



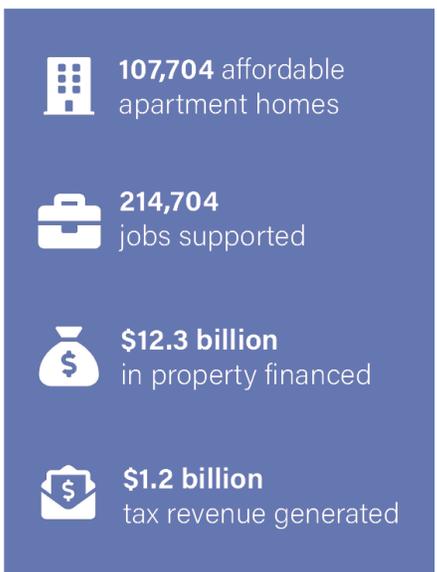
The Role of the Low-Income Housing Tax Credit in Preserving Affordability

Background

The Low-Income Housing Tax Credit (LIHTC) is the largest federal funding program for expanding and preserving the stock of affordable rental housing in the United States. Beyond increasing affordable options, the housing produced through the LIHTC program provides social and economic benefits for North Carolinians, from better educational outcomes and improved health care access to increased economic opportunities and community investment.ⁱ

Since 1987, LIHTC has helped create and preserve more than 107,700 affordable apartment homes in 2,502 properties across North Carolina.ⁱⁱ In the last five years alone, the Agency has awarded credits to create an average of 5,400 units annually. The credit allows developers and investors to claim a deduction on their federal tax liability for a 10-year period in exchange for keeping rents at levels affordable for low-income households. Although early properties were only subject to a 15-year affordability period, properties built after 1989 must remain affordable for 30 years once they are placed in service.ⁱⁱⁱ At the end of this 30-year period, properties may remain affordable to low-income residents—unsubsidized or due to extended affordability requirements from recapitalization (including with a new round of tax credits)—or reposition as market-rate housing. As the LIHTC program matures and the 30-year affordability requirements for the early generation of LIHTC-funded properties approach their expiration, understanding this pivotal transition becomes increasingly important.

Figure 1 | Economic Impact of LIHTC in NC (1987-June 2022)



Potential Outcomes for Year 30

Research has found that several factors influence whether a LIHTC property continues to operate as affordable housing or converts to market-rate housing. Market pressures can provide an economic incentive for LIHTC properties to reposition at market-rate once affordability requirements expire, especially if located in neighborhoods where owners might be able to charge rents greater than the LIHTC maximum. On the other hand, properties located in lower cost communities—where unrestricted rents are similar to LIHTC rent limits—could continue to provide affordable rents, despite the absence of LIHTC affordability requirements.^{iv} Other considerations include: properties approaching the end of their affordability requirements often have significant need for repair, renovation and refinancing and can be at risk of physical deterioration without additional investment;^v LIHTC properties with a mission-driven owner are more likely to remain affordable beyond the regulatory requirements because it is their mission to do so;^{vi} and other affordability requirements from leveraging additional forms of public financing through rental, operating and other assistance may extend a property’s affordability beyond the LIHTC program’s 30-year period.^{vii} For example, a number

of existing LIHTC properties in North Carolina have recapitalized with a new allocation of tax credits, which triggers a new 30-year affordability period.

Although annual LIHTC production will offset losses, the net increase in apartments from year to year will be smaller due to those with expiring requirements. Since the program’s inception, North Carolina has seen approximately 10% of LIHTC apartments (or 10,500 units in 1,012 developments) leave the program due to expiring affordability requirements or early exits from the program due to foreclosures and qualified contract, a regulated early sale option.^{viii} Within the next decade, an additional 15,600 affordable apartment homes across 316 properties (16% of the active LIHTC portfolio) could lose LIHTC-guaranteed affordability if no affordability requirements remain from additional subsidies or no additional preservation efforts are made (see Figure 2 below). As shown in Figure 3, the majority of these apartments are in Metro counties (47%) with the highest concentrations in Wake (13%), Mecklenburg (9%) and Forsyth (8%) counties. By contrast, 21% of apartments are in Central counties, 21% in Eastern counties and 9% in Western counties.^{ix} Most properties (69%) have for-profit owners, while 31% have nonprofit owners. The majority of properties (69%) have no additional HUD or USDA financing that could extend affordability but may have other provisions, like a local government loan, that could require a longer affordability period. As described in the following section, these developments could be candidates for a new allocation of LIHTC rehabilitation/preservation credits.

Figure 2 | Affordable Units with Expiring LIHTC Affordability Requirements, 2022-2031

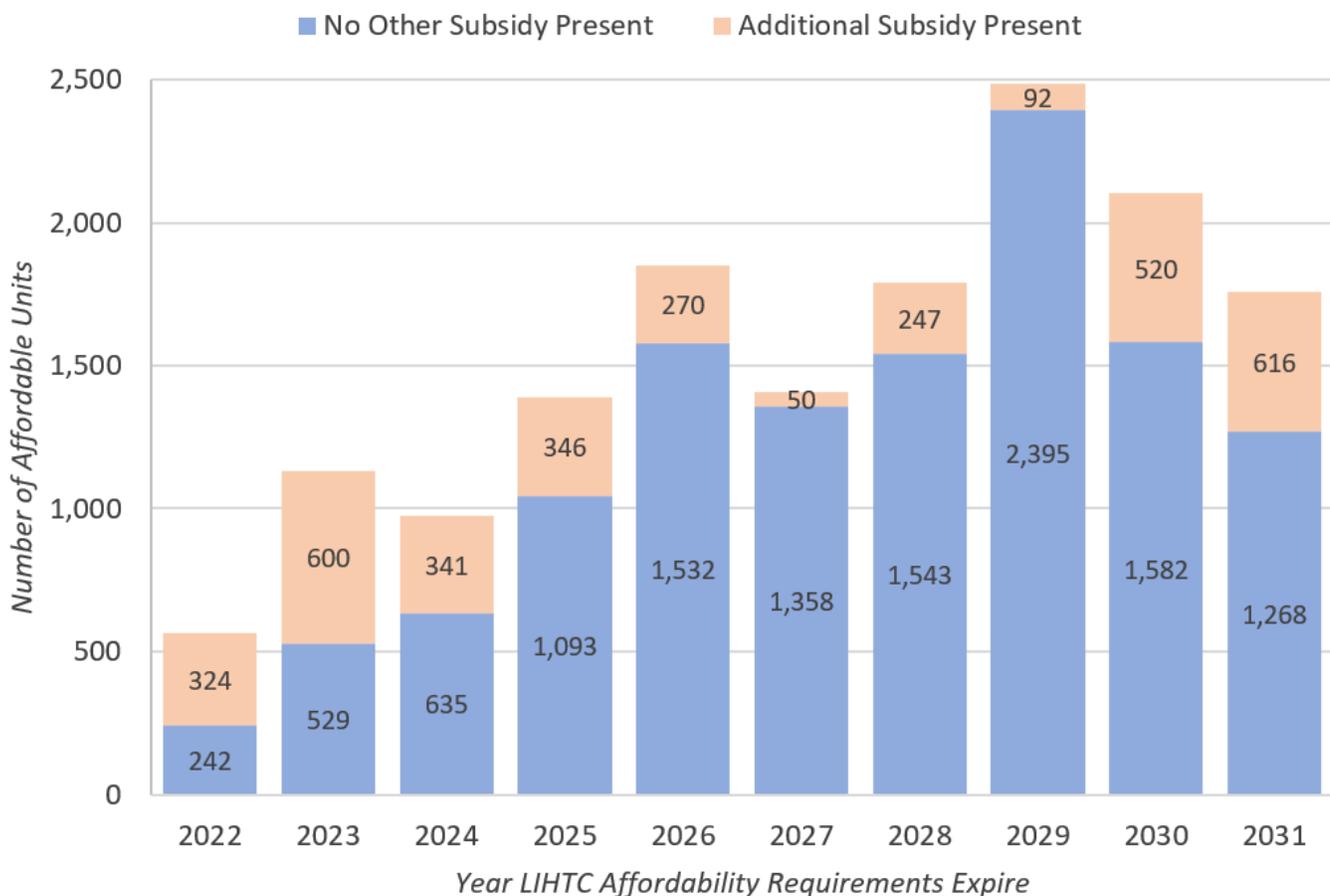
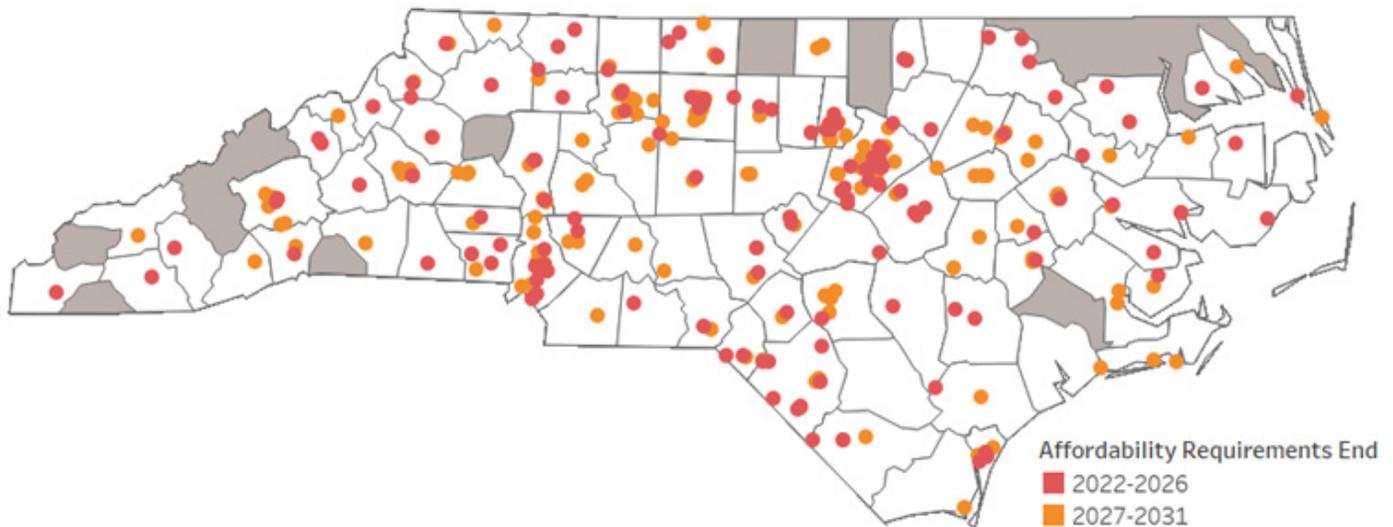


Figure 3 | Properties with Expiring Affordability Requirements, 2022-2031



LIHTC as a Tool for Recapitalization and Preservation

In North Carolina, LIHTC is used not only to produce new affordable housing but also to preserve existing housing, including tax credit properties in need of recapitalization. Since the program's inception, 19% of LIHTC properties have been rehabilitation projects. Preserving existing affordable units is often less costly than new construction, promotes stability for tenants and can increase access to higher opportunity neighborhoods.^x

Many housing finance agencies, including in North Carolina, incentivize preservation in their Qualified Allocation Plans (QAPs), which outline the selection criteria for tax credit allocations. Since 2003, North Carolina has set aside a portion of its competitive tax credit allocations for preservation and rehabilitation activities—currently, 10% is set aside for such rehabilitation/preservation.^{xi} The rehabilitation set-aside can be leveraged to meet a range of preservation needs from recapitalization of previously awarded LIHTC developments to redevelopment of public housing to preservation of naturally occurring affordable housing. Since 2007, 71 properties with 4,300 affordable units have recapitalized with a new allocation of tax credits.^{xii}

Conclusion

Housing finance agencies have some regulatory flexibility and administrative power to incentivize preservation of existing properties. The North Carolina Housing Finance Agency (the Agency) has taken proactive steps to promote preservation by setting aside 10% of its tax credit allocation for rehabilitation, limiting the use of the qualified contract process, which is one of the early exit strategies for owners, and preserving previously awarded LIHTC properties with a new reservation of tax credits. The Agency is also committed to continued analysis of LIHTC data to identify properties where affordability requirements are expiring and to help local and state stakeholders better understand preservation needs. This research brief provides an initial window into the existing tax credit portfolio. Additional research to better understand which risk factors most impact North Carolina properties, what resources already exist for preservation and how to best engage property owners and tenants will inform ongoing preservation strategies.

Appendix A | Affordable Units and Properties at Risk of Losing LIHTC Affordability Requirements in North Carolina

Risk of Losing LIHTC Affordability Requirement	Presence of Additional Subsidies	# of LIHTC Properties	# of LIHTC Units	% of LIHTC Portfolio
LIHTC Requirements Expire in <1 Year	No Other Subsidy Present	8	242	0.2%
	Additional Subsidy Present	8	324	0.3%
LIHTC Requirements Expire in 1-5 Years	No Other Subsidy Present	69	3,789	4%
	Additional Subsidy Present	56	1,557	2%
LIHTC Requirements Expire in 5-10 Years	No Other Subsidy Present	140	8,146	8%
	Additional Subsidy Present	35	1,525	2%
LIHTC Requirements Extend Beyond 10 Years	No Other Subsidy Present	830	58,121	60%
	Additional Subsidy Present	344	23,489	24%

References and Notes

ⁱ NYU Furman Center. (2017). The Effects of the Low-Income Housing Tax Credit. Available from: https://furmancenter.org/files/NYUFurmanCenterLIHTC_May2017.pdf.

ⁱⁱ This figure only includes affordable housing developments and units awarded LIHTCs by the North Carolina Housing Finance Agency. Some of the properties captured in this figure are still under construction. In total, the Agency has help create more than 116,000 affordable rental units, inclusive of LIHTC and other Agency programs.

ⁱⁱⁱ LIHTC projects allocated credits prior to 1990 were subject to a minimum 15-year affordability period. The extended use period was established by Revenue Reconciliation Act of 1989.

^{iv} See, for example: NLIHC and PAHRC. (2018). "Balancing Priorities: Preservation and Neighborhood Opportunity in the Low-Income Housing Tax Credit Program Beyond Year 30." Available from: <https://nlihc.org/sites/default/files/Balancing-Priorities.pdf>; Khadduri, J., Cilmaco, C. & Burnett, K. (2012). "What happens to Low-Income Housing Tax Credit properties at year 15 and beyond?" Office of Policy Development and Research, U.S. Department of Housing and Urban Development. Available from: https://www.huduser.gov/portal/publications/what_happens_lihtc_v2.pdf.

^v PAHRC and NLIHC. (2021) "2021 Picture of Preservation." Available from: https://preservationdatabase.org/wp-content/uploads/2021/10/NHPD_2021Report.pdf.

^{vi} Meléndez, E., Schwartz, A.F., & Montrichard, A.D. (2008). Year 15 and Preservation of Tax-Credit Housing for Low-Income Households: An Assessment of Risk. *Housing Studies*, 23, 67 - 87.

^{vii} Common forms of public financing that may extend a property's affordability beyond 30 years include Project Based Section 8, Rural Housing Service Section 515 loans, or other state and local funds.

^{viii} This figure only represents the number of LIHTC-awarded properties with expired affordability requirements or formal owner opt-outs. North Carolina has only had three properties go through qualified contract and has required potential developer and owners to forfeit the right to a qualified contract. Not all properties in the extended use period are being actively monitored by the IRS or the Agency and therefore could have converted to market-rate.

^{ix} Definitions of geography correspond with regions listed in the 2022 NC Qualified Allocation Plan Section II.B.1

^x Reina, Vincent. (2018). "The Preservation of Subsidized Housing: What We Know and Need to Know. Lincoln Institute of Land Policy." Available from: https://www.lincolninst.edu/sites/default/files/pubfiles/reina_wp18vr1.pdf.

^{xi} Adaptive re-use projects, entirely vacant residential buildings, and proposals to increase and substantially reconfigure residential units are considered new construction.

^{xii} The first LIHTC developments reached the end of their affordability periods in 2003; 2007 was the earliest year for which resyndication data was available.



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