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The Aging of Colorado and the Need for the Low Income Housing Tax Credit Program

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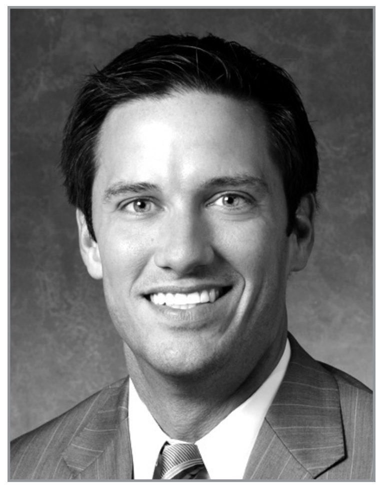

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According to the 2010 U.S. Census, Colorado is currently home to 549,625 seniors aged 65 and older. Colorado's 65+ population is projected to increase by 61% to 891,970 between 2010 and 2020, and by 2030, seniors aged 65 and older are projected to make up 1.24 million of Colorado's total population. Given that most seniors live on fixed incomes (as of December 2011, the average monthly Social Security payment for retired workers in Colorado was $1,215.12), this significant increase in Colorado's senior population will result in the need for more affordable housing for seniors.

The Low Income Housing Tax Credit (LIHTC) program helps address this need for the development of affordable housing. Created by the Tax Reform Act of 1986, the LIHTC program does not provide direct monies to developers of affordable housing, but instead provides tax benefits in the form of a dollar for dollar reduction of federal tax liability. The equity obtained by developers from the syndication of the credits reduces the amount of debt needed to finance the project, which savings are passed along to tenants in the form of affordable rents.

There are two types of tax credits – the 9% credit and the 4% credit. The 9% and 4% credits are designed to yield tax credits over a 10-year period equal to 70% and 30%, respectively, of the present value of eligible costs of a project. The use of the 9% credit is limited to the new construction or substantial rehabilitation of residential rental projects that are not also financed with the proceeds of tax-exempt bonds, whereas the 4% credit can be used for the acquisition of existing buildings undergoing substantial rehabilitation or on tax-exempt bond projects.

A LIHTC project must satisfy certain requirements pertaining to tenant eligibility and occupancy for a minimum of 30 years (15-year compliance period plus a 15-year extended-use period). In addition to being suitable for residential occupancy, a project must satisfy a minimum set-aside test and a rent restriction test. Under the minimum set-aside test (also referred to as the 20/50 or 40/60 test), either: a) 20% or more of the units in a project must be rented to tenants with incomes at or below 50% of the Area Median Income (AMI); or b) 40% or more of the units in a project must be rented to tenants with incomes at or below 60% of AMI. Rents cannot exceed 30% of the tenant's income, as reduced by a utility allowance and adjusted for family size. For 2012, the applicable LIHTC income and rent limits for a one person household renting a one-bedroom apartment in the Denver metro area are as follows: 50% of AMI equal to $27,800 with monthly rent not to exceed $744 and 60% of AMI equal to $33,360 with monthly rent not to exceed $893.

Although LIHTCs are federal credits, the federal government has assigned responsibility for allocating LIHTCs to state housing agencies. Each state must develop and adopt an annual Qualified Allocation Plan (QAP) setting forth guidelines and criteria to evaluate LIHTC applications. In addition to the mandatory LIHTC program requirements, each state may impose additional requirements on recipients as well as tailor its LIHTC application to encourage the development of certain types of projects (e.g., special services, senior, green).

In Colorado, all 9% credits and those 4% credits available for the acquisition of existing buildings undergoing substantial rehabilitation are allocated by the Colorado Housing and Finance Authority (CHFA) through a competitive application process and are awarded in two annual rounds. In 2012, Colorado received an estimated $13 million in tax credits. Colorado's QAP has consistently identified projects targeting seniors as a priority in awarding tax credit allocations, and in 2012, four of the fourteen projects awarded tax credit allocations target seniors.

Once the credits are awarded, developers monetize the credits by partnering with an investor. The investor is typically either a syndicator (i.e., investors who package credits together to sell to other investors) or direct investor (e.g., banks, business corporations or insurance companies) that makes a capital contribution to the partnership in exchange for an allocation of credits. In addition to receiving a 10-year stream of credits, the investor also receives a proportionate allocation of the project's profits, losses and depreciation. As the general partner, the developer controls the partnership and oversees the project's management throughout the 15-year compliance period. Investing in a LIHTC project is risky due to the possibility that a project may fail to comply with the LIHTC program requirements during the compliance period resulting in a recapture of any previously claimed tax credits, and therefore, similar to non-tax credit projects, an investor will evaluate the project's cost, projected financial performance and the developer's experience and resources in determining the project's likelihood of success.

The need for affordable housing for Colorado seniors is great and will continue to grow given its burgeoning senior population and the future uncertainty of social security and other sources of retirement funds. For the past 25 years, the LIHTC program has enabled developers to produce high-quality housing affordable to low and moderate income households despite ever-increasing development and construction costs and will continue to be an essential program in the future in helping Colorado meet the challenge of providing quality affordable housing for its seniors.