yet placed in service, or placed in service but elect to begin credit period in the year following placed in service. Sign and date.

For the first year of the credit period and later, submit:

- A fully completed, signed and dated Owner's Certification of Continuing Program Compliance (HTC 12). Only a person authorized to sign for the respective property's ownership entity may sign the HTC 12. Minnesota Housing may ask for signatory authorization if not on file. Note that the Owner's Certification of Continuing Program Compliance provides that all months within each twelve-month period are subject to certification and all certification items must be checked;
- Tax Credit Summary Report (HTC 13) and accompanying Applicable Fraction Summary. The HTC 13 is to be submitted via Minnesota Housing's Secure Upload Tool or, if an owner is not using Minnesota Housing's Electronic Reporting Program (ERP), in hard copy. It is not necessary to submit both an ERP and a hard copy;
- Compliance monitoring fees of $25 per unit except those properties covered under the Memorandum of Understanding by and between Rural Housing Service and Minnesota Housing; the fee is $15.00 for each unit in the project;
- Characteristics of Tenant Households report, which provides demographic data on households occupying units in the development on 12/31 of the report year. This may also be submitted using the ERP or Characteristics of Tenant Households Report (CTH Report) in Microsoft Excel;
- **IRS forms 8609(s) for each building, with Part II completed as filed with IRS;
- **Completed 8609-A for each building;
- **8586, as filed with the IRS;

Tax Credit Summary Reports (HTC 13) must be fully completed and must document gross income at move-in and certification dates, student status, rent amounts and utility allowance information, gross income at annual recertification and recertification dates, where applicable, move-out and transfer information, etc. At recertification, if tenant income exceeds 140% of the maximum income limit, the owner must comply with the available unit rule (Sec. 42 (g)(2)(D)).

Minnesota Housing prefers that Tax Credit Summary Reports be submitted electronically, and has provided an Excel file to prepare the report. Other software products may be used as long as they are able to produce forms identical to those approved by Minnesota Housing and data can be transferred into this Excel format.

The Characteristics of Tenant Households must be submitted <u>each year</u>. For information on how the form is to be completed see the instructions that

accompany the form. Minnesota Housing must supply this information to the Department of Housing and Urban Development (HUD) annually.

****IRS forms 8609, 8609 Schedules A, and 8586 for the first year of the credit period.** These completed forms must be submitted to Minnesota Housing at the time they are filed with the IRS.

Failure to timely submit legible and thoroughly complete HTC forms 12 and 13, Characteristics of Tenant Households Report and IRS Forms 8609, 8609-A, and Form 8586 when they are due will be considered noncompliance.

C. Compliance Monitoring Review Requirements

General: Under the Minnesota Housing review process, owners must maintain ongoing tenant records on Minnesota Housing-approved forms for each unit in the project. The forms provide a historical record of tenant compliance for each unit.

Minnesota Housing must inspect each project at least once every three years. The Agency shall inspect the tenant income certification(s), the documentation to support the certification(s), and the rent record for each tenant in at least 20% of the low-income units in those projects. In addition, Minnesota Housing will also conduct a physical inspection of 20% of the low-income units in the selected developments. The first inspection for new projects will occur no later than the end of the second year of the credit period.

The HTC units to be inspected or reviewed must be chosen in a manner that will not give owners of HTC projects advance notice that their records will or will not be inspected. Minnesota Housing may give an owner reasonable notice that an inspection will occur so that the owner may assemble records. Noncompliance that is identified and corrected by the owner *prior to notification* of an upcoming compliance review or inspection need not be reported to IRS. IRS considers the date of the notification letter a “bright line” date.

Rural Housing Service: Minnesota Housing and the U.S. Department of Agriculture, Rural Housing Service (RHS) have entered into a Memorandum of Understanding effective November 1, 2000. The parties have agreed to share information pertaining to the Housing Tax Credit Program, including, but not limited to, results of file and physical inspections conducted by RHS. Minnesota Housing will not perform routine inspections on RHS properties, but will rely on the inspection results as noted by RHS staff. If noncompliance is noted, Minnesota Housing will issue a notice of noncompliance to the owner and require evidence of correction in the same manner as all other HTC developments.

Minnesota Housing reserves the right to conduct a review of **any** building after serving appropriate notice and to examine all records pertaining to rental of tax credit units. Minnesota Housing may perform a review at least through the end of the compliance period of the buildings in the project.

D. Procedure for Compliance Inspection

In the year a compliance inspection is due, Minnesota Housing will notify owner by mail and request that owner complete the Compliance Review Worksheet to identify other inspections that are due in the same year so that inspections can be coordinated if possible. Once the date and time of inspection has been agreed to, no earlier than 30 days in advance of the inspection, Minnesota Housing will issue a confirmation letter along with a list of units selected for review. The confirmation letter is considered Minnesota Housing's notification of an upcoming compliance review. Unless otherwise clarified, compliance violations that are uncorrected as of the date of the confirmation letter may be reported on form 8823. Other information, resident selection plans, house rules, tenant ledgers, and other information must be submitted to Minnesota Housing at the time of the tenant file review.

The compliance inspection includes, but is not limited to, a review of: (1) at least 20% of the low-income tenant files including a full inspection and calculation of income eligibility and student status, (2) the Tax Credit Summary Report, (3) utility allowance information and other documentation, and (4) an inspection of the general physical condition of the property including 20% of the low-income units.

Compliance Monitoring Regulations published January 14, 2000, require housing credit agencies to conduct physical inspections consistent with standards governed by the Department of Housing and Urban Development's Uniform Physical Conditions Standards. These standards require properties to be in "decent, safe and sanitary condition and in good repair" and require agencies to inspect the following five major areas:

1. **Site** – The site includes components such as fencing and retaining walls, grounds, lighting, mailboxes, signs (such as those identifying the development or areas of the development), parking lots/driveways, play areas and equipment, refuse disposal, roads, storm drainage and walkways. The site must be free of health and safety hazards and be in good repair.

2. **Building exterior** – Each building on the site must be structurally sound, secure, habitable, and in good repair. The building's exterior components such as doors, fire escapes, foundations, lighting, roofs, walls and windows, where applicable, must be free of health and safety hazards, operable, and in good repair.

3. **Building systems** – The building's systems include components such as domestic water, electrical system, elevators, emergency power, fire protection, HVAC, and sanitary system. Each building's systems must be free of health and safety hazards, functionally adequate, operable, and in good repair.

4. **Dwelling units** – (i) Each dwelling unit within a building must be structurally sound, habitable, and in good repair. All areas and aspects of the dwelling unit (for example the unit's bathroom, call-for-aid, ceiling, doors, electrical systems, floors, hot water heater, HVAC (where individual units are provided), kitchen, lighting, outlets/switches, patio/porch/balcony, smoke detectors, stairs, walls and windows) must be free of health and safety hazards, functionally adequate, operable, and in good repair. (ii) Where applicable, the dwelling unit must have hot and cold running water, including an adequate source of potable water. (iii) If the dwelling unit includes its own sanitary facility, it must be in proper operating condition, usable in privacy, and adequate for personal hygiene and the disposal of human waste. (iv) The dwelling unit must include at least one battery-operated or hard-wired smoke detector, in proper working condition, on each level of the unit.

5. **Common areas** – The common areas must be structurally sound, secure and functionally adequate for the purposes intended. The common areas include components such as basement/garage/carport, restrooms, closets, utility, mechanical, community rooms, day care, halls/corridors, stairs, kitchens, laundry rooms, office, porch, patio, balcony, and trash collection areas, if applicable. The common areas must be free of health and safety hazards, operable, and in good repair. All common area ceilings, doors, floors, HVAC, lighting, outlets/switches, smoke detectors, stairs, walls, and windows, to the extent applicable, must be free of health and safety hazards, operable, and in good repair.

   All areas and components of the housing must be free of health and safety hazards. These areas include, but are not limited to: air quality, electrical hazards, elevators, emergency/fire exits, flammable materials, garbage and debris, handrail hazards, infestation, and lead based paint. For example, the buildings must have fire exits that are not blocked and have handrails that are undamaged and have no other observable deficiencies. The housing must have no evidence of infestation by rats, mice, or other vermin, or of garbage and debris. The housing must have no evidence of electrical hazards, natural hazards, or fire hazards. The dwelling units and common areas must have proper ventilation and be free of mold, odor (e.g., propane, natural gas, methane gas), or other observable deficiencies. The housing must comply with all regulations and requirements related to the ownership of pets, and the evaluation and reduction of lead-based paint hazards and have available proper certifications of such.

   Notwithstanding the above inspection requirements, a low-income housing project under Section 42 must continue to satisfy local health, safety, and building codes. Minnesota Housing may rely on local code inspections rather than performing a separate physical inspection of the property. When selected for a compliance inspection, Minnesota Housing will determine whether there has been or will be a physical inspection that meets the local inspection requirements.

E. Compliance Forms

The following forms have been approved by the National Council of State Housing Agencies (NCSHA) as "recommended practices":

- Owner's Certification of Continuing Program Compliance, MHFA HTC 12
- Tenant Income Certification, MHFA HTC 14
- Student Status and Financial Aid Verification
- Under $5,000 Asset Certification, MHFA HTC 24
- Zero Income Certification
- Employment Verification

The forms with HTC and a number in the footer are required forms (i.e., HTC 12, HTC 13, etc.). **No other forms will be considered acceptable**. The other forms are strongly recommended. Each form has a date located in the lower right hand corner. **Please discard old forms and replace with those that have been newly revised.**

In addition, the following are required forms:

- Tax Credit Summary Report, MHFA HTC 13 (with Y1AF or Y2AF Applicable Fraction Summary)
- Minnesota Government Data Practices Act Disclosure Statement
- Utility Allowance Information, MHFA HTC 21
- Characteristics of Tenant Households Report
- Annual Student Certification, MHFA HTC 35

Each household file must have a fully executed Tenant Income Certification (HTC 14) with supporting documentation and an Annual Student Certification (HTC 35) for each year of occupancy and a Minnesota Data Practices Act Disclosure Statement signed by each household member 18 years of age or older. (See Section 6 - Income Determinations, for additional information).

Rural Housing Service: As part of the Memorandum of Understanding between USDA Rural Housing Service and Minnesota Housing, RHS will require signatures of all household members age 18 and over and information relating to student eligibility, as required by IRS Code, on tenant certifications. In return, Minnesota Housing will accept use of Form RD 1944-8, Tenant Certification in lieu of Minnesota Housing's Tax Credit Program Tenant Income Certification (HTC 14). The Minnesota Government Data Practices Act Disclosure Statement referred to above must continue to be on file.

F. Corrections to Documents

Sometimes it is necessary to make corrections or changes to documents. A document that has been altered, with correction fluid or "white-out" will not be accepted by Minnesota Housing. When a change is needed on a document for the HTC Program, the person making the correction must draw a line through the incorrect information, write or type the correct wording or number, and have all parties initial and date the change.

G. Annual Monitoring Fees

Minnesota Housing will charge annual fees to cover the costs of conducting compliance monitoring. The annual fee(s) must be submitted when the owner's certification is due.

Fees are charged on all units within each project. Minnesota Housing will charge an annual monitoring fee of $25 per unit, based on the total number of units, except for projects covered by the Memorandum of Understanding (MOU) between Minnesota Housing and the U.S Department of Agriculture, Rural Housing Service. The compliance monitoring fee will be $15 per unit per year for projects covered by the MOU. Minnesota Housing reserves the right to adjust fees due to changing circumstances.

H. Minnesota Housing Records Retention

Minnesota Housing will retain records of non-compliance or failure to certify for six years beyond the filing date of the respective Form 8823. In all other cases, Minnesota Housing will retain the certifications and records described in Reg. 1.42-5(c) for three years from the end of the calendar year the Agency receives the certifications and records.

I. Liability

Compliance with the requirements of Section 42 is the responsibility of the owner of the building for which the credit is allowable. Minnesota Housing's obligation to monitor for compliance with the requirements of Section 42 does not make the Agency liable for an owner's non-compliance (Reg. 1.42-5(g)).

Chapter 5 – Project Rental Requirements

A. Allowable Fees and Charges

Application fees may be charged to cover the actual cost of checking a prospective tenant's income, credit history, and landlord references. The fee is limited to recovery of the actual out-of-pocket costs. No amount may be charged in excess of the average expected out-of-pocket costs of checking tenant qualifications at the project. Customary fees, normally charged, such as damage deposits and pet deposits are permissible. However, an eligible tenant cannot be charged a fee for the work involved in completing the additional forms or documentation required, such as the Tenant Income Certification.

Please Note: If tenant facilities (e.g. parking, garages, swimming pools, etc.) were included in the eligible basis, they must be made available to all tenants on a comparable basis, and a separate fee must not be charged for their use.

Gross rents for the tax credit program are the rents paid by tenants (excluding federal or state rent assistance such as Section 8) plus an allowance for utility costs paid directly by tenants (except telephone and cable) and any other mandatory charges. Charges for non-optional services such as a washer and/or dryer hookup fee and built in/on storage sheds or lockers (paid month-to-month or in a single payment) must always be included within gross rent. The total gross rent cannot exceed the applicable Multifamily Tax Subsidy Project (MTSP) rent limits for the project. In addition, IRS has clarified that month-to-month lease fees and mandatory renter's insurance are considered rent. The fees are allowable, but the gross rent must include these amounts and must be below the applicable rent limit. When completing the Tenant Income Certification and Tax Credit Summary Report (HTC 13) include the amount in the column with tenant paid rent.

It is permissible to charge eligible tenants the first and last months' rent if the same is charged to other tenants.

Decorating fees or fees for preparing a unit for occupancy must not be charged; owners are responsible for physically maintaining units in a manner suitable for occupancy.

If after occupying a unit an eligible tenant cannot pay the rent or is otherwise in violation of the lease provisions, the owner has the same legal rights in dealing with the eligible tenant as with any other tenant. Note, however, that during the compliance period, extended use period and for three years after expiration of the Declaration of Land Use Restrictive Covenants, households in qualified tax credit units may not be evicted or tenancy terminated for other than good cause.

B. Section 8 Rents

Subsidy payments to an owner under various HUD Section 8 programs or any other comparable program are excluded and not considered in determining gross rent. The tenant's portion of the rent payment, plus the applicable utility allowance and any mandatory charges are considered in determining if the rent exceeds the gross rent maximum for the county. Sec. 42(0)(2)(B)(i). Similarly, when considering rent-to-income ratios, managers must compare income only to the tenant paid portion of the rent – not including the subsidy payment.

The portion of the rent paid by Section 8 tenants can exceed the tax credit rent ceiling as long as the owner receives a section 8 assistance payment on behalf of the resident. If no subsidy is provided, the tenant may not pay more than the maximum allowable tax credit rent.

With the passage of the Omnibus Budget Reconciliation Act of 1993, owners are prohibited from refusing to lease to a prospective tenant based solely on the fact that the applicant holds a Section 8 rental voucher or certificate.

C. Minimum Lease Requirement

All tenants occupying HTC units are required to be certified and to execute at least an initial six-month lease. (Exceptions for housing for the homeless and single room occupancy are listed below). The six-month requirement may include free rental periods of one month or less. Succeeding leases are not subject to a minimum lease period.

The lease must reflect the correct date of move-in, or the date the tenant takes possession of the unit.

At a minimum, the lease must include:

- the legal name of parties to the agreement and all other occupants
- a description of the unit to be rented
- the date the lease becomes effective
- the term of the lease
- the amount of rent
- the use of the premises
- the rights and obligations of the parties, including the obligation of the household to annually recertify its income
- the signatures of all household members 18 years of age or older and/or persons under the age of 18 who are the head of household, co-head or spouse
- a statement explaining that the development is participating in the Housing Tax Credit Program, and that tax credit units are under certain program regulations including income eligibility, student eligibility, and annual recertification of household income.

Single room occupancy (SRO) housing must have a minimum lease term of one month. Tenants in SRO housing may share bathrooms, cooking facilities, and dining areas.

Federal rules allow for month-to-month leases for the following types of SRO housing for homeless individuals:

1. SRO units in projects receiving McKinney Act and Section 8 Moderate Rehabilitation assistance;
2. SRO units intended as permanent housing and not receiving McKinney Act assistance;
3. SRO units intended as transitional housing that are operated by a governmental or nonprofit entity and providing certain supportive services.

D. Household Size

The number of household members is needed in order to determine the maximum allowable income.

1. **Minimum and Maximum Household Size:** While IRS regulations do not specifically address occupancy requirements, Minnesota Housing encourages maximum utilization of space. Therefore, it is Minnesota Housing 's recommendation that written occupancy policies be established which reflect maximum utilization (at least 1 person per bedroom is recommended as a minimum) and set maximum standards of no fewer than two persons per bedroom. In situations where there is more than one qualified applicant for a unit, Minnesota Housing recommends giving preference to the household that is most suitable to the unit size. Owners should comply with state and local laws, regulations and financing requirements (e.g., if Rural Housing Service, use RHS regulations).

2. **Factors that Affect Household Size.** When determining family size for income limits, the owner must include the following individuals who are not living in the unit:
   - Children temporarily absent due to placement in a foster home;
   - Children in joint custody arrangements who are present in the household 50% or more of the time (if disputed, determine which parent claimed the children as dependents for purposes of filing a federal income tax return);
   - Children who are away at school but who live with the family during school recesses;
   - Unborn children of pregnant women; when a pregnant woman is an applicant, the unborn child is included in the size of the household, and may be included for purposes of determining the maximum allowable income. The rental application should ask the following question: "Will there be any changes in household composition within the next 12 month period?" If an applicant answers that a child is expected, the manager should explain to the tenant that in order to count the child as an additional household member and use the corresponding income limit, a self-certification of pregnancy must be provided.
   - Children who are in the process of being adopted;
   - Temporarily absent family members who are still considered family members. For example, the owner may consider a family member who is working in another state on assignment to be temporarily absent.

Persons on active military duty are considered temporarily absent (except if the person is not the head, co-head or spouse or has no dependents living in the unit). If the person on active military duty is the head, co-head, or spouse, or if the spouse or dependents of the person on active military duty resides in the unit, that person's income must be counted in full;

- Family members in the hospital or rehabilitation facility for periods of limited or fixed duration. These persons are temporarily absent as defined above; and
- Persons permanently confined to a hospital or nursing home. The family decides if such persons are included when determining family size for income limits. If such persons are included, they must be listed on the Tenant Income Certification as "other adult family member". If the family chooses to include the permanently confined person as a member of the household, the owner must include income received by these persons in calculating family income.

When determining family size for establishing income eligibility, the owner must include all persons living in the unit except the following:

- A live-in aide/attendant is a person who resides with one or more elderly persons, near-elderly persons, or persons with disabilities, and who:
    - Is determined to be essential to the care and well-being of the person(s);
    - Is not obligated for the support of the person(s); and
    - Would not be living in the unit except to provide the necessary supportive services.

While a relative may be considered to be a live-in aide/attendant, they must meet the above requirements, especially the last. The live-in aide qualifies for occupancy only as long as the individual needing supportive services requires the aide's services and remains a tenant, and may not qualify for continued occupancy as a remaining family member. Managers must obtain verification of the need for a live-in care attendant and should not add the attendant to the lease.

- Foster adults or children should be included in the size of the household, but are not included for the purpose of determining the maximum allowable income.

*Deployment of Military Personnel to Active Duty

Owners are encouraged to accommodate the unique circumstances of households where a member is called to active duty in the Armed Forces. Specific actions that owner can take and remain in compliance include, but are not limited to:

1. Allow a guardian to move into the low-income unit on a temporary basis to provide care for any dependents the military person leaves in the unit. The guardian's income is not included in the household's income.
2. Allow a tenant living in a low-income unit to provide care for any dependents of persons called to active duty in the Armed Forces on a temporary basis as long as the head and/or co-head of the household continues to service in active duty. Income of

the dependent (e.g., SSI benefits, military benefits) is not included in the household's income.

3. Allow leases to remain in effect for a reasonable period of time without recertification (if required) depending on the length of deployment beyond that required by the Soldiers' and Sailors' Civil Relief Act of 1940, 50 U.S.C. §§501-591, even though the adult members of the military family are temporarily absent from the unit.

E. Utility Allowance

The Internal Revenue Service requires that utility allowances be set according to 26 C.F.R. 1.42-10 (April 24, 1994), effective May 2, 1994, and amended 7/29/2008. Please read these regulations carefully.

If a utility (other than telephone, cable television or internet) is paid directly by the tenant(s), and not by or through the owner of the building, the gross rent includes a utility allowance. If all utilities are paid by or through the owner the utility allowance is zero.

Utility allowances are applied individually to each building in the development. Therefore, depending on the development, an owner or manager could have buildings in the same development using different utility allowances.

Utility allowances must be reviewed and updated at least annually. Regulations require that new utility allowances be used to compute rents that are due 90 days after the effective date of the new allowances. For new buildings, owners are not required to review or implement new utility allowances until a building has achieved 90 percent occupancy for a period of 90 consecutive days or the end of the first year of the credit period, whichever is earlier.

Section 42 lists the different sources of utility allowances for tax credit developments. The following is a summary of the sources of utility allowances:

1. USDA Rural Housing Service (RHS) financed projects, or units with tenants receiving RHS assistance, must use the RHS utility allowance.
2. HUD regulated buildings must use the HUD utility allowance (project based HUD financing).
3. Any individual apartments occupied by residents who receive HUD assistance (Section 8 Existing, etc.), must use the HUD utility allowance from the Public Housing Authority (PHA) administering the assistance. As of May 2, 1994, the PHA utility allowance would only need to be used for the specific apartment the PHA resident occupied. Check to find out who administers the local Section 8 Existing Housing Program; it may be the city or county HRA/PHA.
4. For Section 42 buildings without RHS or HUD assistance, the following options may be used:
   a. A PHA utility allowance from the local housing authority administering section 8 vouchers for the area in which the property is located.
   b. A utility company estimate. Any interested party (including a low-income tenant, a building owner, or an agency) may request the utility company estimation of utility consumption in the building's geographic area. The estimate is obtained when the interested party receives, in writing, information from a local utility company providing the estimated

cost of that utility for a unit of similar size and construction for that geographic area. Costs incurred in obtaining the estimate are borne by the initiating party. The party that obtains the local utility company estimate must retain the original of the utility company estimate and must furnish a copy to the owner and the monitoring agency. The owner of the building must make copies available to all tenants in the building. In the case of deregulated utility services, the interested party is required to obtain an estimate only from one utility company even if multiple companies can provide the same utility service to a unit. However, the utility company must offer utility services to the building in order for that company's rates to be used. The estimate should include all component deregulated charges for providing the utility service.

c. An "Agency Estimate" based on actual utility usage data and rates for the building. See Sec. F, Owner's Average of Actual Consumption, Utility Allowance Procedures for instructions.
d. A HUD Utility Schedule Model.
   This model can be found on HUD's website at http://www.huduser.org/portal/resources/UtilityModel/hdd.html, or successor URL. Utility rates using the HUD utility model must be no older than the rates in place 60 days prior to the effective date of the utility allowance.
e. An Energy Consumption Model using an energy and water and sewage consumption and analysis model. The model must at a minimum take into account specific factors including, but not limited to, unit size, building orientation, design and materials, mechanical systems, appliances, and characteristics of the building location. The utility consumption estimates must be calculated by a mechanical engineer properly licensed in the State of Minnesota. The engineer and building owner must not be related within the meaning of IRC section 267(b) or 707(b), to which the engineer and building owner must certify. The owner and engineer must also certify that the model complies with the minimum requirements described above. Use of the energy consumption model is limited to a building's consumption data and local rates for the 12 month period ending no earlier than 60 days prior to the effective date of the utility allowance. In the case of new buildings with less than 12 months of consumption data, 12 months of data can be used for units of similar size and construction in the geographic area.

With the exception of HUD and RD-regulated properties, owners may combine any methodology for each utility service type (electric, water gas etc.) For example, if residents are responsible for electricity and water, an owner may use the appropriate PHA allowance to determine the water portion of the allowance and use the Owner's Average of Actual Consumption to determine the electric portion of the allowance. Be advised, however, that the effective date of the PHA allowance will likely be different than the Owner's Average of Actual Consumption resulting in adjustments to utility allowances and, potentially, rents multiple times during the year.

Failure to maintain or provide the Utility Allowance and supporting documentation annually is considered noncompliance; without proof of the amount of the allowance, there is no way to correctly compute the rent. In addition, an incorrect utility allowance calculation may result in noncompliance for rents that exceed the tax credit rent limits.

It is the owner's responsibility to contact the appropriate organization to request current utility allowance information. Minnesota Housing does not collect or maintain the various utility allowances. Unless otherwise provided for above, any costs incurred in obtaining a utility allowance are the responsibility of the owner.

Utility allowances and supporting documentation for options d and e must be submitted to Minnesota Housing at the beginning of the 90-day period before utility allowances can be used in determining the gross rent. This includes the Utility Allowance Information form HTC 21, which shows the totals for each building and unit size, all source documentation used to calculate the allowances, and the signed and dated Utility Allowance Certification HTC 21A. The effective date of the utility allowance shown on HTC 21 must be no later than 60 days after the rates used in the supporting documentation.

The owner must maintain and make the data upon which the utility allowance schedule is calculated available for inspection by the tenants. Records shall be made available at the resident manager's office during reasonable business hours or, if there is no resident manager, at the dwelling unit of the tenant at the convenience of both the apartment owner and tenant. The HUD Utility Schedule Model and energy consumption model must be made available to tenants no later than 90 days after the effective date.

Rents may need to be adjusted <u>more than once</u> in a year because the release of median income figures and utility estimates may occur at different times. Any increase in the utility allowance may cause gross rent to exceed the limit. For example, assume the rent charged on an apartment is at the maximum allowable rent; if the $50 utility allowance is increased to $60, the rent paid by the tenant must be lowered by $10 in order to remain below the rent limit. The new utility allowance must be implemented within 90 days of the effective date. Any change to resident paid rent must be in conformance with respective resident leases.

F. Owner's Average of Actual Consumption Utility Allowance Procedures

- Allowances must be based on the most recent 12-month period available (most recent month must be no older than 60 days from the effective date).
- Sampling must include a twelve month history of occupied low-income units. Units that were vacant for 2 weeks or more in any given month may not be included in the calculation.

- Sampling must be representative of all buildings of similar type (i.e., separate allowances are required for apartments vs. townhouses and/or single family dwellings) and of each bedroom size. Sampling must not contain a disproportionate number of small households vs. larger and to the extent possible must represent a variety of household sizes.
- Properties with less than 50 low-income units must use sampling by respective bedroom size as follows:
  - If 16 units or more, include 50% of the units. Sampling does not need to include more than 16 total units;
  - If less than 16 units but more than 6, include 75% of the units. Sampling does not need to include more than 8 total units;
  - If 6 or less units, include all of the units.

Example –less than 50 low-income units (always round up to a whole unit):

Bedroom Size	1BR	Sample	2BR	Sample	3 BR	Sample
# of units	20	10	15	8	6	6

- Properties with 50 or more low-income units must use sampling by respective bedroom size as follows:
  - If 30 units or more, include 50% of the units. Sampling does not need to include more than 30 total units;
  - If less than 30 units but more than 10, include 75% of the units. Sampling does not need to include more than 15 total units;
  - If 10 units or less, include all of the units.

Example – more than 50 low-income units (always round up to a whole unit):

Bedroom Size	1BR	Sample	2BR	Sample	3 BR	Sample
# of units	90	30	29	15	10	10

- The local utility provider may provide actual consumption records; however the print out must include the name of the provider. It may be necessary to obtain the resident's permission when requesting consumption records from local utility providers. A form of release can be found in the UA Sample Average of Actual Consumption excel file.
- Monthly utility billings received by tenants are acceptable. When copies of actual utility bills are used, the provider's name, unit number and resident's name must be visible on the billing.
- Monthly actual usage must be categorized by utility type (gas, oil, LP, electric, water, etc.), by unit size (1BR, 2BR, etc., regardless of differences in amenities such as additional bath or den, or square footage) and itemized by unit number in a spreadsheet which calculates an average utility allowance per unit size and includes all taxes and fees for which residents are responsible. This calculation must be consistent with the Minnesota Housing UA Sample Average of Actual Consumption excel file.
- Averages ending in cents must be rounded up to the next whole dollar.
- The average for each unit size and each type of utility must be entered onto form HTC 21, Utility Allowance Information. Separate forms HTC 21 must be completed for different buildings if they contain different unit types or

utility types (i.e., heat source in one building is gas and in another building is electric, and/or property contains both apartments and townhomes).

- The completed documentation must be submitted to Minnesota Housing for review and approval prior to implementation. Minnesota Housing will base its review and decision for approval or non-approval on a random sampling of information provided. Approval of the utility allowance does not constitute a guarantee that the utility allowance is absolutely correct. If at any time it is determined that a utility allowance has been understated and, therefore, some or all of the units are not rent restricted under section 42(g)(2), then Minnesota Housing must report the noncompliance to the IRS on form 8823.

Owners must collect actual consumption records and conduct the analysis using the methodology above and determine a new utility allowance annually. The Utility Allowance Certification, spreadsheet and HTC 21 must be updated no later than the anniversary of the effective date. Changes must be implemented no later than 90 days after the effective date. Any adjustment to rent must be in accordance with the respective lease agreement.

IRS Notice 2009-44 clarified that effective 7/29/2008, under IRC 1.42-10, utility costs paid by a tenant based on actual consumption in a sub-metered rent-restricted unit are treated as paid directly by the tenant. Sub-metering measures tenants' actual utility consumption, and tenants pay for the utilities they use. A sub-metering system typically includes a master meter, which is owned or controlled by the utility supplying the electricity, gas, or water, with overall utility consumption billed to the building owner. In a sub-metered system, building owners (or their agents) use unit-based meters to measure utility consumption and prepare a bill for each residential unit based on consumption. The building owners (or their agents) retain records of resident utility consumption, and tenants receive documentation of utility costs as specified in the lease.

(1) The utility rates charged to tenants in each sub-metered rent-restricted unit must be limited to the utility company rates incurred by the building owners (or their agents);
(2) If building owners (or their agents) charge tenants a reasonable fee for the administrative costs of sub-metering, then the fee will not be considered gross rent under § 42(g)(2). The fee must not exceed an aggregate amount per unit of 5 dollars per month unless State law provides otherwise; and
(3) If the costs for sewerage are based on the tenants' actual water consumption determined with a sub-metering system and the sewerage costs are on a combined water and sewerage bill, then the tenants' sewerage costs are treated as paid directly by the tenants for purposes of the utility allowances regulations.

Owners utilizing this methodology to calculate the utility allowance should be aware of the risk with any variation from section 1.42-10. This methodology to calculate allowances has not been approved by the IRS.

Note: Pursuant to Treas. Reg. 1.42-10, units occupied by households with a Section 8 Housing Choice Voucher or Minnesota Housing rental assistance must use the utility allowance required by the applicable rental assistance program.

G. Physical Requirements of Qualified Units, Suitable for Occupancy

Qualified Units rented to, or reserved for, eligible tenants:

- Must have substantially the same equipment and amenities (excluding luxury amenities such as a fireplace) as other units in the Project;
- Must be substantially the same size as other units in the Project; and
- Cannot be geographically segregated from other units in the Project.
- HTC units must be suitable for occupancy under Uniform Physical Conditions Standards (UPCS) and local health, safety and building codes. Units that are not suitable for occupancy, including previously qualified low-income units being rehabilitated in the first year of the credit period, are considered "out of compliance". The noncompliance is corrected when the unit is again suitable for occupancy, and the unit's character will be determined based on the household that occupied the unit immediately preceding the rehabilitation.

The UPCS do not supersede or preempt local health, safety and building codes. A low–income housing project under Section 42 must also satisfy the local standards.

Units intended for eligible tenants must be comparable in size, location, and quality to those rented to other tenants. In the event that units rented to non-qualifying households are above the average quality standards of the units rented to HTC households, then the basis in the project which is used to determine the amount of tax credits must be reduced by the portion which is attributable to the excess costs of the above-standard units. This reduction in eligible basis need not occur if an election is made to exclude such excess costs pursuant to Section 42(d)(3) of the Code.

H. Discrimination Prohibited in Project and General Public Use

Housing tax credit properties are subject to Title VIII of the Civil Rights Act of 1968, also known as the Fair Housing Act. The Fair Housing Act prohibits discrimination in the sale, rental and financing of dwellings based on race, color, religion, sex, national origin, familial status, and disability. See 42 U.S.C. sections 3601 through 3619. Minnesota law additionally prohibits discrimination based on marital status, disability, public assistance status, family status, creed and sexual orientation.

The Fair Housing Act also mandates specific design and construction requirements for multifamily housing built for first occupancy after March 13, 1991, in order to provide accessible housing for individuals with disabilities. The failure of housing tax credit properties to comply with the requirements of the Fair Housing Act will result in the denial of the housing tax credit on a per unit basis.

The Department of Housing and Urban Development (HUD) enforces the Fair Housing Act. Minnesota Housing will refer complainants to HUD for follow-up and/or investigation. Any finding of discrimination, adverse final decision by HUD, adverse final decision by a substantially equivalent state or local fair

housing agency, or an adverse judgment from a federal court is a violation that Minnesota Housing must report to the Internal Revenue Service.

Anyone with questions regarding the accessibility requirements can obtain the Fair Housing Act Design Manual from HUD by calling (800) 343-3442.

IRS also requires HTC properties be otherwise available to the general public. Under Treas. Reg. 1.42-9(b) if a residential unit is provided only for a member of a social organization or provided by an employer for its employees, the unit is not for use by the general public and is not eligible for credit under Section 42. Residential rental units either designated for a single occupational group, or through a preference for an occupational group, also violate the general public use requirements.

Note that the General Public Use Rule was clarified on July 30, 2008, to allow occupancy restrictions or preferences that favor tenants 1) with special needs, 2) who are members of a specified group under a federal or state program or policy that supports housing for such specified group, or 3) who are involved in artistic or literary activities.

I. Vacant Units

If a low-income unit in a property becomes vacant, reasonable attempts must be made to rent that unit or the next available unit of comparable or smaller size to a qualifying household before any units can be rented to non-qualified households. The owner or manager must be able to document reasonable attempts to rent the vacant units to eligible tenants.

Only units that have been previously occupied by an eligible household and <u>are suitable for occupancy</u> may be included as a qualifying low-income unit for compliance purposes. If a unit has never been occupied by an eligible household or has been vacated by a market rate household, that unit is not counted as a qualifying low-income unit.

The Vacant Unit Rule is the subject of Revenue Ruling 2004-82, Answering 12 Questions About Low-Income Housing Credit Under I.R.C. Section 42 (see questions #8, #9, and #10), published August 30, 2004. The Revenue Ruling clarifies that an owner may not move a household from building to building to qualify more than one unit in a property (question #8); that “reasonable attempts” are customary methods of advertising apartment vacancies in the area of the property for identifying prospective tenants and may include, but are not limited to: displaying a banner and for-rent signs at the entrance to the property, placing classified advertisements in local newspapers, and contacting prospective low-income tenants on a waiting list for the property and on a Section 8 and public housing waiting list with the local public housing authority (question #9); and that a unit is not an available vacant unit if the unit is no longer available for rent due to contractual arrangements that are binding under local law, such as a reservation entered into between the owner and a prospective tenant (question #10).

J. Other Stipulations

An owner or a person related to the owner may reside in a building if it contains five or more units. If a building contains four or fewer units, an owner, or a person related to the owner, occupying a unit in the building would cause the building to be in non-compliance, *unless* the building is acquired and rehabilitated pursuant to a development plan sponsored by the state or local government or qualified non-profit organization.

K. Student Eligibility

Under Section 42 Regulations, most households where all of the members are full-time students are not eligible and units occupied by these households may not be counted as HTC units. IRS Code Section 151(c)(4) defines 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 described in IRC Sec 170(b)(1)(A)(ii). Treas. Reg. Sec. 1.51-3(b) further provides that the five calendar months need not be consecutive.

The determination of student status as full or part-time should be based on the criteria used by the educational institution the student is attending.

An educational organization, as defined by IRC Sec. 170(b)(1)(A)(ii) is one that normally maintains a regular faculty and curriculum, and normally has an enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. The term "educational organization" includes elementary schools, junior and senior high schools, colleges, universities, and technical, trade and mechanical schools. It does not include on-the-job-training courses.

There are five exceptions to the limitation on households where all members are full-time students. Full-time student households that are income eligible and satisfy one or more of the following conditions are considered eligible:

1. Students are married and entitled to file a joint tax return;
2. The household consists of a single-parent with child(ren) and the parent is not a dependent of someone else, and the child(ren) is/are not dependent(s) of someone other than a parent;
3. At least one member of the household receives assistance under Title IV of the Social Security Act (formerly Aid to Families with Dependent Children (AFDC), now known as Temporary Assistance for Needy Families (TANF), or in Minnesota, the Minnesota Family Investment Program (MFIP)); or
4. At least one member of the household participates in a program receiving assistance under the Job Training Partnership Act (JTPA) or other similar federal, state, or local laws**.
5. At least one member of the household was previously in foster care***.

**The JTPA program was repealed in 1998, and replaced with the Workforce Investment Act (WIA). WIA, and JTPA when it existed, funds programs such as adult literacy, English as a second language, General Education Diploma (GED) courses, vocational services for the blind, employment and training programs for

Native Americans and migrant and seasonal farmworkers, job corps, veterans employment programs, summer youth employment and training, employment and training for dislocated workers and displaced homemakers, etc. Students in those programs are eligible for the JTPA exemption provided the school or community education dept., verifies that the applicant/resident is a participant in a program similar to those funded under JTPA or WIA. For more information about JTPA and WIA, visit:
http://en.wikipedia.org/wiki/Job_Training_Partnership_Act,
http://www.ed.gov/policy/adulted/leg/legis.html, and
http://www.deed.state.mn.us/youth/wiayouth.htm

***"Previously" means within five (5) years of the effective date of the initial income certification. "Foster care" means substitute care for children placed away from parents or guardians and for whom the state agency has placement and care responsibility. This includes, but is not limited to, placement in foster family homes, foster homes of relatives, group homes, emergency shelters, residential facilities, child care institutions, and pre-adoptive homes. A child is in foster care in accordance with this definition regardless of whether the foster care facility is licensed and payments are made by the state or local agency for the care of the child, whether adoption subsidy payments are being made prior to the finalization of an adoption, or whether there is a Federal matching of any payments that are made.

In order to properly document student eligibility, all households must complete an Annual Student Certification (form HTC 35) as part of the initial certification and annually thereafter. Properties that are 100% tax credit qualified and not required to recertify income are **not** exempt from this requirement. Note this is a required form.

Verification also must be obtained, when applicable, to support the full or part-time student status (use form HTC 15, Student Status and Financial Aid Verification (see section 6 for income information regarding student financial aid)) and the applicable exemptions(s) (i.e., tax return, marriage certificate, verification of participation in JTPA or similar program, verification of MFIP income, or verification from the state agency of previous participation in foster care).

Part-time students are not "students" for this section and their eligibility is not subject to special restrictions. However, verification of part time status is required for households comprised entirely of students that do not meet one of the exemptions.

L. Loss of Eligibility Upon Becoming a Full-Time Student

If a previously qualified HTC household becomes a full-time student household, the household **must** meet at least one of the above exemptions and be able to prove such status in order for the unit to remain in compliance. Under current legal interpretations of federal HTC regulations and requirements, the "available unit rule" that applies to HTC units with households that are no longer income eligible does not apply to student households that qualify under one of the exceptions above and later ceases to qualify. Unlike changes in income, a unit

occupied by a full-time student household that does not meet or no longer meets one of the above exceptions ceases to count as a tax credit unit immediately.

M. Unit Transfers

IRS considers each building in a property to be a separate project unless owner elects to treat certain buildings as part of a multiple building project. Owners make the election for multiple building projects on Part II, line 8b of IRS form 8609. Until Minnesota Housing becomes aware of an owner's election Minnesota Housing will treat the property as if all buildings are separate projects.

According to IRS, there is no such thing as a "transfer" between buildings that are **not part of the same multiple-building project**. If a household moves to another project within the same property, it must be reported as a move-out for the vacated unit. In order to treat the newly occupied unit as a qualified tax credit unit the household must be certified and meet initial eligibility requirements. The newly occupied unit must be reported as a new move-in. Managers of properties containing buildings treated as separate projects must obtain copies of the owner's filed 8609's and use caution when determining if a transfer or move-out/move-in applies.

Transfer within Same Building - When a current household moves to a different unit within the same building, the newly occupied unit adopts the status of the vacated unit. Thus, if a current household, whose income exceeds the applicable income limitation moves from an over-income unit to a vacant unit in the same building, the newly occupied unit is treated as an over-income unit. The vacated unit assumes the status the newly occupied unit had immediately before it was occupied by the current resident.

Transfer to Different Building/Same Project - When a household whose income is no greater than 140% of the income limit moves to a low income unit in a different building within the same project during any year of the 15-year compliance period, the vacated unit assumes the status the newly occupied unit had immediately before it was occupied by the current resident. If a household whose income exceeds 140% of the applicable income limit wishes to move to a different building in the same project, the newly occupied unit will be treated as a non-qualifying unit. Mixed income properties can rely on the most recent income certification. Properties that are exempt from income recertification requirements may allow transfers between buildings in the same project even though the household's current income is not known.

Example - Transfer to different building/ same project: ABC Acres consists of building A and building B. Owner has elected to treat buildings A and B as part of a multiple-building project. If a household moves from building A to building B it is a unit transfer.

Example - Move-out/Move-in to different building/different project: XYZ Apts. consists of building 1 and building 2. Owner has *not* elected to treat buildings 1 and 2 as part of a multiple-building project. Even though the two buildings are both part of XYZ Apts., and are located next door to each other, if a household

moves from building 1 to building 2 it is reported as a move-out for building 1 and a new move-in requiring a new initial certification for building 2.

Minnesota Housing has provided a form entitled “Documentation of Unit Transfer” to assist in documenting when a unit transfer occurs and the status of the units involved.

Chapter 6 – Income Determinations

Potential tenants for rent-restricted units should be advised early in the application process of the maximum income limits that apply to these units. Management should explain to potential tenants that the anticipated income of all persons 18 years of age or older and unearned income of minor children expecting to occupy the unit must be included, verified, and certified on a Tenant Income Certification.

This section of the Manual explains the procedures for determination of income. According to the Compliance Monitoring Regulations contained in Section 1.42-5 for the HTC Program, "Tenant income is calculated in a manner consistent with the determination of annual income under section 8 of the United States Housing Act of 1937 ("Section 8"), not in accordance with the determination of gross income for federal income tax liability."

Owners and managers should use current circumstances to project income, unless verification forms or other verifiable documentation indicate than an imminent change will occur. For guidance in this section and in determination of tenant income, the HUD Handbook 4350.3, Occupancy Requirements of Subsidized Multifamily Housing Programs, is used and is recommended as a reference guide. The HUD Handbook 4350.3 and HUD notices can be obtained by calling 1-800-767-7468 or by visiting HUD's web site at http://www.hud.gov/offices/adm/hudclips/handbooks/hsgh/4350.3/index.cfm.

To determine if a household meets the income test, look at the sources of income as stated in 24 CFR 813.106 which is the test for HUD Section 8 program (IRS Notice 88-80). If the amounts from these sources when aggregated are equal to or less than the applicable income limit for the county and household size, then the household is an income-qualified household. -

Please keep in mind that rental agents sometimes attempt to establish only that the applicant has sufficient income to support monthly rent payments. However, tax credit projects are both rent restricted and income restricted. Therefore, if a rental agent intends to include the applicant as an eligible tenant**, income from all required sources must be verified and included in the income calculation.**

A. Income Certification/Recertification

It is the owner's responsibility to select and rent to qualified tenants. Minnesota Housing will not qualify or approve eligible tenants. The Tenant Income Certification is to be completed, signed and dated by the owner or manager and signed and dated by all adult household members (adults include persons under the age of 18 who are treated as adults because they are the head, spouse or co-head of household).

1. Initial Eligibility Determination

Initially, tenant eligibility is determined at the time of move-in certification. Before a household takes occupancy, owners or managers must determine that the household will cause the unit to be a qualifying HTC unit.

Since the HTC Program uses special definitions for income and households, standard property management application forms may not collect sufficient information to determine tenant eligibility. Owners and managers need to make sure their applications collect all the necessary information. The information furnished on the application should be used as a tool to determine all sources of income, including total assets and income from assets.

An application, fully completed by the applicant in their own handwriting, unless assistance is requested or required, is critical to an accurate determination of tenant eligibility. The following items need to be included in the application:

- The full name and birth date of each person that will occupy the unit (legal name should be given just as it will appear on the lease and tenant income certification).
- The student status of each applicant.
- All sources and amounts of current and anticipated annual income expected to be received during the twelve-month certification period (this should include total assets and asset income).
- The name of any person not listed on the application expected to move into the unit during the next 12 months.
- The signature of all applicants age 18 and older, and the date the application was completed. It may be necessary to explain to the applicant that all information provided is considered sensitive and will be handled accordingly.

It is correct to first have potential residents disclose their income and assets, family composition, etc., on a Household Questionnaire and complete the top portion of relevant verification forms for release of information. In addition, the Annual Student Certification (HTC 35) must be completed at the time of application. Third party verification should then take place (note that verifications are valid only if they are no older than 120 days from the effective date of the certification—the application must also be no older than 120 days). Any incomplete, inconsistent or missing information on the verifications must be followed up with the verification source and a notation made to the resident file. A Phone Verification/Clarification Record can be used for this purpose. Finally, management should calculate income and income from assets based on information provided on the verification forms, and complete the Tenant Income Certification (TIC). This process must take place prior to the effective date of the Initial Certification (move-in date). The TIC should be signed no earlier than 5 days before the move-in date, but must be signed no later than the move-in date. The TIC should be effective as of the date

of move-in. An Initial Certification that is done after the move-in date is considered late and would cause a noncompliance event.

If a tenant is unable to sign the forms on time due to extenuating circumstances, the owner must document the reasons for the delay in the tenant file and indicate how and when the tenant will provide the proper signature.

Rural Housing Service projects must use the Section 8 method of calculating income based on "annual income" not the RHS method of "adjusted annual income" for HTC qualified tenants.

2. Special instructions for newly placed in service properties with existing residents

Acquisition/Rehab. For households occupying a unit at the time of acquisition, an initial TIC may be completed up to 120 days after the date of acquisition using the income limits in effect on the day of acquisition. The effective date and move-in date on the TIC is the acquisition placed in service date. If a TIC is completed more than 120 days after the acquisition, the effective date will be the date the last adult member of the household signs the certification. Note that all verifications must be no older than 120 days from the effective date and all verifications must be complete prior to the effective date.

For rehab-only properties, the initial certification may be completed any time on or after the rehab placed in service date. The move-in date on the TIC must be no earlier than the rehab placed in service date. The effective date may be any date the owner chooses on or after the placed in service date (note that verifications must be no older than 120 days from the effective date and all verifications must be complete prior to the effective date).

For the tax credit initial certification of project-based Section 8 or other HUD or Rural Development subsidized units, Minnesota Housing will accept an annual certification (but not an interim recert) effective within 120 days of the placed in service date (note that except for Rural Development properties, a Tenant Income Certification, HTC 14, must also be completed and signed).

It is important to note that even if a unit is occupied by a household that appears to be qualified, until the Tenant Income Certification is fully and properly completed and signed, the unit is treated as non-qualifying and tax credits are not available.

Properties with an existing allocation of housing tax credits that receive an additional allocation: Households determined to be income-qualified for purposes of the IRC §42 credit during the 15-year compliance period are concurrently income-qualified households for purposes of the extended use period as long as all §42 requirements have been met. As a result, any household determined to be income qualified at the time of

move-in for purpose of the extended use agreement is a qualified low-income household for any subsequent allocation of IRC §42 credit. If the new allocation is for rehabilitation only, vacant units will continue to be treated as low-income units subject to the vacant unit rule. If the new allocation is for acquisition/rehabilitation, vacant units lose their status as low-income units until they are occupied by qualified households that are properly certified.

3. Annual Recertification

Mixed Income Projects: Owners of mixed income projects are required to recertify annually as to the gross annual income of HTC households. Income recertification should be performed in accordance with the verification requirements for an initial certification.

The recertification process should begin 120 days prior to the anniversary date of the previous certification. The residents must complete a recertification application/questionnaire (see the Household Questionnaire provided by Minnesota Housing) to disclose income, assets, family composition and student status and also complete the top portion of relevant verification forms for release of information. In addition, the Annual Student Certification, form HTC 35, must be completed at the time of recertification. Third party verification should then take place. Any incomplete, inconsistent or missing information on the verifications must be followed up with the verification source and a notation made to the resident file. Finally, calculate income and income from assets based on information provided on the verification forms, and complete a Tenant Income Certification (TIC). The TIC is to be signed after all verifications are received and management has completed the form, but it must be effective on or before the anniversary date of the previous certification. It is acceptable to do a recertification before the anniversary date (to conform to the annual recertification date for a Section 8 household, for example). Recertifications that are done after the anniversary date cause a noncompliance event. However, if an owner sends timely notice informing a tenant that annual recertification is due, but the household vacates the unit, the unit will not be considered out of compliance. Owners must document attempts to timely obtain the recertification and the date the tenant actually moves out of the unit.

100% Housing Tax Credit Projects*: Effective 1/1/2009, annual income recertifications are not required for 100% low-income projects. A project is 100% low-income when the allocation was based on all units in the project and all units (common space units are not part of the equation) are in compliance. It is absolutely essential that each initial certification in a 100% low-income project be done very carefully and thoroughly. If a tenant income certification has insufficient documentation of gross annual household income or it is determined for any reason that one or more households do not qualify, the owner must resume conducting annual recertifications until 100% of the units are back in compliance.

***IMPORTANT:** IRS considers buildings to be separate projects unless owner elects to treat certain buildings as a multiple-building project. Owners make the election for multiple building projects on Part II, line 8b of IRS form 8609. Until Minnesota Housing becomes aware of an owner's election Minnesota Housing will treat the property as if all buildings are separate projects. Managers of properties containing some 100% buildings and some mixed-income buildings must obtain copies of the filed 8609's and use caution when determining if 100% buildings are exempt from recertification. If the 100% buildings are part of a multiple-building project that includes mixed income buildings the 100% buildings do not qualify for the exemption. If the 100% buildings are treated as a separate project or are part of a multiple-building project that contains only 100% HTC buildings, then they do qualify for the exemption.

Example 1- Recert exemption does not apply: A property consists of building A (100% HTC) and Building B (mixed income). Owner has elected to treat buildings A and B as part of a multiple-building project. Building A is not exempt from recertification because the project is not 100% HTC.

Example 2 – Recert exemption applies but only to certain buildings: A property consists of building A (100% HTC) and Building B (mixed income). Owner has *not* elected to treat buildings A and B as part of a multiple-building project. Building A is exempt from recertification because it is a 100% project. Because building B is mixed income, annual income recertifications must be completed for building B.

Example 3 – Recert exemption applies but only to certain buildings: A property consists of building A (100% HTC), building B (mixed income), building C (100% HTC) and Building D (mixed income). Owner has elected to treat buildings A and B as part of a multiple-building project. Owner has elected to treat buildings C and D as separate projects. Building A is not exempt from recertification because the project is not 100%. Building C is exempt from recertification because it is a separate 100% project. Because building D is mixed income, annual income recertifications must be completed for building D.

Example 4 – Recert exemption applies: A property consists of building A (100% HTC) and Building B (100% HTC). Regardless of whether owner elected to treat buildings A and B as separate projects or as part of a multiple-building project, both building A and building B are exempt from recertification.

The recertification exemption applies only to the Housing Tax Credit Program. Units funded by certain other programs (e.g., HOME, section 8, MARIF, etc.) have income recertification requirements that must be separately met.

All Projects: The Annual Student Certification (HTC 35) is always required annually, no later than the anniversary of the Initial Certification.

All owners are advised to read IRS Revenue Procedure 2003-82, effective November 24, 2003, which provides safe harbors under which the Internal Revenue Service will treat a residential unit in a building as low income if the household income has been certified as eligible in the year before the first credit year but their incomes exceed the income limit at the beginning of the first taxable year of the credit period. The Revenue Procedure was issued as a result of questions from taxpayers regarding when individuals must satisfy the applicable income limit when they move into an existing building (or are existing residents) on or after the date a taxpayer acquires a building to be rehabilitated, but before the beginning of the first credit year. Because of those questions, some taxpayers required that the household income not exceed the applicable income limit at the beginning of the first credit year, even though the household income was below the income limit when the household moved into the unit (or was initially certified). This has resulted in some households being evicted, where permissible under local law, from tax credit properties.

Please note that the purpose of this Revenue Procedure is to provide taxpayers protection from challenge by the Internal Revenue Service on this issue. Testing for application of the Available Unit Rule referred to in the Revenue Procedure consists of confirming with the household(s) that the sources and amounts of anticipated income included on the TIC are still current. If additional sources or amounts are identified, the TIC must be updated based on the household's documentation. It is not necessary to complete third party verifications. Minnesota Housing is not required to monitor for compliance with Revenue Procedure 2003-82.

4. Change in Household Composition

For all properties, if there is a change in household composition within the first six (6) months of occupancy, owners or managers must certify the household as if it were a new move-in. This requirement to certify does not apply in cases of natural changes in household composition such as birth, adoption, or death. The combined household income must be at or below the applicable move-in income limit for the new household size. The purpose of this rule is to not allow the addition or removal of household members in order to "manipulate" move-in eligibility.

For mixed-income properties, after six months the addition of a household member to an existing low-income household requires the income certification for the new member of the household, including third party verification. The new tenant's income is added to the income disclosed on the existing household's most recent tenant income certification. The household continues to be considered income-qualified; however, if the combined income exceeds 140%, owners must apply the available unit rule. Note that a certification done in conjunction with adding a household member does not "re-set" the due date for the annual recertification. The annual recertification will be due on its regular anniversary date.

For 100% HTC properties that are exempt from annual income recertification, the new tenant's income is added to the income disclosed on the existing household's original income certification or, if a recertification is on file because the household occupied the unit for more than a year prior to 1/1/2009 when the exemption became effective, the most current recertification.

Minnesota Housing strongly recommends owners and managers screen subsequent household members in the same manner as any new household (i.e., credit check, landlord reference, etc.) prior to allowing them to occupy a unit and to add them to the lease at the time they move-in.

Decreases in family size do not trigger an immediate income certification. Subsequent annual income recertifications will be based on the income of the remaining members of the household. Minnesota Housing has provided a form entitled "Documentation of Decrease in Household Composition" to assist in documenting when the change occurs and who is being removed from a unit.

For all properties, a household may continue to add and remove members as long as at least one member of the original low-income household continues to live in the unit. Once all the original tenants have moved out of the unit, the remaining tenants must be certified as a new income-qualified household unless the remaining tenants were income qualified at the time they moved into the unit. For this reason, managers must document all decreases in household composition even where an annual recertification is not required.

If an owner takes action to remove a noncompliant household by initiating an eviction action, the unit will not be considered out of compliance. If the household does not vacate the unit (i.e., court does not grant the UD), a recertification will be required within 120 days of the determination.

5. Available Unit Rule

Following initial certification, an eligible household's income can increase to 140% of the maximum income level. A household whose income exceeds the maximum income level by more than 140% (an "over-income" household) will remain in compliance as long as the unit continues to be rent restricted and the next available unit or any available unit of comparable or smaller size in the same building is rented to an eligible household at the qualifying rent. The owner must continue to rent any available comparable unit to a qualified household until the percentage of low-income units in a building (excluding the over-income units) is equal to the percentage of low-income units on which the credit is based. At that point, failure to maintain the over-income units as low-income units has no immediate significance.

If any comparable unit that is available or that subsequently becomes available is rented to a nonqualified household, all over-income units for

which the available unit was a comparable unit within the same building lose their status as HTC units; thus, comparably sized or larger over-income units would lose their status as HTC units.

A comparable unit must be measured by the same method the taxpayer used to determine qualified basis for the credit year in which the comparable unit became available (i.e., floor space fraction or unit fraction). An owner may consider a residential unit with similar square footage and amenities to be a comparable unit. A unit that is no longer available for rent due to a reservation that is binding under local law is not an "available unit" for purposes of this rule.

B. Tenant Income Certification (HTC 14)

The Tenant Income Certification, HTC 14, is used to certify a project's eligible households. The use of this Tenant Income Certification form is required in order to ensure the continuity necessary for accurate monitoring of these projects. The form is a legal document which, when fully executed, qualifies the applicant to live in a HTC unit. It is not to be used as a rental application.

After all income and asset information has been verified and computed, management personnel must prepare the Tenant Income Certification. It must be signed and dated by all household members over age 18 and by the owner or owner's agent at initial move-in and upon annual recertification. The effective date of the initial certification should be the move-in date. For projects receiving their credit allocation due to acquisition and/or rehabilitation and where there are existing households, the effective date of the first HTC certification for those existing households cannot be earlier than the first placed in service date (i.e., the acquisition placed in service date). Minnesota Housing recommends that the initial Tenant Income Certification be signed no earlier than 5 days prior to the effective date and no later than the effective date. Annual recertifications must be effective on or before the anniversary of the effective date of the previous certification.

A Tenant Income Certification that is unsigned, undated, or completed late - either after the date the household occupied the unit, or after the anniversary date of the previous certification, will cause the unit to be considered out of compliance until a proper and complete certification or recertification is performed. To avoid issues of noncompliance, Minnesota Housing strongly advises owners and managers to certify and recertify on a timely basis.

Note: Supporting documentation (application/questionnaire, income verifications, asset verifications, etc.) is considered part of the Tenant Income Certification and must be added to the file each year.

Management should instruct the prospective tenant(s) to sign the Tenant Income Certification exactly as the name appears on the form. The tenant's legal name should be given and used just as it will appear on the lease. A unit does not qualify for tax credits unless the household is certified and under lease.

C. Government Data Practices Act Disclosure Statement

In working with tenants, the owner/manager warrants compliance with applicable data privacy laws and regulations including the Minnesota Government Data Practices Act which sets policies on the information that can be obtained, stored and/or released in connection with public programs. In order to comply with this regulation, the signed and dated Government Data Practices Act Statement form must be kept in each household's permanent file. The name of the property must be printed in the box provided, and relevant attachments must be indicated by checking the appropriate boxes. Note that this is **not** a release authorization for verification of income and assets and must not be used as such. Each adult household member's name must be printed clearly at the top in the box provided. An unsigned and/or undated form is not valid and will be noted at time of file inspection.

1. The form is to be signed one-time and is valid as long as the resident lives at the property and participates in the program(s) identified in item #2 on page 1 of the form. If a resident moves from one unit to another, the original signed and dated form should be moved to the file for the new unit. A copy should be kept in the file for the old unit.
2. A valid form **must** include all relevant attachments. Some properties or units within a property may require 2 or more attachments for multiple programs.
3. Only one form is needed per unit as long as the head of household, spouse, co-head, and all household members over the age of 18 have signed and dated the form.
4. If an adult is added to the household or a minor reaches age 18, they must be added to, sign, and date the original form. It is not necessary to complete a new form.
5. A copy of the form should be made available to the applicant/tenant. It is acceptable to give them an unsigned copy.
6. For new residents, the form should be completed at the time of initial application.

D. Miscellaneous Forms to Verify Income

The forms listed below are provided to assist in qualifying eligible tenants. The release of information (at top of form) must be completed and signed by the person who is the subject of the verification prior to sending the form to an employer or other income source. Completed and returned verifications must be attached to the Tenant Income Certification.

- Asset Verification 401K
- Asset Verification Whole or Universal Life
- Alimony/Child Support Verification
- Annuity/Pension/Investment Verification
- Bank Verification
- Certification of Unborn Child/Adoption/Custody
- Disability/Handicap Status
- Divestiture of Assets Verification
- Employment Verification
- Evidence of Income
- Foster Care Verification
- Live-in Aide Verification
- Live-in Aide Agreement
- Military Pay Verification Zero
- Phone Verification/Clarification Record
- Public Assistance Verification
- Real Estate Verification
- Regular Contributions Verification
- Self-Employment Certification
- Special Needs Verification
- Stocks/Bonds Verification
- Student Status and Financial Aid Verification
- Unemployment Compensation Verification
- Veteran's Benefits Verification
- Verification of Section 8 Eligibility
- Workers Compensation Verification
- Zero Income Certification

The use of these particular forms is optional as long as a form that contains the same or additional information is used. A Calculation Worksheet form can be used to assist managers in showing the individual calculations of income and asset income. This is highly recommended and will greatly assist an inspector during a file review.

E. Annualized Income

Income determination is based on the annual gross income a household anticipates it will receive for the 12-month certification period. Verification of all sources of current and anticipated income for all household members age 18 and older, persons under the age of 18 who are treated as adults because they are the head of household, co-head or spouse, and unearned income of minor children must be obtained in order to establish that the income limits are not exceeded.

Owners must convert all verified incomes to annual amounts.

1. To annualize full-time employment, multiply:

   - Hourly wages by 2,080 hours
   - Weekly wages by 52
   - Bi-weekly wages by 26
   - Semi-monthly wages by 24
   - Monthly wages by 12

2. To annualize income from other than full-time employment, multiply:

   - Hourly wages by the number of hours the individual is expected to work per week by 52. If verification shows a range of hours, use the average number of hours (i.e., verification shows 30-35 hours per week, use 32.5 hours).
   - Average weekly amounts by the number of weeks the individual is expected to work.
   - Other periodic amounts (monthly, bi-weekly, etc.) by the number of periods the individual expects to work.

Use an annual wage without additional calculations. For example, if a teacher is paid $25,000 a year, use $25,000, whether the payment is made in 12 monthly installments, 9 installments or some other payment schedule.

- Seasonal or Sporadic Income

If an eligible tenant indicates that income might not be received for the full 12 months (e.g. unemployment insurance), the owner should still determine an annual income as described below.

If an eligible tenant is in a seasonal line of work, for example, a job dependent on weather conditions such as roofing, and normally collects unemployment during the "off" months, both incomes are used for the appropriate number of months. For example, if an individual makes $1,200 a month, typically works 9 months per year and collects unemployment in the amount of $600 a month for the remaining 3 months, income is calculated as follows:

$1,200 x 9	=	$10,800	
$600 x 3	=	$1,800	
		$12,600	= Total Annualized Income

- Unemployed Applicants

The income of unemployed applicants with regular income from any source, such as Social Security, Pension, recurring gifts, etc., must be verified as covered previously.

If an applicant is currently unemployed with no regular verifiable income from any source and claiming zero (0) income, he/she must execute a Certification of Zero Income (found in the Verification Section of the Compliance Manual). Note that the HUD Handbook requires non-monetary contributions (excluding groceries) to be counted as income.

F. Annual Income

The HTC Program uses HUD's definition of "annual income" as contained in the U.S. Housing Act of 1937 as amended. HUD's definition of annual income is very specific and is not simply the amount contained on tax returns.

Annual income is the gross income the household anticipates it will receive from all sources, including all net income derived from assets, during the 12-month period following the effective date of the income certification or recertification. This includes income received by all adult members of the household (18 years of age and older, including full-time students), and unearned income of minor children. In addition, persons under the age of 18 who have entered into a lease under state law are treated as adults, and their annual income must also be counted. These persons will be either the head, spouse, or co-head; they are sometimes referred to as emancipated minors.

Please note that annual income is not the same as adjusted income. Annual income generally corresponds to gross income, with no adjustments (deductions) for child-care, medical expenses, dependents, etc. Adjusted income is used in some federal housing programs, such as Section 8 and Rural Development Section 515, to determine the level of benefit provided to a household. However, it is not used in the HTC Program.

Total Income from all Sources = Annual Income

Earned/ Unearned Income	+	Income from assets	=	Annual Income

Annual income has two components: Earned/Unearned income and Asset income.

Earned/Unearned income includes the following sources: gross wages and salaries including tips and overtime; gross income from social security or welfare; and payments in lieu of earnings (e.g., unemployment compensation, workers' compensation). There are certain mandated inclusions and exclusions which apply when determining earned/unearned income.

Asset income is the amount generated by savings accounts, real estate, and other investments. Assets are items of value, other than necessary personal items, and are considered along with verified income to determine the eligibility of a household.

Please refer to the HUD Handbook 4350.3 for a complete listing and discussion of earned/unearned income and asset income.

The following are examples of income that are included in Annual Income. Also listed are specific types of income that are excluded from income. For those types of income with no specific verification instructions, see Section 6. P., General Income Verification Requirements, below. Generally, if a particular type of income is not specifically mentioned as being excluded, then it is included in Annual Income:

- Interest, dividends and other income from net family assets;
- The gross amount (before any payroll deductions) of wages and salaries, overtime pay, commissions, fees, tips, bonuses, and other compensation for personal services of all adults in the household (including foster adults and persons under the age of 18 who are the head, spouse or co-head). This includes salaries of adults received from a family-owned business.
- Net income, salaries, and other amounts distributed from a business.

Self-Employed Income Verification: The following documents show income verification for the previous year. Owners or their agents must consult with tenants and use this data to estimate income for the next 12 months:

a. Copy of individual federal income tax return (1040) including any:

- Schedule C (Small Business)
- Schedule E (Rental Property Income)
- Schedule F (Farm Income);

b. Copy of Corporate or Partnership tax return (if applicable);

c. Audited or unaudited financial statement(s) of the business (such as a recent profit and loss statement); and

d. Applicant's notarized statement or affidavit as to net income realized from the business during previous year.

Note: All tax returns and related documents must be signed and dated if not filed electronic.

If the business is new and the resident has not yet filed a tax return showing income from a business, a Self Employment Verification – New Business should be completed and the resident must self-certify the anticipated net income from the business. Self-employment can be annualized for the current year business activity based on the number of full months in business. The formula is:

$$\frac{\text{(Net Income Year to Date) x 12 months}}{\text{Number of Months in business during the current year}}$$

- The gross amount (before any deductions for Medicare, etc.) of periodic social security payments. Include payments received by adults on behalf of individuals under the age of 18 including foster children or by individuals under the age of 18 for their own support);

  The following item is required to verify the income derived from the above sources:

  o Copy of current award or benefit statement. This statement is issued when the benefit commences or when a change in the benefit occurs, such as a cost of living adjustment. If an eligible tenant does not have a benefit statement from Social Security that lists the gross monthly benefit, the eligible tenant (or rental applicant) may call the local office of the Social Security Administration or online at http://www.socialsecurity.gov. From the left side bar, select "What you can do online", then select "If you get benefits", then select "Request a Proof of Income Letter". Applicant/tenant should check the box "All Benefit Information Available" to make sure all benefits received are provided. To request a Proof of Income Letter from SSA's toll-free number, call 1-800-772-1213. The Social Security Administration has stated that benefit statements will arrive in the mail in about 10 days.

- The full amount of periodic amounts received from annuities, insurance policies, retirement funds, pensions, disability or death benefits and other similar types of periodic receipts (e.g. Black Lung Sick Benefits, Veterans Disability, Dependent Indemnity Compensation (widow of killed in action serviceman). The withdrawal of cash or assets from an investment received as periodic payments should be counted as income. If benefits are received through periodic payments, do not count any remaining amounts in the account as an asset;
  - Federal Government/Uniformed Services pension funds paid directly to an applicant's/tenant's former spouse pursuant to the terms of a court decree of divorce, annulment, or legal separation are not counted as annual income. The state court has, in the settlement of the parties' marital assets, determined the extent to which each party shares in the ownership of the pension. That portion of the pension that is ordered by the court (and authorized by the Office of Personnel Management (OPM), to be paid to the applicant's/tenant's former spouse is no longer an asset of the applicant/tenant and therefore is not counted as income. However, any pension funds authorized by OPM, pursuant to a court order, to be paid to the former spouse of a Federal government employee is counted as income for a tenant/applicant receiving such funds.
  - Other state, local government, social security or private pension funds paid directly to an applicant's/tenant's former spouse pursuant to the terms of a court decree of divorce, annulment, or legal separation are also not counted as annual income and should be handled in the same manner as above. The decree and copies of statements should be obtained in order to verify the net amount of the pension that should be applied in order to determine eligibility and calculate rent.
  - In instances where the applicant/tenant is a retired Federal Government/Uniformed Services employee receiving a pension that is determined by a state court in a divorce, annulment of marriage, or legal separation proceeding to be a marital asset and the court provides OPM with the appropriate instructions to authorize OPM to provide payment of a portion of the retiree's pension to a former spouse, that portion to be paid directly to the former spouse is not counted as income for the applicant/tenant. However, where the tenant/applicant is the former spouse of a retired Federal Government/Uniformed Services employee, any amounts received pursuant to a court ordered settlement in connection with a divorce, annulment of marriage, or legal separation are reflected on a Form-1099 and is counted as income for the applicant/tenant.
  - Other state, local government, social security or private pensions where pensions are reduced due to a court ordered settlement in connection with a divorce, annulment of marriage, or legal separation and paid directly to the former spouse are not counted as income for the applicant/tenant and should be handled in the same manner as above.

- Delayed periodic payments received because of delays in processing unemployment, welfare or other benefits.

- Payments in lieu of earnings, such as unemployment and disability compensation, workers' compensation and severance pay. Any payments that will begin during the next 12 months must be included.

Unemployment compensation may be verified by:

- A verification form completed by the unemployment compensation agency, records from the unemployment office stating payment dates and amount, or a print-out of the applicant/tenant's unemployment information from the unemployment office's official web site. Note that such print-outs may not contain the person's name only their account number. If the print-out does not contain the person's name, have the applicant/tenant sign and date the print-out with a short statement that this information accurately represents his or her account information.

- Student Financial Assistance.

  All forms of student financial assistance (grants, scholarships, educational entitlements, work study programs, and financial aid packages) are excluded from annual income except for students receiving Section 8 assistance. This is true whether the assistance is paid to the student or directly to the educational institution

  For students receiving Section 8 assistance, all financial assistance a student receives (1) under the Higher Education Act of 1965, (2) from private sources, or (3) from an institution of higher education that is in excess of amounts received for tuition is included in annual income except if the student is over the age of 23 with dependent children or the student is living with his or her parents who are receiving Section 8 assistance. See Paragraph 3-13 of HUD Handbook 4350.3 for further information on eligibility of students to receive Section 8 assistance and the Glossary for the definition of Student Financial Assistance.

  This rule applies to both part time and full time students.

- Welfare assistance.

Documentation Required: To verify income from welfare or public assistance, a written statement from the welfare agency is required. The statement should address the type and amount of assistance the family is currently receiving and note any changes in assistance expected during the next 12 months.

Annual Income for Section 8 Household: The annual income for a household receiving housing assistance payments under Section 8 may be verified by obtaining a statement from the Public Housing Authority (PHA). The owner must submit the Verification of Section 8 Eligibility form to the PHA for completion. If the form shows that the tenant's income does not exceed the applicable income limit, the household is eligible to occupy a rent-restricted unit.

Please note: The annual income is the gross annual income without any adjustments or Section 8 Program allowances. Due to the seriousness of accurate income eligibility, Minnesota Housing recommends that the owner/owner's agent verify and calculate the household income directly from the source(s) and not rely on PHA verification for initial certifications.

- Alimony and child support awarded by the court. Owners must count alimony or child support amounts awarded by the court unless the applicant certifies that payments are not being made and that he or she has taken all reasonable legal actions to collect amounts due, including filing with the appropriate courts or agencies responsible for enforcing payment.

Documentation Required: If alimony or child support is being received, obtain one of the following:

- Copy of a separation or settlement agreement or copy of a divorce decree stating the amount and type of support and payment schedule.
- Verification form completed by the person paying the support or support enforcement office as to amounts being paid.
- A copy of the latest check.
- When no documentation of child support, divorce, or separation is available, either because there was no marriage or for another reason, the owner may require the family to sign a certification stating the amount of child support received.

In many cases, child support has been court ordered but the full amount is not being received. If this is the case, verification from the child support enforcement agency will be sufficient. Or, request tenant to provide a statement attesting to the fact that support payments are not being received; the likelihood of support payments being received in the future, and that a reasonable effort has been made to collect the amounts due.

Alimony or child support paid by a member of the household is not deducted from income, even if it is garnished from wages.

- Recurring monetary or non-monetary contributions or gifts regularly received from persons not living in the unit. These sources may include rent, utility and other payments paid on behalf of the household, and other cash or noncash contributions provided on a regular basis.

Documentation Required: Verification of continuing monetary or non-monetary gifts may be verified in one of two ways:

  - A Regular Contributions Verification signed by the person providing the assistance stating the purpose, dates and value of the contributions and/or gifts; or
  - A statement or affidavit from the tenant stating the purpose, dates and value of the gifts.

Groceries and/or contributions paid directly to the child care provider by persons not living in the unit are excluded from annual income.

Temporary, nonrecurring, or sporadic income (including gifts) is not counted.

- Relocation payments made pursuant to Title II of the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970;
- Actual income distributed from trust funds that are not revocable by or under the control of any member of the tenant family.
- All regular pay, special pay, and allowances of a member of the Armed Forces, except hostile fire pay. Note that until January 1, 2012, Basic Pay Allowance for housing is disregarded for properties located in a county that contains a qualified military installation to which the number of members assigned to units based out of the military installation as of June 1, 2008, has increased by 20% or more from December 31, 2005. This applies to the county that contains the military installation and also to adjacent counties. A qualified military installation is a military installation or facility with 1,000 or more members as of June 1, 2008.

G. Exclusions from Annual Income

- Income from employment of children (including foster children) under the age of 18 years;
- Meals on wheels or other programs that provide food for the needy; groceries provided by persons not living in the household; and amounts received under the School Lunch Act and the Child Nutrition Act of 1966, including reduced lunches and food under the Special Supplemental Food Program for Women, Infants and Children (WIC);
- Amounts paid by a State agency to a family with a developmentally disabled family member living at home to offset the cost of services and equipment needed to keep the developmentally disabled family member at home;
- Grants or other amounts received specifically for medical expenses, including Medicare premiums paid by an outside source, set aside for use under a Plan to Attain Self Sufficiency (PASS) and excluded for purposes of Supplemental Security Income eligibility, out of pocket expenses for participation in publicly assisted programs (such amounts must be made solely to allow participation in these programs. These expenses include special equipment, clothing, transportation, child care, etc.);
- Earnings in excess of $480 for each full-time student 18 years of age or older (<u>excluding</u> the head of household, co-head or spouse);
- Adoption assistance payments in excess of $480 per adopted child;
- Loans such as personal loans (see HUD Handbook 4350.3 on business loans which are <u>not</u> excluded);
- Temporary, nonrecurring or sporadic income (e.g. gifts);
- Amounts received by the household in the form of refunds or rebates under state or local law for property taxes paid on the dwelling unit;
- Special pay to a household member serving in the armed forces who is exposed to hostile fire (e.g., in the past, special pay included Operation Desert Storm);
- Deferred periodic amounts from Department of Veterans Affairs disability benefits that are received in a lump-sum or in prospective monthly amounts;

- Amounts received under training programs funded by HUD;
- Compensation from state or local employment training programs and training of a household member as resident management staff. Amounts excluded under this provision must be received under employment training programs with clearly defined goals and objectives, and are excluded only for a limited period as determined in advance under the program by the state or local government;
- A resident service stipend. A resident service stipend is a modest amount (not to exceed $200 per month) received by a resident for performing a service for the owner, on a part-time basis, that enhances the quality of life in the development. Such services may include, but are not limited to, fire patrol, hall monitoring, lawn maintenance, and resident initiatives coordination. No resident may receive more than one such stipend during the same period of time.
- Reparation payments made by a foreign government pursuant to claims filed under the laws of that government by persons who were persecuted during the Nazi era. Examples include payments by the German and Japanese governments for atrocities committed during the Nazi era.
- Deferred periodic amounts from supplemental security income and social security benefits that are received in a lump-sum amount or in prospective monthly amounts
- Payments received for the care of foster children or foster adults.
- Amounts received in behalf of someone not living in the unit as long as the amounts are (i) not inter-mingled with the family funds, and (ii) used solely to benefit the person not residing with the family. For such amounts to be excluded, the individual must provide the owner with an affidavit stating that the amounts are received on behalf of someone who does not reside with the family and the amounts meet the conditions above.
- Recurring child care payments paid directly to a provider by persons not living in the unit.

H. Income Excluded by Federal Statute:

- The value of the allotment provided to an eligible household under the Food Stamp Act of 1977.
- Payments received under Domestic Volunteer Service Act of 1973 (employment through VISTA, Retired Senior Volunteer Program, Foster Grandparents Program, youthful offender incarceration alternatives, senior companions).
- Interests of individual Indians in trust or restricted lands, and the first $2,000 per year of income received by individual Indians that is derived from trust or restricted lands.
- Payments received under the Alaska Native Claim Settlement Act (43 U.S.C. 1626(c)) received from a Native Corporation, including:
  - Cash (including cash dividends on stock received from a Native Corporation) to the extent that it does not, in the aggregate, exceed $2,000 per individual per annum;
  - a partnership interest;
  - land or an interest in land (including land or an interest in land received from a Native Corporation as a dividend or distribution of stock); and
  - an interest in a settlement trust.

- Payments from certain submarginal U.S. land held in trust for certain Indian tribes.
- Payments from disposal of funds of Grand River Bank of Ottawa Indians.
- The First $2,000 of per capita shares received from judgments awarded by the Indian Claims Commission or the Court of Claims or from funds the Secretary of Interior holds in trust for an Indian tribe.
- Payments, rebates or credits received under Federal Low-income Home Energy Assistance Programs. Includes any winter differentials given to elderly.
- Payments received under programs funded in whole or in part under the Job Training Partnership Act (employment and training programs for native Americans and migrant and seasonal farmworkers, Job Corps, veterans employment programs, State job training programs, career intern programs, AmeriCorps.)
- Payments received under Title V of the Older Americans Act (Green Thumb, Senior Aides, Older American Community Service Employment Program).
- Payments received after January 1, 1989, from the Agent Orange Settlement Fund or any other fund established pursuant to the settlement in the In re Agent Orange, product liability litigation. M.D.L. No. 386 (E.D.N.Y.)
- Payments received under the Maine Indian Claims Settlement Act of 1980 (Pub. L. 96-420, 9z Stat. 1785).
- Any earned income tax credit to the extent it exceeds income tax liability. (26 U.S.C. 32(j)).
- The value of any child care provided or arranged (or any amount received as payment for such care or reimbursement for costs incurred for such care) under the Child Care and Development Block Grant Act of 1990 (CCDBGA) (42 U.S.C. 9858q).

I. Income from Assets

Assets are items of value, other than necessary personal items, and are considered along with verified income to determine the eligibility of a household. Assets of all household members, including minors, foster children, and foster adults must be considered.

Verification of assets is required. The asset information (total value and income to be derived) should be obtained at the time of application or recertification. The applicant will affirm that this information is correct by executing the Tenant Income Certification, HTC 14.

Third party verification of assets is required when the combined value of assets exceed $5,000.

Effective October 11, 1994, an owner may satisfy the third party documentation requirement for a tenant's income from assets if the tenant submits to the owner a signed, sworn statement that the value of the combined assets is less than $5,000. The use of Minnesota Housing 's form entitled Under $5000 Asset Certification, HTC 24 is required for this procedure. The form must also be used when an applicant/tenant declares there are no assets including checking and/or savings accounts. If a project is required to obtain third party verifications

because of participation in another housing program (i.e., Section 8, HOME, RHS, etc.), or an owner's or management company's policy is to third-party verify assets, then do not also use the Under $5000 Asset Certification, HTC 24.

Note that neither the Under $5,000 Asset Certification nor third party verification of assets is required if a Housing Choice Voucher recipient's gross annual household income is verified by the HRA/PHA on a Verification of Section 8 Eligibility form as these amounts will already have been verified and included by the HRA/PHA.

Minnesota Housing 's monitoring procedure and IRS Revenue Procedure 94-65 do not permit an owner to rely on a low-income tenant's signed, sworn statement of annual income from assets if a reasonable person in the owner's position would conclude that the tenant's income is higher than the tenant's represented annual income. In this case, the owner must obtain other documentation of the low-income tenant's annual income from assets to satisfy the documentation requirement of third party asset verification.

The following information is based upon the HUD Section 8 Program. The owner must use the definition of "Net Family Assets" in 24 CFR 813.102, which provides definitions for the HUD Section 8 Program.

Household Assets include:

- Cash held in savings and checking accounts, safe deposit boxes, homes, etc. For savings accounts use the current balance. For checking accounts, use the average balance for the last six months. Assets held in foreign countries are considered assets.

Documentation Required:

- Verification forms, account statements (must obtain 6 months worth of statements to determine 6 month average balance for checking accounts), passbooks, certificates of deposit, letters or documents from a financial institution or broker.
  - If an owner accepts an IRS Form 1099 from the financial institution, the owner must adjust the information to project earnings expected for the next 12 months.
  - In the case of real estate that is in the process of being foreclosed, satisfactory documentation would be 1) a copy of the most recent property tax statement showing the current market value of the home, and 2) a copy of the most recent mortgage statement or foreclosure notice showing the balance owed.

- Revocable trusts. Include the cash value of any revocable trust available to the household.

- Equity in rental property or other capital investment. Include the current fair market value less (a) any unpaid balance on any loans secured by the property; and (b) reasonable costs that would be incurred in selling the

asset (i.e., penalties, broker fees, etc.). Note: If the person's main business is real estate, then count any income as business income. Do not count it as an asset and as business income.

Documentation Required: Only the interest portion of the monthly payment received by the tenant is included. For interest income from the sale of real property, if said property was sold on an installment sales contract, request:

- A letter from an accountant, attorney, real estate broker, the buyer, or a financial institution stating interest due for the next 12 months. (A copy of the check(s) paid by the buyer to the tenant is NOT sufficient since appropriate breakdowns of interest and principal are not included.); or
- Amortization schedule showing interest for the 12 months following the date the purchaser intends taking occupancy.

For rental income from property owned by the tenant, request:

- IRS Form 1040 with Schedule E (Rental Income).
- Lessee's written statement identifying monthly payments due the tenant and tenant's affidavit as to net income realized.

- Stocks, bonds, treasury bills, certificates of deposit, money market accounts. Interest or dividends earned are counted as income from assets even when the earnings are reinvested. The value of stocks and other assets vary from one day to another. The value of the asset may go up or down the day before or after income is calculated and multiple times during the year thereafter. The owner may assess the value of these assets at any time after the authorization for the release of information has been received.

  Documentation Required:

  Broker's quarterly statements showing value of stocks or bonds and any earnings or dividends, or quotes from a stock broker as to net amount the family or household would receive if they liquidated securities.

  - Individual retirement and Keogh accounts. These are included when the holder has access to the funds, even though a penalty may be assessed. If the individual is making occasional withdrawals from the account, determine the amount of the asset by using the average balance for the previous six months. (Do not count occasional withdrawals as income.)

  - Retirement and pension funds. While the person is employed include only amounts the family can withdraw without retiring or terminating employment. Count the whole amount less any penalties or transaction costs. At retirement, termination of employment, or withdrawal, periodic receipts from pension and retirement funds are counted as income. Lump sum receipts from pension and retirement funds are counted as assets. Count the amount as an asset or as income as provided below:

- If benefits will be received in a lump sum, include the lump sum receipt as an asset.
- If benefits will be received through periodic payments, include the benefits in annual income. Do not count any remaining amounts in the account as an asset unless the remaining amount can be withdrawn.
- If the individual initially receives a lump sum benefit followed by periodic payments, count the lump sum benefit as an asset and treat the periodic payment as income. In subsequent years, count only the periodic payment as income. Do not count the remaining amount as an asset unless the remaining amount can be withdrawn.
- In instances where the applicant/tenant is a retired Federal government employee receiving a pension that is determined by a state court in a divorce, annulment of marriage, or legal separation proceeding to be a martial asset and the court provides OPM with the appropriate instructions to authorized OPM to provide payment of a portion of the retiree's pension to a former spouse, that portion to be paid directly to the former spouse is not counted as income for the applicant/tenant. However, where the tenant/applicant is the former spouse of a retired Federal government employee, any amounts received pursuant to a court ordered settlement in connection with a divorce, annulment, of marriage, or legal separation are reflected on a Form-1099 and is counted as income for the applicant/tenant.

- Cash value of life insurance policies available to the individual before death (i.e., the surrender value of a whole life policy or a universal life policy). It would not include a value for term insurance, which has no cash value to the individual before death.
- Personal property held as an investment. Include gems, jewelry, coin collections, and antique cars held as an investment. An applicant's wedding ring and other personal jewelry are not considered assets.
- Lump sum receipts or one-time receipts. These include inheritances, capital gains, one-time lottery winnings, victim's restitution; settlements on insurance claims (including health and accident insurance, worker's compensation and personal or property losses); and any other amounts that are not intended as periodic payments.
- A mortgage or deed of trust held by an applicant (e.g., contract for deed). Payments on this type of asset are often received as one combined payment of principal and interest with the interest portion counted as income from the asset.

This combined figure needs to be separated into the principal and interest portions of the payment. (This can be done by referring to an amortization schedule that relates to the specific term and interest rate of the mortgage.)

To count the actual income for this asset, use the interest portion due, based on the amortization schedule, for the 12-month period following the certification.

To count the cash value of this asset, determine the unpaid principal as of the effective date of the certification. Each year this balance will decline as more principal is paid off.

J. Household Assets Do Not Include

- Necessary personal property including clothing, furniture, cars, etc.
- Interests in Indian trust land.
- Term life insurance policies.
- Equity in the cooperative unit in which the family lives.
- Assets that are part of an active business (not including rental of properties that are held as investment and not a main occupation).
- Assets that are not effectively owned by the applicant. That is, when assets are held in an individual's name, but the assets and any income they earn accrue to the benefit of someone else who is not a member of the household, and that other person is responsible for income taxes incurred on income generated by the assets.
- Assets that are not accessible to the applicant and provide no income to the applicant (i.e., a battered spouse owns a house with her husband. Because of the domestic situation, she receives no income from the asset and cannot convert the asset to cash). Nonrevocable trusts are not covered under this paragraph.

K. Assets Owned Jointly

Assets owned by more than one person should be prorated according to the percentage of ownership. If no percentage is specified or provided by state or local law, prorate the assets evenly among all owners.

L. Instructions for Valuing Assets

In computing assets, owners must use the cash value of the asset; that is, the amount the family or household would receive if the asset were converted to cash. Cash value is the market value of the asset minus reasonable costs that were or would be incurred in selling or converting the asset to cash. Expenses which may be deducted include:

- Penalties for withdrawing funds before maturity;
- Broker/legal fees assessed to sell or convert the asset to cash; and
- Settlement costs for real estate transactions.

For non-liquid assets, enough information should be collected to determine the current cash value -- the net amount the family would receive if the asset were converted to cash.

Owners must count assets disposed of for less than fair market value during the two years preceding certification or recertification. The amount counted as an asset is the difference between the cash value and the amount actually received, if the difference is more than $1,000. If a tenant has sold his/her home (either a private residence or rental) or disposed of other assets within the past two years for less than fair market value, request:

- Copies of closing documents (HUD-1, settlement statement) showing the selling price, the distribution of the sales proceeds and the net amount to the tenant.
- Divestiture of Assets Verification identifying the disposed-of asset, the cash value and amount actually received.

If net family/household assets exceed $5,000.00, the annual income must include the greater of:

- The actual income from assets; or
- An imputed income from assets.

Owners must determine estimated asset income by multiplying total net assets by the interest rate specified by HUD. Until further notice, use a rate of two percent (.02). This rate is effective September 29, 1995.

M. Example of Calculating Income from Assets

Type of Asset	Cash Value of Asset	Actual Income Per Year
Checking Account	$300	$0
Savings Account	2,000	115
Certificates of Deposit	10,000	986
Rental Property	15,000	0
TOTALS	$27,300	$1,101

1. Since total assets exceed $5,000, estimated (imputed) income must be calculated:

   Total Assets x .02 = $27,300 x .02 = $546

2. Annual income must include the $1,101 actual income because it is greater than the estimated (imputed) income received on the assets.

N. General Income Verification Requirements

All income and asset sources must be disclosed on the eligibility application and verified. A good application must be used as the basis for determining which written third party verifications may be necessary. The application, along with all supporting documentation and the Tenant Income Certification (HTC 14), will be reviewed by Minnesota Housing staff during a tenant file review.

Written verification directly from the source (third-party verification) is the standard and most reliable method of verifying income. Written verifications must contain complete and detailed information and include, at a minimum, direct written verification from all sources of regular income and income from assets. The owner may obtain accurate third-party written verification by facsimile, e-mail, or Internet, if adequate effort is made to ensure that the sender is a valid third-party source. Information verified on the Internet is

considered third party verification if the owner is able to view web-based information from a reputable source on the computer screen. Use of a printout from the Internet may also be adequate verification in many instances.

Verifications must contain a release authorization signed by the applicant/tenant. Do not use a blanket release authorization as this entitles the owner or manager to obtain information to which it is not entitled or needed for eligibility determination. The Data Practices Act Disclosure Statement is not a verification release. Applicants should be asked to sign two copies of each verification form. The second copy may be used if the first request has not been returned in a timely manner.

Income verification requests must be sent directly to and from the source. They are never given to the tenant to obtain signatures. It is suggested that a self-addressed stamped envelope be included with a mailed request for verification. If the returned verifications do not contain complete information (typical examples include failure to indicate interest rates, dates of anticipated raises, amounts of anticipated raises, etc.), managers must follow up with the source to obtain complete information. All pertinent information must be documented in the file and must also include the name, phone number and title of the contact, the name of the person accepting the information, and the date.

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 contact 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. When written, third-party verification is not possible, there are two options:

1. Second party verification including copies of pay stubs (the most recent four to six, consecutive, recent pay stubs are required, but six months worth is recommended and more may be needed particularly in situations where a person works varying hours during different seasons), quarterly or monthly asset statements, W-2's, etc. Copies of paychecks or bank statements showing direct deposit are not acceptable because deductions are not shown.
2. An owner may accept a tenant's sworn statement regarding the veracity of information submitted if the information cannot be verified by another acceptable verification method.

Prior steps used to obtain written verification must be documented to show just cause for using other types of verification. The owner must include the following documents in the tenant file:

1. A written note explaining why third-party verification is not possible; or
2. A copy of the date-stamped original request that was sent to the third party;
3. Written notes or documentation indicating follow-up efforts to reach the third party to obtain verification; and
4. A written note indicating the request has been outstanding without a response from the third party.

Note: If a tenant is employed by a business owned by the tenant's family or is employed by the property owner or the management company, a copy of a recent pay stub, verifying year-to-date earnings, is also required.

Upon receipt of all verifications, owners or managers must determine if the resident is qualified for participation in the HTC Program. All verifications should be reviewed and calculations made as necessary.

O. Effective Term of Verification

Written verifications of income are valid for 120 days prior to the effective date of move-in and annual recertification. After this time, new written verification must be obtained.

P. Date Stamp

All tenant income, asset, and eligibility verifications should be date-stamped as they are received.

Chapter 7 – Sale, Transfer or Disposition of the Project after the Placed-In-Service Date

Since Minnesota Housing is required to notify the Internal Revenue Service via form 8823 in the event of sale (including change in ownership or ownership interest), foreclosure, abandonment, casualty loss, and/or destruction, owners must notify Minnesota Housing of such events. It is recommended that, whenever possible, notification occur in advance of a transfer so that the appropriate documentation is obtained.

When a sale or transfer occurs after the placed-in-service date, the owner must submit the Notice of Intent to Transfer Ownership, or Change Owner Name or Status (HTC 27) with the required documentation and a letter advising Minnesota Housing of the transfer of ownership. The new owner must include a copy of the recorded Statutory Warranty Deed indicating the change of ownership or a copy of the title policy indicating the new owner as the vested owner of the property.

It is not necessary to send duplicate sets of documentation if a transfer of ownership involves a property on which Minnesota Housing has financing and an assumption of the loan(s) is involved.

Minnesota Housing will recognize a new owner or ownership entity only after all required documentation has been submitted. Until such time, all compliance requirements will be the responsibility of the owner of record and any compliance violations will be reported to the IRS under the name of the owner of record.

The IRS has also suggested in Reg. 1.42-5 that, if a building is sold or otherwise transferred by the owner, the transferee should obtain from the transferor all information related to the first year of the credit period so the transferee can substantiate credits claimed.

Please note: Under current Minnesota Housing policies, any change or transfer of ownership from the date of reservation to five years after the placed in service date will have an adverse effect on all individuals/entities that wish to submit applications for tax credits in future years.

Under 42(j)(6), revised 7/30/2008, there is no recapture on dispositions as long as a) it is reasonably expected the building will continue to be operated as a qualified low-income building; and b) the taxpayer elects to be subject to the new longer statute of limitations. Owners are no longer required to post a Credit Disposition Bond or pledge Treasury Securities to avoid recapture.

Chapter 8 – Correction and Consequences of Non-Compliance

In January 2007, the Internal Revenue Service issued its Guide for Completing Form 8823, Low Income Housing Credit Agencies Report of Noncompliance or Building Disposition (8823 Guide), which provides instructions for monitoring agencies to determine noncompliance, what constitutes correction, and how and when noncompliance and property dispositions are to be reported.

Owners and property managers are encouraged to read the guide and refer to it when questions arise as to how noncompliance should be corrected. The 8823 Guide can be found on Minnesota Housing's website at: http://www.mnhousing.gov/housing/tax-credits/compliance/MHFA_004655.aspx.

A. Notice to owner

Minnesota Housing is required to provide prompt written notice to the owner of a housing tax credit project if Minnesota Housing does not receive the certification form HTC 12 and other forms, or does not receive or is not permitted to inspect the tenant income certifications, supporting documentation, and rent records, or discovers by inspection, review, or in some other manner, that the project is not in compliance with the provisions of Section 42 or its Declaration of Land Use Restrictive Covenants.

B. Correction Period

The correction period will be established by Minnesota Housing and set forth in the notice of non-compliance and will be a period of up to 90 days from the date of the notice to the owner described in paragraph (e)(2) of Reg. 1.42-5. Minnesota Housing is permitted to extend the correction period for up to six total months, but only if Minnesota Housing determines there is good cause for granting the extension. Requests for an extension must be in writing, must be received by Minnesota Housing no later than the last day of the correction period identified on the Notice of Noncompliance, and must include an explanation of the efforts to correct the noncompliance and the reason the extension is needed.

Minnesota Housing will review the owner's response and supporting documentation, if any, to determine whether the noncompliance has been clarified or corrected.

C. Notice to Internal Revenue Service

Minnesota Housing is required to file Form 8823, "Low Income Housing Credit Agencies Report of Non-Compliance or Building Disposition," with the IRS no later than 45 days after the end of the correction period (including permitted extensions).

Minnesota Housing must check the appropriate box on Form 8823 indicating the nature of the non-compliance or failure to certify and indicate whether the owner has corrected the non-compliance or failure to certify. If the non-compliance or failure to certify is corrected, Minnesota Housing will provide a date on which the noncompliance was corrected. If Minnesota Housing cannot determine that an owner's actions have corrected all noncompliance, no correction date will be provided; however, an attachment to the 8823 will be provided which identifies any noncompliance that is corrected. Any change in either the applicable fraction or eligible basis under paragraph (c)(1)(ii) and (vii) of Reg. 1.42-5, respectively, that results in a decrease in the qualified basis of the project under Section 42 (c)(1)(A) is non-compliance that must be reported to the IRS. Minnesota Housing will send the owner a copy of the form 8823 at the time it is filed with the IRS.

If uncorrected noncompliance is reported to IRS, a corrective 8823 cannot be filed until all instances of noncompliance are corrected for that building.

If Minnesota Housing reports on Form 8823 that a building is entirely out of compliance and will not be in compliance at any time in the future, it is not necessary to file Form 8823 in subsequent years to report that building's non-compliance.

D. Recapture of Credit

Generally, during the Compliance Period a project is out of compliance and recapture applies if:

- There is a decrease in the qualified basis of the building from one year to the next; or
- The building no longer meets the minimum set-aside requirements of Section 42(g)(1), the gross rent requirements of Section 42(g)(2), or the other requirements for the units which are set-aside.

Vacant units that were previously occupied by Housing Tax Credit tenants can continue to be counted for minimum eligibility as long as the owner/manager has made reasonable attempts to rent the unit to an eligible tenant. See Revenue Ruling 2004-82, Q9 for guidance on what constitutes reasonable attempts.

If the project is out of compliance, a penalty will apply to all units in the Project (IRS Form 8611). Penalties may include:

- Recapture of the Accelerated Portion of the tax credits for prior years;
- Disallowance of the credit for the entire year in which the non-compliance occurs; and
- Assessment of interest for the recapture year and previous years.

If the non-compliance is due to a reduction in qualified basis and the minimum eligibility requirements of twenty percent (20%) or forty percent (40%) are still met, recapture and disallowance of credit will apply only to units not in compliance.

If there is a minimal reduction in the floor space fraction or number of Qualified Units, no recapture will occur, provided the building remains a qualifying Housing Tax Credit building.

Recapture will not occur if, within a reasonable time after the non-compliance was discovered, the situation is corrected.

In the event of a casualty loss, recapture will not occur if the property is restored or replaced within a reasonable period of time.

The above information has been provided for informational purposes in order to give a general understanding of recapture procedures. The Internal Revenue Service bears the responsibility for determining whether a building owner has claimed the correct amount of credit each year and whether a building owner is subject to recapture. Minnesota Housing is not responsible for determining whether or not a specific event of noncompliance is a recapture event.

Chapter 9 – Compliance & Monitoring After Year 15

Background

After the 15-year Compliance Period has expired, there may be no tax impact in the event of noncompliance. Therefore, filing IRS form 8823 to report noncompliance is no longer an effective consequence. By establishing policy which reflects the terms of the Declaration rather than all Internal Revenue Code (IRC) Section 42 regulations, by creating reasonable and less frequent inspection criteria, and by redefining some of the reporting and eligibility criteria as identified below, it is hoped that it will be administratively easier and less costly for owners and managers to operate tax credit properties and maintain compliance at a time when the tax benefit is no longer available. Therefore, after year 15, compliance can be achieved much easier, but the spirit of the program is not compromised and the housing will continue to serve the people for whom the program was intended.

IRC Section 1.42-5 contains the regulations for agencies' compliance monitoring during the Compliance Period; however, the regulations do not require agencies to monitor according to these regulations in the Extended Use Period. IRS officials and other experts have indicated that agencies may not report noncompliance to IRS after the Compliance Period is over. The tax benefit to the owner is exhausted and IRS can no longer recapture or disallow credits. Therefore, Minnesota Housing must establish policy regarding how properties are to be monitored and consequences for noncompliance during the Extended Use Period.

In addition, based on the requirements of the Extended Use Period specified in IRC Section 42 regulations and in Declaration of Land Use Restrictive Covenants referenced below, the agency has the authority to establish different criteria for eligible/ineligible student households, available unit rule, unit transfers, and the process for performing annual recertifications during the Extended Use Period, as long as income and rent restrictions, general use requirements (fair housing), Section 8 acceptance, minimum set-aside, applicable fraction, and initial and annual recertifications are required.

A. Compliance Period

Under Internal Revenue Code (IRC) Section 42(j)(1) the Compliance Period means, with respect to any building the period of 15 taxable years, beginning with the first taxable year of the credit period.

The first year of the Compliance Period is the first year in which the owner claimed credits. The first year must be either the year the building(s) are placed in service, or at the owner's election the year following placed in service. All requirements of IRC Section 42 including the 1.42-5 monitoring regulations are in effect during the 15-year Compliance Period.

B. Extended Use Period

IRC Section 42(h)(6) establishes that buildings are eligible for the credit only if there is a minimum long-term commitment to low-income housing. Specifically, in order to receive a credit allocation in 1990 and later, the owner must record an extended low-income housing commitment. The document that evidences this commitment is called the Declaration of Land Use Restrictive Covenants for Housing Tax Credits (Declaration). The Declaration is recorded with the respective County Recorder and/or Registrar of Titles and "runs with the land", regardless of subsequent changes in ownership.

1. For purposes of this section, the term "Extended Use Period" means the period:

   a) beginning on the last day in the Compliance Period on which such building is part of a qualified low-income housing project, and
   b) ending on the later of—
      i. the date specified by the agency in the Declaration, or
      ii. the date which is 15 years after the close of the Compliance Period

   IRC Section 42(h)(6)(E) provides exceptions to the Extended Use Period in the case of a legitimate foreclosure or deed in lieu or, for projects that have not waived this right, if the agency is unable to present a qualified contract pursuant to IRC Section 42(h)(6)(F). This Compliance Manual does not contain guidance for the provisions of IRC 42(h)(6)(F) regarding the qualified contract referenced in IRC Section 42(h)(6)(E)(i)(II).

2. Under IRC Section 42(h)(6)(E)(ii) the termination of an Extended Use Period due to foreclosure or deed in lieu, or for failure to present a qualified contract shall not be construed to permit before the close of the 3-year period following such termination:

   a) the eviction or the termination of tenancy (other than for good cause) of an existing tenant of any low-income unit, or
   b) any increase in the gross rent with respect to such unit not otherwise permitted by the applicable rent limits.

3. Under the Minnesota Housing Declaration of Land Use Restrictive Covenants for Housing Tax Credits the owner agrees to comply with the following for the term of the agreement:

   a) it will maintain the applicable fraction by leasing units to individuals or families whose income is 50% or 60%, as irrevocably elected by the owner at the time of allocation, or less of the area median gross income (including adjustments for family size) as determined in accordance with IRC Section 42;
   b) it will maintain the Section 42 rent and income restrictions;
   c) all units subject to the credit shall be leased and rented or made available to members of the general public who qualify as low-income tenants (or otherwise qualify for occupancy of the low-income units) under the

applicable election specified in IRC Section 42(g) (Section 42(g) pertains to the minimum set-aside election);

d) the owner agrees to comply fully with the requirements of the Fair Housing Act as it may from time to time be amended;
e) the owner will not refuse to lease a unit to the holder of a Section 8 voucher because of the status of the prospective tenant as such a holder;
f) each low income unit will remain suitable for occupancy;
g) the determination of whether a tenant meets the low-income requirement shall be made by the owner at least annually on the basis of the current income of such low-income tenant ; and
h) other restrictions as required under the specific year's Qualified Allocation Plan (QAP) and related points the owner received in order to obtain a credit allocation. These restrictions are property-specific within the respective Declarations and to the extent they are not otherwise time-limited, the additional restrictions remain in force and effect during the Extended Use Period.

Note that the Declarations have changed from year-to-year according to the respective Qualified Allocation Plans. However, the basic language pertaining to the Extended Use Period required by IRC has not materially changed.

C. Tenant Eligibility Criteria During the Extended Use Period

During the Extended Use Period, Minnesota Housing requires tenant eligibility and certification of income, as follows:

1. Tenant Income Certification. At initial occupancy, an initial income certification is required (calculated in a manner consistent with the determination of annual income under section 8 of the United States Housing Act of 1937 ("Section 8"), not in accordance with the determination of gross income for federal income tax liability). Annual recertification is as follows:
   - **Mixed-income** tax credit properties must recertify annually but owners are not required to verify income and income from assets (unless there is other financing or rental subsidy program that requires verification). Households must complete a Household Questionnaire or similar form. From information provided by the tenant household, owners must calculate gross annual income, complete the Tenant Income Certification form and report the recertification on the Tax Credit Summary Report.
   - **100%** tax credit properties have no recertification requirements; however, on the anniversary date of move-in or the last certification effective date, owners must report the unit and household on the Tax Credit Summary Report and complete all information except current income and student status (see 2, below).

   Any household that experiences a change in composition within the first six (6) months of occupancy (not including birth or death) must meet initial eligibility requirements and a new initial tenant income certification must be performed.
2. Student Status. Since student status is not one of the defined requirements of the Declaration, the student rules under IRC Section 42 are no longer applicable.

3. Unit Transfers. Unit transfers from building to building are allowed without triggering noncompliance regardless of the multiple-building election or whether a household's income is over the applicable limit at the time of transfer.
4. Available Unit Rule. The available unit rule is revised to provide that if a household's income goes over 140% of the applicable income limit, a currently vacant unit or the next unit in the same building must be rented to a qualifying household (the "comparable or smaller" requirement no longer applies). This is essentially a one-for-one unit replacement.
5. Applicable Fraction. Only the unit fraction will be examined to determine a building's applicable fraction.
6. Rent Limits. Rent limits as elected by the owner at the time of allocation continue to be in force during the Extended Use Period. Owners of properties that were awarded selection points for additional rent restrictions should refer to the respective Qualified Allocation Plan or Declaration to determine whether those additional rent restrictions are time-limited or if they are in effect for the full term of the Extended Use Period.
7. Utility Allowances. Utility Allowances must continue to be updated annually. Revised utility allowances must be implemented within 90 days of their published effective date.

   Minnesota Housing will continue to update the Housing Tax Credit Program income and rent limits published by HUD annually.

D. Monitoring Compliance During the Extended Use Period

The following is the monitoring procedure Minnesota Housing will follow during the Extended Use Period:

1. Annual Certification. By February 15, or the next business day, Minnesota Housing will require all owners to submit an annual certification of compliance. The Owner's Certification of Compliance During the Extended Use Period, form HTC 12(Y15), contains agency-defined certification language pursuant to the terms of the Declaration.

2. Annual Reporting. The Tax Credit Summary Report (HTC 13) and related Applicable Fraction Summary must be submitted to Minnesota Housing annually along with the HTC 12(Y15), but owners are not required to report on student status.

3. Inspections. Every five years, Minnesota Housing will perform a physical inspection of the property and review of tenant files and other pertinent documentation. The first review in the Extended Use Period will be five years from the last inspection conducted during the Compliance Period. A minimum of 3 low-income units chosen at random, or maximum of 10% of the low-income units not to exceed 15 units in any development will be inspected. If the first 3 units pass inspection, then no additional units need to be inspected. Different units may be chosen for the file review as those receiving a physical inspection. Minnesota Housing Tax Credit compliance staff will continue to work with other inspection entities such as local inspection officials, other government agencies, Minnesota Housing staff etc.,

to share inspection information. Also, we will accept HRA HQS inspections done in the same year as our review. If inspected by Minnesota Housing Tax Credit Compliance staff, inspection will be pursuant to Uniform Physical Conditions Standards. Minnesota Housing reserves the right to conduct a review of any building after serving appropriate notice and to examine all records pertaining to rental of tax credit units. Minnesota Housing may perform a review at least through the end of the Extended Use Period of the buildings in the project.

4. Annual Monitoring Fees. The amount of annual compliance monitoring fees is $15 per unit since inspections are less frequent and are done on a smaller number of units. The agency reserves the right to adjust the fee due to changing circumstances. Fees are due at the same time as the Annual Certification and Summary Report.

5. Properties with HUD or Rural Development. No Housing Tax Credit inspections or fees will be required for properties with project-based Section 8, Rural Development or other HUD programs since these properties are already subject to inspections and consequences under those programs are in place. Owners will only be required to submit the Owner's Certification of Continued Monitoring of Federal Program (HTC 12(Y15A)), indicating whether or not the property is subject to monitoring for such federal programs and identifying the date of the most recent inspection review. This certification is due on February 15th or the next business day. If a property is no longer subject to monitoring for HUD and/or Rural Development programs, then the property must be placed back on the Housing Tax Credit monitoring schedule. If the development is placed back on the Housing Tax Credit monitoring schedule, Minnesota Housing will resume all compliance monitoring activities, including charging a fee for monitoring. The timing of the next review will be based on the last inspection conducted by Rural Development, HUD or its Contract Administrator.

6. Transfer of Ownership or Ownership Interest. A transfer agreement is required in the event of a transfer of ownership or ownership interest. Such transfer agreement will put the new owner or partner on notice that it is subject to the terms of the Declaration including all compliance restrictions and annual compliance monitoring. Documentation of signatory authorization for the new owner or partner may be requested. Owners contemplating transfers of ownership or ownership interest should notify Minnesota Housing and request a copy of the appropriate transfer agreement.

7. Expiration or Termination of Extended Use Period. During the 3-year period after the Declaration has expired or terminated pursuant to IRC Section 42(h)(6)(E)(ii), owners are required to annually submit the HTC 13 listing all low-income households that occupied a unit at the end of the term of the Declaration, the respective tenant-paid rent, utility allowance, and move-out date, if applicable, along with a certification that no low-income residents have been evicted or displaced for other than good cause. This report and certification will be due on February 15th or the next business day. No

monitoring fees will be due during this 3-year period and Minnesota Housing is not required to perform inspections.

The Declaration of Land Use Restrictive Covenants allows for an amendment by written agreement between Minnesota Housing and the owner. An amendment to the Declaration may be negotiated in the event a property suffers from a decline in market conditions that is not expected to improve and subsequent vacancies compromise the economic viability of the property. Owner must demonstrate that reasonable efforts have been made to meet all compliance requirements. A change in applicable fraction, rent limits or other terms may be negotiated with Minnesota Housing in order to preserve as many low-income units as possible, but still protect the economic viability of a property.

E. Consequences of Noncompliance During the Extended Use Period

The following are the procedures for and consequence(s) of noncompliance:

1. All properties whose Compliance Period has expired and are subject to the requirements of the Extended Use Period will be listed on Minnesota Housing's web site categorized in either "Good Standing" or "Not in Good Standing".

2. If an owner fails to comply with the monitoring requirements and/or terms of the Declaration, Minnesota Housing will issue a Notice of Noncompliance and recommendations for correction similar to what is issued during the Compliance Period. All owners will be given a period of time not to exceed 90 days with which to clarify or correct noncompliance and report to Minnesota Housing that all corrections have been made. An extension of an additional 90 days may be granted, with good cause. If a property has one or more compliance violations, but the owner is making a good faith effort to correct within a reasonable time then the property can be considered in Good Standing. If the violation(s) cannot be corrected within the 90-day correction period (or within the 90-day extension, if granted) Minnesota Housing may request that the owner and/or management agent formulate a plan and reasonable timeline to bring the violation(s) back into compliance and advise Minnesota Housing in writing of such a plan. Owners will have demonstrated good faith efforts by carrying out the plan within the referenced timeline and the property will remain in Good Standing.

3. If an owner repeatedly delays or ignores requests for monitoring reviews, fails to submit annual certifications, reports and compliance monitoring fees, does not correct violations timely or according to the agreed-upon plan, where applicable, or otherwise chooses to ignore the compliance and monitoring requirements (serious and/or flagrant noncompliance) the following are consequences:
   a. The owner and management company are considered to be Not in Good Standing and Minnesota Housing's web site will be updated to reflect the change in status.
   b. A Report of Development Not in Good Standing, form HTC 31 will be issued for such serious and/or flagrant noncompliance. This report will be

sent to the owner and filed with the Minnesota Housing Development team. No further Minnesota Housing funds or tax credits will be awarded to the owner, its partners and/or proposed developments to be managed by the management company until the property is back in Good Standing. Once good faith efforts are demonstrated to the agency's satisfaction, the agency will reinstate the property, owner and management company in Good Standing and update the web site to reflect the change in status.

c. The agency and any interested party have the right to enforce specific performance of the Declaration through the court system.

Important: Owners and management agents must keep careful track of when a development, and in some cases certain buildings within a development, transition from the Compliance Period into the Extended Use Period. Premature implementation of the Extended Use Period compliance and monitoring guidelines may result in noncompliance with IRC Section 42 for which Minnesota Housing would be required to file IRS form 8823.

Minnesota Housing reserves the right to modify this Housing Tax Credit Compliance Manual including but not limited to the foregoing policy and procedure for compliance and monitoring during the Extended Use Period, as needed.

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Chapter 10 – Tax Credit Assistance Program (TCAP) and Section 1602 (Tax Credit Exchange) Program.

Background

The American Recovery and Reinvestment Act of 2009 established two new programs providing state allocating agencies, including Minnesota Housing, with tools to help certain Housing Credit-financed rental housing projects close financing gaps created by reduced credit pricing and lack of syndicator equity: the Tax Credit Assistance Program (TCAP), administered by HUD, and a program authorizing state allocating agencies to exchange Housing Credits for cash (the Section 1602 Program), administered by the U.S. Department of Treasury (Treasury). TCAP funds may only be awarded to projects where there is an allocation of Housing Tax Credits. Section 1602 funds may be awarded to projects with or without Housing Tax Credits.

A. Compliance and Asset Management

Properties funded with TCAP and/or Section 1602 Program funds must comply with Minnesota Housing loan documents and with IRC Section 42 for the full term of the compliance and extended use periods, as evidenced by a Declaration of Land Use Restrictive Covenants. Additionally, during the compliance and extended use period, both programs are subject to asset management oversight by Minnesota Housing.

B. Monitoring and Reporting

Minnesota Housing will monitor compliance with TCAP and the Section 1602 Program in the same manner as the Housing Tax Credit Program as described in this manual. However, Section 1602 will require reporting violations to Treasury in a form and manner required by Treasury, and not to IRS on form 8823. Asset management includes but is not limited to lease-up compliance monitoring, operational and financial reporting, and other monitoring pursuant to a Regulatory Agreement with Minnesota Housing.

Questions regarding asset management activities should be directed to Gayle Rusco, 651-296-8093 or gayle.rusco@state.mn.us.