Year 15 Exits of Low Income Housing Tax Credit Properties: Homeownership Conversion Potential of Small-Scale Units in North Carolina

by

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EXECUTIVE SUMMARY

The Low Income Housing Tax Credit (LIHTC) program is a federal subsidy program designed to increase private development of rental housing that is affordable to the low-income population. Since low-income housing produces small cash flows, the government supplies additional benefit in the form of tax credits, a dollar-for-dollar reduction in the amount of taxes owed. Tax credits are also a commodity, since they can be sold or traded, making them a fairly secure source of revenue. As such, the LIHTC program has grown in both popularity and complexity.

Currently, developers of a LIHTC project must enter into a legal agreement attached to the property, requiring affordable rents for a duration of 30 years. The development entity must also remain the owner for a minimum of 15 years, else the IRS could revoke some portion of the tax credits awarded to them. Difficulties can arise after 15 years if the development entity wishes to sell the property, since the property remains subject to affordability restrictions regardless of a transfer of ownership. Several options for "exiting" the property exist, but the conditions which influence the exit approach and the preservation of both affordability and structural maintenance of the property remain unclear.

This paper looks at all single-family LIHTC properties within the State of North Carolina in an attempt to evaluate the potential of a particular exit strategy: selling the property to the low-income tenant. Owners and tenants of these properties were contacted via a mail survey to solicit their interest in selling or buying, respectively, and to ask for their general feedback and their future plans in relation to their unit. Income qualifications of the tenants were also evaluated to determine their ability to afford a mortgage payment based on their current rents using a mortgage structure based on several products and services offered to first-time homebuyers through the North Carolina Housing Finance Agency (HFA).

The results were mixed. A significant number of property owners responded that they were interested in exiting their property, and would consider selling it to their existing tenant or a future tenant. Several questions were raised by owners who were ready to begin that process. Unfortunately, response rates from tenants were extremely low and an overall analysis of tenants' finances indicates that many may be unlikely to obtain a mortgage for an amount as high as their property's tax value.

The homeownership conversion policy in Missouri was reviewed to provide a basis for consideration of how the conversion process could be structured and regulated in North Carolina. Missouri has created a conversion process that is sequentially detailed and provides ample protections to tenants, both of which are designed to maintain the affordability of LIHTC housing in that state. North Carolina does not require similar legal agreements with their LIHTC owners as Missouri does, and so their legal ability to regulate a homeownership conversion process is much more limited.

Regulation of any future homeownership conversions, however, is dependent upon each state's priorities in preserving the LIHTC stock over a long timeframe. The necessity of doing so may be limited if the stock of affordable housing is relatively stable, or if the preservation of affordable housing could be better served by alternative priorities. The expense of developing a conversion policy can also be time-consuming and unnecessary if the resulting conversions are limited in number. Some states, including North Carolina, no longer award tax credits to small-scale properties, and thus the proportion of this type of LIHTC unit is small and diminishing. And for this small subset of properties, homeownership conversion is only one exit option, although it is an option well-suited for this property type. Even in Missouri, only a "handful" of small-scale properties have converted thus far (Giffin).

As a result of this analysis, the North Carolina HFA has issued a memo to all existing owners of small-scale properties, informing them of its willingness to work with owners interested in homeownership conversion. The memo is significantly less complex than the policy document published in Missouri, and encourages interested owners to contact the Agency. North Carolina HFA staff members will need to work individually with owners on a case-by-case basis to encourage a fair and feasible exit strategy.

Low Income Housing Tax Credit Program - Overview

The Low Income Housing Tax Credit (LIHTC) program is a federal program aimed at encouraging the development of affordable[1] housing for the low-income population. Since its inception, the LIHTC program has become "the primary engine for the creation of affordable housing in the United States" (Beesemyer & Falk 1) and currently constitutes the "largest source of federal subsidy for adding new or rehabilitated rental housing units to the affordable housing stock in the U.S." (Gustafson forward). Nationwide, the program has created over 1 million units as of 2001 (ibid).

The program is an indirect subsidy program in that the government does not provide any monetary contribution directly into the construction of the unit(s). Instead, they allocate federal tax credits to the investors in the LIHTC projects; the credits can significantly offset their federal taxes due to the government. Tax credits are a dollar-for-dollar reduction in the amount of taxes due. In return for these credits, the investors must agree to limits on both the rents and incomes of their tenants over a period of at least fifteen years.

The Tax Reform Act of 1986 was a sweeping piece of legislation that, among other changes affecting the tax code, enhanced the home mortgage interest deduction incentive for home-ownership. Concern that investment in rental housing, and thus housing for the low-income population, could stagnate as a result, Congress added the LIHTC program to provide balance. By providing an incentive for the private market to invest in the development of low-income affordable housing, the LIHTC program is indicative of a general policy shift away from government provision of housing for low-income households in favor of private market participation.

Each year, the Internal Revenue Service allocates tax credits to each state based on their population. In 2007, this amount was equal to $1.95 per capita. North Carolina, therefore, with a 2006 population of 8.8 million per the U.S. Census would have received approximately $17 million worth of tax credits.[2] Each state must designate a state agency to administer the program; in North Carolina, this responsibility has been given to the Housing Finance Agency (HFA). The LIHTC program has grown in popularity such that developers of prospective LIHTC properties must now participate in a competitive application process.

The process of developing a LIHTC unit typically begins with a real estate developer, who identifies a potential LIHTC project and begins the process of acquiring site control and performing due diligence. Along with an equity-contributing investor, the developer generally creates either a limited partnership, or a Limited Liability Corporation (LLC) for the purpose of pursuing the development. Within the partnership, the developer is the General Partner (GP), and the equity investor is the Limited Partner (LP). The developer/GP is in charge of developing the project, leasing the property, and managing

[1] To be "affordable" residents may not pay any more than 30% of their income towards rent, including utilities.
[2] In 2007, the NC Housing Finance Agency awarded a total of $17,255,319 in tax credits.

operations. The investor/LP has limited, if any, involvement in project operations; they contribute equity financing and in return, receive the profits, losses, and/or tax credits generated by the property.

Developers apply to their state's Housing Finance Agency (HFA), or other similarly designated organization, for a tax credit allocation, which is based on the eligible capital budget of the project. Competing applications are evaluated on criteria specified by each state's Qualified Allocation Plan (QAP), a yearly document produced by the HFA that details selection criteria and application requirements. Within the QAP, states may indicate preferences for a wide variety of development characteristics, such as the targeted population (elderly, disabled, families, etc.), and professional credentials of the partnership, such as the experience level of the development team.

Tax credits awarded to approved projects are based on the eligible portion of the capital budget – 9% annually over 10 years for new construction, and or 4% annually over 10 years for acquisition and light rehabilitation (although the exact percentage fluctuates). The eligible portion of the capital budget (i.e. the total cost of development) does not include land costs, permanent financing costs, rent reserves or marketing costs. Therefore, if the current credit rate for new construction is 7.95% for a new construction LIHTC project with a $2.7 million eligible basis, the investors will receive approximately $2.15 million (or 80% of the eligible basis) in tax credits over a ten year period.

As currently structured, the LIHTC program requires that properties must remain affordable for a total of 30 years, but legislation includes a provision for investors to sell their interest in the property after 15 years (often referred to as the initial 15 year compliance period), since all of the tax benefits will have been realized by this time. After 30 years, the property "exits" the LIHTC program and the investor may be able to increase rents depending on what the market will bear. Government officials and affordable housing advocates are justifiably concerned about what happens to affordability when a property exits the program, since it could result in a loss of affordable rental housing units, and has the potential to displace low-income residents who are afforded limited protections. The problems presented by the mortality rates of LIHTC units over time have led policy makers to pursue options for encouraging the preservation of the LIHTC housing stock.

The Case for Preserving Low Income Housing

The need for affordable housing in the United States is well documented. According to the North Carolina HFA, 48% of North Carolina's low-income population paid more than 30% of their household income towards housing[3] (State Housing). Despite the success of the LIHTC program in placing new units on the market, production cannot keep up with demand. In 2004, the North Carolina HFA received 155 applications for $54 million in tax credits, which was over three times the amount of credits available (State and Local). Therefore, it is important to facilitate the preservation of existing affordable units in

[3] The low-income population is defined as those households that earn 80% or less of the state's median household income.

addition to production. Since 2002, when the first generation of LIHTC properties began to exit the program, more attention has been paid to what happens to affordable properties once they are freed from their affordability restrictions.

The maintenance of affordable housing units has been a concern of the federal government as long as there has been government subsidy of housing production. In 1986 (the same year that the LIHTC program was created), the federal government passed the Emergency Low-Income Housing Preservation Act (ELIHPA) in an attempt to preserve affordable housing units created under other federal housing programs, Section 515 and 514. In 1990, ELIHPA was succeeded by the Low Income Housing Preservation and Resident Homeownership Act (LIHPRHA). Both sought to prevent market-rate conversion by prohibiting property owners from pre-paying their mortgage, which would most likely result from a sale of the property. Since the cost of maintaining the property as affordable was generally greater than the benefits received from the program under which the structure was built, the federal government offered compensatory financial incentives to investors in exchange for extended affordability restrictions (Affordable).

While in effect, the ELIHPA and LIHPRHA programs proved successful at preserving HUD-sponsored affordable housing, although it required significant federal investment. In California, HUD paid over $500 million to project owners and investors, "covering nearly 100 percent of all preservation costs" (Affordable 1-4).

Although HUD is heavily involved with the LIHTC program, it is administered in a decentralized manner through both the Department of the Treasury's Internal Revenue Service and each state's Housing Finance Agency, and thus has not been affected by steps taken to preserve HUD-sponsored housing. Although many decentralized efforts have strived towards preserving LIHTC units, it should be noted that affordability of government-sponsored housing has generally been preserved through the intervention of the government, through regulation of new units coming online, or financial incentives to preserve existing units. Thus far, the LIHTC program has proven to be successful at leveraging private investment in the creation of affordable housing, but has only recently begun to observe how these units exit the program, and whether or not there is a role for the private market to play in preservation.

Have Affordable Properties Converted to Market Rate?

The first generation of LIHTC properties, placed into service between 1986 and 1987, reached the end of their 15 year compliance period (Y15) in 2002. At this time, the investors and their properties were freed from restrictions prescribed through the LIHTC program. A report issued in 2001 by the California Housing Partnership Corporation cited concern that 4,529 units, or 30% of the State of California's first generation LIHTC stock, was at "high risk" for conversion to market-rate units. These units were deemed high risk because: 1) they lacked additional restrictions from programs other than the LIHTC program, 2) their developers were for-profit, and 3) they were located in areas with strong property value appreciation (Beesemyer and Falk iv.).

An article in Multi-Housing News in 2003 reported that relatively few properties reaching Y15 on Dec 31st, 2002 converted to market-rate, citing the poor demand for housing in many of the markets where LIHTC properties were located (Foong).

The Local Initiative Support Corporation (LISC) cites that, as of 2006, the "majority of year 15 transitions so far have been 'rollovers,' where the sponsoring general partner, in most cases the [local non-profit Community Development Corporation], has assumed existing debt and simply continued operating [the property], possibly at a loss. Approximately 10% have needed to resyndicate with new tax credits to continue as affordable housing… A very small percentage (approximately 3%) have become market rate projects" (Turnock 5).

Beginning in 1990, additional restrictions were put in place to ensure continued affordability after Y15, but it is difficult to determine if significant levels of market conversion has occurred since 2002. Administration of the LIHTC program is one of many responsibilities of state HFAs, and up to this point, most effort has been invested in adjusting the application and construction process. The process of monitoring and facilitating the exit process will require a significant effort for which HFAs may not have adequate staffing. For this reason, there is very little data available on what has happened to LIHTC units after Y15, preferred exit strategies, their impact on tenants, and determining factors.

Factors Affecting Conversion

Affordability Restrictions

LIHTC properties often require more than one government program to finance the development and many will attach their own affordability restrictions to the development. Public funds, such as HOME funds or Farmer's Home Administration 515 mortgages may contain affordability restrictions up to 20 years or even 50 years, respectively. When investors seek to refinance their mortgages on LIHTC properties, government agencies have a second opportunity to attach extended affordability periods to their attractive financing offer. Generally, the greater the number of public subsidies that are utilized by a LIHTC property, the longer the affordability period is likely to extend.

California's first generation LIHTC housing portfolio is illustrative of the importance of restrictions placed on LIHTC properties by other financing sources. Of the 15,535 properties in California's first generation LIHTC portfolio, 65% received some form of additional government subsidy. The below table lists the various government subsidies, restrictions that may have been attached to the subsidy, and the number of properties that received that subsidy.

Number of Units	Subsidy
1,598	California's Department of Housing & Community Development financing (through four different programs) includes a 55 year affordability restriction.
6,052	California's State Tax Credit Program includes a 30 year affordability restriction.
2,952	Farmer's Home Administration's Section 515 financing does not include any affordability restrictions by itself, but is often coupled with additional financing that does.
1,557	Financed by local municipalities or non-profits. There is no readily available data on how many of these financing agreements include affordability restrictions.

Source: Beesemyer, 10-11.

Partnership Agreements

Within the legal arrangements establishing the partnership between the General and Limited Partner(s), a provision may be added that gives the General Partner the right of first refusal in purchasing the Limited Partner's share of the property. This is a likely scenario when the GP is a Community Development Corporation (CDC) or other non-profit entity that has a social, as well as financial agenda. LISC has even published a guide for assisting CDCs with navigating the purchase of the LP's shares, or even the entire project (Turnock). In the case that a non-profit GP purchases the project from the LP, the property is likely to remain affordable.

Investor Motivations

As mentioned above, non-profit developers are more likely to maintain the affordability of their projects, even if it involves a financial loss. HFAs are currently required to award at least 10% of their tax credits to non-profits, although many exceed this rate. There is some concern that non-profits are not as efficient as the private market in constructing and operating rental housing, yet HFAs have good reason to trust in non-profits to see the bigger picture. John Brandenburg, the Managing Director of Asset Management at Enterprise Social Investment Corp. and a frequent contributor to LIHTC literature states "by Year 15, most investors are looking for exit strategies. Nonprofit developers, however, seek solutions to sustain affordability." (Brandenburg 1)

Financial Considerations

Perhaps the most important factor in determining the future affordability of a LIHTC property is the property's financial situation, which is driven primarily by market conditions affecting the properties value. LIHTC developments located in areas where the property values have increased are at much higher risk of market conversion than those located in areas with low property values. A higher market value also increases the investor's ability to pay off any remaining mortgage on the property and other expenses associated with the disposition of investment real estate. This may indicate why California anticipated such a large loss of affordable housing beginning in 2002. Relative to the rest of the United States, California has a robust real estate market, and is at a disadvantage in mitigating the loss of affordable units. A separate analysis of local real estate markets and neighborhood effects on LIHTC properties is outside the scope of this paper, but could prove to be insightful in evaluating market conversion risk.

Exit Taxes

In their periodic technical assistance newsletter, the Community Affordable Housing Equity Corp. (CAHEC), a non-profit syndicator of tax credits in North Carolina, identifies exit taxes as the "single largest barrier to the preservation of affordable housing" (Duffley 1). When selling a LIHTC property, the investor is subject to additional income tax, popularly called an exit tax, if the value of the tax credits received, paid-out dividends (if any), and proceeds from the sale of the property are greater than the amount originally invested in the property. These taxes are enforced even if the investor receives no net cash proceeds from the sale of the property, which can occur if the sales amount is used to pay off an outstanding mortgage balance, or if the property is donated to a non-profit organization. CAHEC identifies this as a disincentive for an investor to exit a property unless the sales price of the property is large enough to cover any outstanding mortgage and the exit taxes (ibid).

Second Generation LIHTC Properties

Extended Use Period

In 1989, Congress passed the Omnibus Reconciliation Act, which included several provisions affecting the LIHTC program. A measure was included to preserve the affordability of LIHTC units for an additional 15 year "extended use period" while still allowing the investor to exit the property after Y15. Passage of the new Act was possible in part to increased demand for tax credits, which has reached and exceeded available supply. Beginning with projects placed into service in 1990, the new Act requires that LIHTC units remain affordable to their target population for a total of 30 years – 15 year initial compliance period after which the investor may sell, plus the new 15 year extended use period. The year 2006 was the first year in which this second generation of LIHTC properties completed their initial 15-year compliance period. These properties are considered to be much less susceptible to market-rate conversion than first generation properties.

For the first 15 years of a LIHTC property's life the investor must comply with regulations set forward within Section 42 of the IRS code. Any violations of this code can be met with tax penalties. The extended use period, however, is enforced only by a Land Use Restriction Agreement (LURA), a legal agreement between the state HFA and the investor when the LIHTC project was initially approved. Although a LURA refers in general to any legally binding land use agreement, a LURA signed as part of a LIHTC development should always include provisions that enforce affordability and tenant income restrictions for a total of 30 years from the date the building was placed in service. An investor may therefore sell their LIHTC unit after 15 years since compliance with Section 42 has presumably been met, but the restrictions set forth in the LURA must be met by any subsequent owner of that property within the 30 year time frame.

Enforcement of the LURA is a difficult task, however, that requires the HFA to monitor each property for compliance. The ability of HFAs to do so is dependent upon their available resources and therefore is likely to vary from state to state.

Qualified Contract

Since the ability of investors to sell their interest in a LIHTC property after Y15 is decreased due to the extended use period, the new legislation explicitly provides an additional (and potentially easier) opportunity to do so, by requiring state HFAs to allow for Qualified Contracts, a legal arrangement between the investor and the HFA that serves as an escape valve for the investor. Without providing more incentives to investors in exchange for the extended use period, they were provided with an allowance for their exit to avoid neglect and disinvestment of the properties.

Beginning in the property's 14th year, the investor may apply to the HFA for a Qualified Contract, indicating their desire to leave the program. Upon receiving an application for a qualified contract, the HFA must determine an asking price for the property (the contract price) and then find a buyer for that price who must also comply with any and all remaining restrictions on the property. If the HFA is unable to find a buyer within one year's time, then the entire property is freed from the restrictions associated with the extended use period; in effect the investor may sell the property or raise rents as they please.

For affordable housing advocates, the Qualified Contract (QC) presented an unknown in the affordability equation. The first state HFAs to address the QC provision only began structuring their policies as recently as 2005 (Wong). North Carolina was one of the earlier states to address the QC, which is detailed within each state's Qualified Allocation Plan. Since acquiring a QC requires an application process, some state HFAs have detailed cumbersome requirements on the part of the investor to receive one. For example, Minnesota's HFA requires that investors applying for a QC pay a $5,000 application fee, pay for submission materials, an appraisal, a market study and a rent comparability study (Wong).

North Carolina requires a minimum $1,050 processing and application fee, and may require a deposit up to $30,000 to be used for third party fees. The investor must also submit a multitude of paperwork, including annual tax returns filed over the holding period, annual financial statements over the holding period, loan documents for all debt used to finance the property, partnership agreements, waivers of any right-of-first refusals to purchase, a physical needs assessment, property appraisal, market study, title report, and a Phase I environmental assessment (NCHFA). The HFA asks for these documents in order to determine the asking price and for presentation to prospective buyers, yet the requirements can be burdensome to some investors.

As previously mentioned, the availability of data on exiting first generation LIHTC properties is limited. Inclusion of the extended use period and QC will make the exit process of second generation LIHTC properties fundamentally different from the first, and thus we have even more limited data on properties exited thus far, and what to expect in the future. We can presume that issues dealing with the physical deterioration of 15 year old properties and investors' motivations to maintain upkeep will be also surface.

LIHTC Exit Process - Overview

Because of the extended use period, owners of second generation LIHTC properties have a more difficult time disposing of their property than investors in first generation properties. The traditional methods employed by investors in disposing of their ownership share after Y15 include:

1) selling their ownership share to the General Partner, generally a non-profit entity who will continue to operate the property at affordable rates,
2) transferring or selling the property to a charitable organization or government entity who will continue to operate the property at affordable rates, or
3) selling to new investors who may apply for new (rehabilitation) tax credits, allowing them to upgrade the property and maintain affordability.

Selling to the General Partner

As mentioned previously, partnership agreements between General and Limited Partners in a LIHTC project may include a right of first refusal for the General Partner to buy-out the Limited Partner(s) after Y15. This is mostly likely when the GP is a non-profit organization.

Selling to a Charitable Organization

In 1990 congress passed additional legislation explicitly authorizing the inclusion of right-of-first refusal purchase clauses for non-profit organizations, tenant groups, or public agencies. In exchange for selling LIHTC properties to these types of groups at below-market rates, the investors are protected against certain tax liabilities. The legislation additionally set the minimum purchase price to be equal to a minimum amount equaling the outstanding debt attributable to the property plus taxes associated with the sale.

Resyndication: Four Percent Rehabilitation Tax Credits

In addition to new construction, the LIHTC program allows states to distribute tax credits to minor rehabilitation projects at a lower rate of approximately 30% of the eligible rehabilitation capital budget, or 4% on an annual basis over 10 years. When these credits are used to finance improvements to an existing LIHTC property, it is called resyndication.

The property, which will be at least 15 years old at the time of resyndication, will receive new tax credits in return for physical rehabilitation of the property, since most properties (market rate or affordable) are likely to need physical maintenance at this age. This option does allow the HFA to reset the affordability clock, requiring the now-standard 30 years of affordability. Given the high level of competition for a limited amount of tax credits, HFAs may be hesitant to promote this option, preferring instead to create new units unless they feel that the property is in danger of market conversion.

HFAs may be more inclined to use their tax credits for resyndication more often, however, given emerging concerns over affordability. In 2005, Texas's Qualified Allocation Plan sets aside 15% of its $40 million worth of tax credits to be used for rural housing at risk of converting to market-rate, and Massachusetts set aside 40% of its tax credit allocation for the preservation of affordable housing (including federally- and state-assisted affordable housing) (Wong 2-3).

In 2006, North Carolina's QAP set aside an amount of tax credits specifically for rehabilitation, equaling the lesser of 20% of the state's annual tax credits, or the amount required to rehabilitate 10 properties (State and Local Housing Preservation Initiatives).

Continue to Operate

Remaining the owner of a LIHTC unit does have some benefits since the restrictions set forth by Section 42 of the IRC are stricter than those set forth by the LURA alone. Unfortunately, there are also significant disadvantages in the low cash flows provided by rents, exhaustion of all tax credit benefits, and a potential need for rehabilitation of the aging structure.

Preservation Options

Any number of options exist for preserving the affordability of LIHTC properties. Most options involve various units of government offering favorable financing or refinancing terms in return for continued affordability restrictions or by acquiescing to non-profit or government agencies the right of first refusals to purchase the property (See Wong for various creative financing strategies).

Affordable Housing Trust Fund

On October 10, 2007, the House of Representatives passed the Affordable Housing Trust Act, which will create a national trust fund aimed at producing, rehabilitating and preserving affordable housing in the U.S. The measure has been described as "the biggest expansion of federal housing programs in over a decade" (House Passes Affordable Housing Trust Fund Act). The goal of the trust is to target 1.5 million affordable housing units over a 10 year period, by allocating its funds, under the direction of HUD, to the states (40% of annual allocation) and municipalities (60%). Initially the trust will distribute between $800 million and $1 billion on an annual basis. Similar to the LIHTC program, fund recipients must create an allocation plan to specify how the funds will by used, priority of usage, and all relevant application processes (H.R. 2895). The bill is currently circulating in the Senate, where it faces a less certain future.

Many states, including North Carolina, have already created state-wide housing trust funds. The trust fund provides North Carolina with a flexible source of funds that can be used towards a variety of means, including home ownership programs, new construction, rehabilitation, and more. Monies can be made available to applicants through loans, grants, and/or interest reduction. It has provided “the state’s largest source of funds for financing emergency repairs and accessibility modifications” for the elderly and disabled (North Carolina Housing Trust Fund Fact Sheet).

Housing trust funds can be flexible, and successful at leveraging private investment, yet require a large amount of dedicated public source of funds to create.

Affordable Housing Preservation Tax Relief Act

In December of 2000, Congress established the Bipartisan Millennial Housing Commission to “examine a variety of issues affecting the United States housing industry, including ways to increase the role of the private sector in providing affordable housing” (Duffley 1). Based on the findings of the Commission, which identified exit taxes due by the investor upon sale of a subsidized property as the primary barrier to preserving affordable housing, the Affordable Housing Preservation Tax Relief Act was introduced to Congress in 2003. Although it may seem unusual that facilitating the sale of a LIHTC unit would assist in preserving it, a sale may facilitate the transfer of the property to a “preservation purchaser,” such as a CDC. Furthermore, anticipation of exit taxes may increase a seller’s asking price, forestalling a sale, and potentially resulting in the physical depreciation of the property if neglected by an unmotivated owner.

The bill proposed to create a preservation tax credit, which would be made available to an owner of a government-subsidized affordable multi-housing development upon sale to a preservation entity. The bill was not passed in 2003, but has reemerged in early 2007, but has been stalled in committee.

This option is remarkably similar to the LIHTC program itself by providing a comparatively small subsidy of foregone taxes to each seller, and encourages the preservation of the property through a sale to an entity likely to maintain affordability indefinitely.

Conversion to Homeownership

The Internal Revenue Code (IRC) allows for homeownership conversion as a LIHTC exit strategy. Initially, the code was somewhat confusing in that it required owners of post-1989 LIHTC properties to keep rents affordable for a total of 30 years, yet also allowed owners to grant their tenant a right-of-first refusal to purchase the property after Y15. These were contradictory policies, however, since a tenant who purchases their property as their primary residence (and not with the intent to lease it) is technically in violation of the extended use period regulation, since the property is, by definition, no longer affordable rental housing. This issue was clarified by an IRS Revenue Ruling 95-49, which ruled to allow HFAs (“credit agencies”) to replace LURAs in the case of homeownership conversion with one more suited to homeownership. Many specifics have yet to be defined, however, due to the relatively small number of pioneering owners and tenants that have used this option.

Furthermore, in 2006, a developer of a multi-family LIHTC property in Kansas City, MO requested that the IRS rule on whether conversion of their property to affordable condominiums was an acceptable exit strategy, as interpreted from IRC Section 42. The IRS ruled favorably in early 2007 that it would accept the conversion of LIHTC properties to homeownership provided that existing tenants receive the right of first refusal to purchase their units, and that mortgage payments plus condominium fees do not exceed the equivalent rent restrictions (Brown). In this way, the investor and the property may effectively exit the LIHTC program in a manner that preserves affordability for the tenant.

Although the IRS ruling lacks widespread applicability, they have indicated their overall acceptance of the homeownership conversion concept, resulting in renewed interest in the LIHTC exit process.

Conversion Options

John Brandenburg, the managing director of asset management at Enterprise Social Investment Corp., promotes lease-purchase agreements as one method of fostering a homeownership conversion of LIHTC units. For the most part, he attributes many advantages of this option to the assumption that homeownership is a powerful motivator for attracting responsible, long-term residents who take better care of the structure (Brandenburg, Countdown, 76-78). PolicyLink recommends refining the LIHTC program to "require conversion to co-ops of rental buildings financed through LIHTC," claiming that such a policy would "produce less displacement at the expiration of the tax credit, and [allow residents to gain] valuable experience in self-governance years before the conversion takes place" (PolicyLink Policy Priorities).

Section 42 of the IRC currently allows tenants and tenant co-ops to purchase LIHTC properties, although this option has received little research. Brandenburg identifies a number of strategies for enabling this form of LIHTC conversion, including: lease-purchase agreements, co-op conversions, and condo conversion (Brandenburg, Year 15). The North Carolina HFA is interested in exploring the potential of homeownership conversion, and has decided to begin their efforts by targeting single-family LIHTC units within the state.

For a variety of reasons, affordable housing advocates have reason to be excited about this newly explored option, since it is tempting to assume that tenants of LIHTC properties have a vested interest in remaining in their own unit, providing an obvious buyer as long as the price is affordable.

CASE STUDY: North Carolina Single-Family LIHTC Properties

The North Carolina HFA has identified 472 currently active LIHTC units on 323 different properties that have four or fewer units per property, and were allocated tax credits beginning in 1990 or thereafter. Through much of the 1990s, the NCHFA allocated tax credits to both multi-family and scattered-site single-family developments. When scattered among market-rate, single-family neighborhoods, single-family LIHTC units have some perceived advantages over multi-family housing, including the deconcentration of poverty; the promotion of a homeownership culture and a traditional middle-class family lifestyle; and a decreased stigma of low-income housing due to a structural appearance that is indistinguishable from its neighbors.

Beginning in 1998, however, the NCHFA ceased allocating tax credits to single-family developments. Since the NCFHA receives far more applications for tax credits than they can distribute, it made sense to target tax credits towards multi-family housing, which can produce more units per credit. Additionally, compliance monitoring conducted by the NCHFA takes the same amount of time per property, regardless of the number of units on that property. Therefore, it was more logical for the NCHFA to eliminate the consideration of single family LIHTC units from both a financial and time-management standpoint.

Due to their smaller size, these developments also created investment opportunities for small-scale, and frequently individual, investors. Typically, these individual investors simply paid for the construction of the unit, acting as developer and investor in one. Typically, a discussion of a LIHTC exit process must distinguish between the developer and the investor, since they have differing roles and motivations to consider, but herein we need only refer to the singular “owner.” This arrangement has the potential to simplify the exit process, since fewer stakeholders are involved. As mentioned previously, investor motivations and additional affordability restrictions are influential in the preservation versus conversion decision. These properties do not involve any non-profit developers and construction of a single unit is usually affordable enough for a single investor to finance without additional government subsidy.

The process of exiting single-family and other small-scale properties involves unique obstacles compared to multi-family housing. There is no data to indicate what exit methods are most commonly used by owners of these particular structures, but we may hypothesize that they are bureaucratically and economically more difficult to exit than multi-family structures. Because of the small-scale business operations required to own and maintain one of these properties, it is unlikely that these owners have maintained the historic paperwork necessary to apply to the North Carolina HFA for a qualified contract.

Their small size also inhibits their financial appeal to investors willing to purchase LIHTC properties. Small units are an inherently risky investment since 1 vacant unit in a 1 unit property negatively impacts cash flows more so than a 10 unit vacancy in a 100 unit property. Also, since credits are no longer provided to construct single family homes, it is unclear whether or not a new owner could successfully apply for rehabilitation credits.

Conversion to condos or cooperatives is not generally a suitable exit strategy for small-scale units. The standard remaining options for conversion are a lease-purchase agreement with, or direct sale to the tenant, although other creative transfers could be structured. A sale of the land to a land trust, and the structure to the low-income tenant is one such option that has received little research.

The purpose of this case study is to evaluate the potential of homeownership conversion among these 472 small-scale units. This analysis has been conducted by contacting owners and tenants of these properties to determine their interest in such a transaction and by a supplemental analysis of property and tenant characteristics. Analysis of conversion of multi-family LIHTC structures into condominiums or co-operative housing is outside the scope of this analysis.

Methodology of Study

In order to facilitate the establishment of homeownership conversion as an allowable exit strategy in North Carolina, policies and procedures must be set in place, and owners and tenants must be notified of the option. This research takes one step in that direction by documenting the precedent for homeownership conversion, contacting LIHTC owners and tenants to begin a dialogue on the issue, and make suggestions for the next steps in establishing requirements for property transfers.

In December of 2007, the North Carolina HFA provided an extensive database of 1-4 unit LIHTC properties that were currently active within the LIHTC program. In general, the database included information on the owner(s) of the properties, location of the properties, and information on the tenants, including rents paid and annual income. This data was used to develop a mass mailing directed at both LIHTC owners and tenants of small-scale units that could be possible candidates for homeownership conversion.

The database of tenant and owner information was used to create a mass mailing list. Letters were sent only to those tenants and owners in the case that the tenant (or at least one of the tenants) paid at least $275 out-of-pocket towards rent, assuming that tenants paying less could not possibly afford a mortgage. In late January of 2008, 169 owners and 352 tenants were contacted via a mass mailing. Four sets of letters were sent:

1. Owners of properties that have passed Y15
2. Owners of properties that has not passed Y15
3. Tenants of properties that have passed Y15
4. Tenants of properties that has not passed Y15

The letters briefly informed the recipients that they were being contacted as part of a master's student research into the preservation of LIHTC units, and that public records indicated that they were the owner/tenant of such a unit. Further, the letter briefly described that owners of LIHTC units are allowed to sell their property after the structure reaches 15 years in age, and that the North Carolina HFA was currently researching homeownership conversion as a possible exit strategy.

The letter asked for their general feedback on the issue, and listed a few prompting questions. The questions were only meant to prompt the recipient to think about the issue and to assist with the beginnings of a conversation, and not to extract data which could be used to run statistical analysis. They were asked to respond via phone, fax or email by February 15th, 2008, at which time their input would be forwarded on to the HFA.

The survey was not officially endorsed by the North Carolina HFA, which may explain the relatively low response rate, particularly by tenants. Overall, the owner response rate was expected to be higher than that of the tenants. Owners are necessarily familiar with the LIHTC program, and could have a financial incentive to investigate a newly advertised exit option. In addition, the North Carolina HFA has become aware of several owners' desire to exit their property through informal conversations. Several owners indicated that they would not have entered the program had they anticipated the difficulty in exiting.

Property Characteristics

Location

The 323 sample properties are all located in the State of North Carolina within 13 counties (out of 100), and are predominantly located within Wake County. Forty seven percent of the 323 properties are located within the City of Raleigh. Locations of the sample properties are displayed in Exhibits 1 and 2 and listed by county in Exhibit 3.

Physical Description

On average, the sample LIHTC properties are 892 square feet in size. We do not have information on the quality of the structures or the physical upkeep, and so cannot make a generalization regarding the marketability of the properties.

Placed Into Service

The date that a LIHTC building is placed into service is the date at which a building is certified by the state and/or local government for occupation. The IRS uses this date to begin the countdown to Y15. So far, 11% of the sample units have reached the end of the first 15 years of compliance as of Dec 31st, 2007, and all of the units will reach Y15 by Dec 31st, 2012. Placed-into-service dates are listed in Exhibit 4.

Over 50% of these properties will reach Y15 between 2010 and 2012. There is sufficient time for the North Carolina HFA to analyze the potential for homeownership conversion and to determine a procedure for enabling such conversion in time to affect a large number of properties.

EXHIBIT 1

Number of Sample Low Income Housing Tax Credit Properties in North Carolina by County

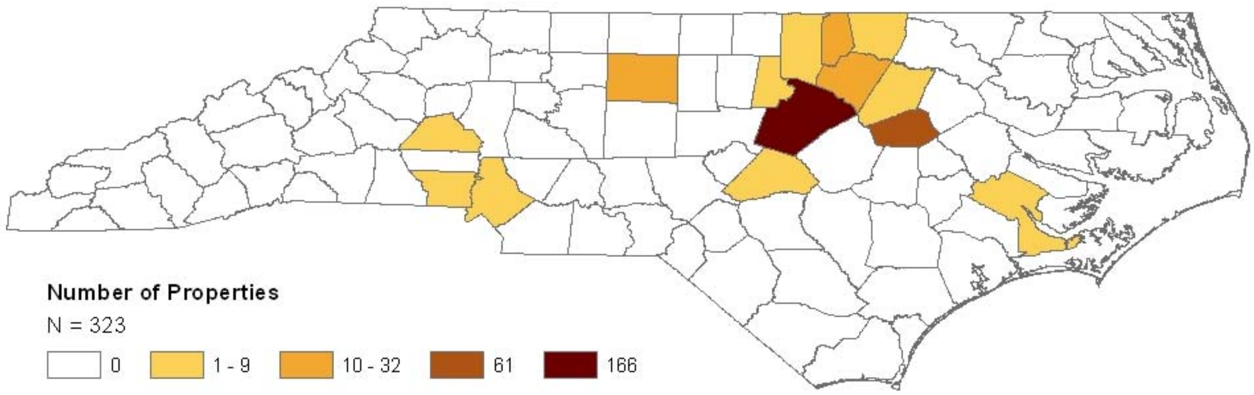

EXHIBIT 2

Number of Sample Low Income Housing Tax Credit Properties in Wake County, NC by Zip Code

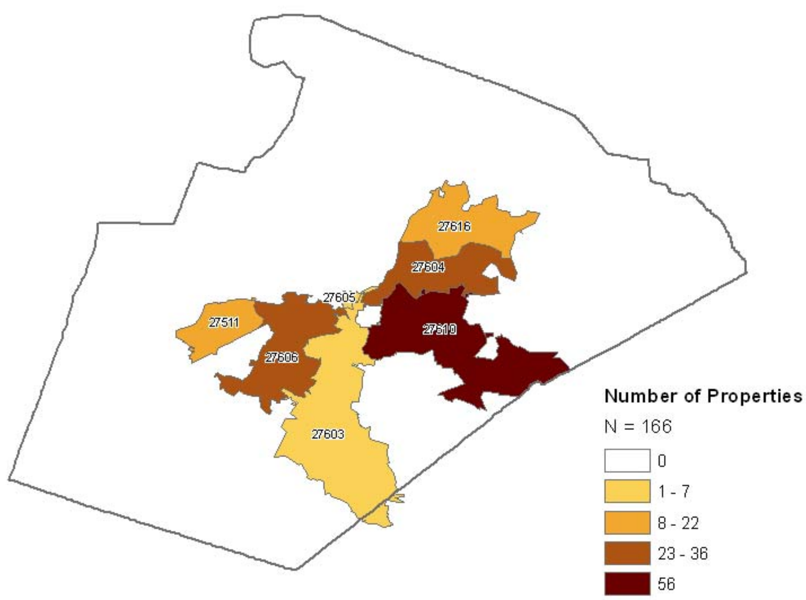

EXHIBIT 3: Location by County

County	Number of Properties	% of Total
Wake	166	51%
Wilson	61	19%
Guilford	32	10%
Vance	26	8%
Franklin	13	4%
Granville	9	3%
Warren	5	2%
Gaston	3	1%
Craven	2	1%
Durham	2	1%
Catawba	1	0%
Harnett	1	0%
Mecklenburg	1	0%
Nash	1	0%
	323	

EXHIBIT 4: Year Placed Into Service

Year Placed into Service	Number of Units	Will reach Y15 on Dec 31st of:
1990	1	2005
1991	1	2006
1992	48	2007
1993	52	2008
1994	86	2009
1995	97	2010
1996	142	2011
1997	45	2012
	472	

<u>Applicable and Annual Income</u>

Approved LIHTC developments must target low income populations, based on the Area Medium Income (AMI) of the geographical area, as determined by HUD. At a minimum, a LIHTC property must target either 20% of its units to tenants below 50% of the AMI, *or* 40% of its units to tenants below 60% of the AMI. These limitations can be adjusted for household size and unique characteristics of the geographic area that affect the range of rental rates. Of the 323 sample properties, tenants in 48 of the units have incomes above 60% of the AMI. There are two primary reasons why theses tenants could have incomes above the 60% maximum. First, these tenants' income could have increased since the time they moved into the unit. The North Carolina HFA receives periodic updates on LIHTC units, and these numbers may have been updated since the tenant was initially qualified for the LIHTC unit. Second, the local area AMI could have decreased, in which case the existing tenants would not have been penalized for their relatively "heightened" income. HUD has adopted several "hold harmless" policies that effectively freeze income limits in the case that local AMI decreases (Emrath 289).

Overall, the subject properties serve a very low income population, with over 70% of the units being rented to tenants at 50% or below of the AMI. This is supported by tenants' low annual income. A majority of tenants' make below $30,000 annually, as shown in Exhibit 6. Although this indicates that the LIHTC program has been successful at housing a very needy population, these individuals are poor candidates for homeownership, due to their low income and greater need for additional housing assistance. Tenant income as a percentage of Area Median Income (AMI) is listed in Exhibit 5.

EXHIBIT 5: Applicable Income

Tenant Income (Percentage of AMI)	Number of Units	% of Total
> 60	48	10%
<= 60	66	14%
<= 50	45	10%
<= 45	40	8%
<= 40	51	11%
<= 35	43	9%
<= 30	178	38%
unknown	1	0%
	472	

EXHIBIT 6: Tenant Income

Tenant Income Range	Number of Units	% of Total
0	12	3%
$1 - 5,000	20	4%
$5,001 - 10,000	71	15%
$10,001 - 20,000	178	38%
$20,001 - 30,000	137	29%
$30,001 - 40,000	39	8%
$40,001 - 50,000	8	2%
$50,000 - 65,450	3	1%
unknown	4	1%
	472	

Additional Federal Assistance

LIHTC properties may also be the recipients of additional federal housing assistance in the form of Section 8 vouchers or Operational Assistance grants. Section 8 vouchers originate from an older federal housing assistance program and may be used in tandem with the LIHTC program. Vouchers are used to supplement rental income received by the owner of a rental housing unit in order to decrease the rent charged to low-income tenants. To redeem the value of the voucher, owners submit them to the government for a direct cash payment.

Vouchers may come in one of two forms. The first and primary type of voucher is a tenant-based voucher, whereby a voucher is assigned to a qualified tenant who may use the voucher to supplement their rental payment wherever a landlord is willing to accept it, and if the rental unit meets certain structural quality criteria set forth by the program. This method of distributing vouchers gives tenants greater freedom to move locations with less fear of losing housing assistance. LIHTC program regulations require owners to accept vouchers. Tenants in 29% of our sample LIHTC units receive a Section 8 voucher of this type.

The second type is a project-based voucher whereby a local public housing authority distributes the vouchers directly to the owner of new construction or rehabilitation projects. This voucher type is tied to the physical unit(s) for a specified period of time, and does not follow a tenant. Regulations cap the distribution of these vouchers to 15% of the yearly voucher supply. Only 3% of our sample LIHTC units receive this type of assistance.

Only four units received an operational assistance grant, a federal grant issued to business owners to assist with needs such as accounting, business plans or engineering assistance. The type of housing assistance received by tenants and the average amount received per LIHTC unit is listed in Exhibit 7.

EXHIBIT 7: Additional Housing Assistance

Type of Housing Assistance	Number of Units	%	Average Amt of Assistance per Unit
No Assistance Received	304	64%	$4.67
Sect 8 Vouchers	138	29%	$572.70
Sect 8 Project-Based Vouchers	16	3%	$673.88
Operational Assistance	4	1%	$395.00
Unknown	10	2%	$22.30
	472		

A majority of the subject units receive no additional assistance beyond the tax credits. We can assume that tenants without federal rental assistance have a greater capacity to afford a mortgage payment within affordability restrictions than those tenants receiving additional rental subsidy. Tenants who receive Section 8 vouchers are unlikely candidates for homeownership. Although vouchers can technically be used towards mortgage payments, they are an unreliable source of financial assistance for the tenant, since they need to be renewed yearly. Since need for housing assistance has continually exceeded supply, and since funding for Section 8 vouchers needs federal approval each year, it is unlikely that this resource will be targeted towards homeownership initiatives.

Rent

The total monthly rent due to owners of the sample properties ranges from $0 - $999, with most lying in the $500 - $699 range. Due to the additional subsidy received by many tenants, the amount paid out-of-pocket ranges from $0 - $825, with most lying in the $300 - $499 range. Total rents charged and the total rents paid out-of-pocket by the tenants are displayed in Exhibits 8 and 9.[4]

In the case that a tenant purchases their unit, their monthly rent paid out-of-pocket is the best indicator of what they can afford, since they are unlikely to receive additional subsidy as a homeowner.

EXHIBIT 8: Total Rent*

Total Rent Range	Number of Units
$1 - 299	**0**
$300 - 499	70
$500 - 699	166
$700 - 899	68
$900 and Above	3
	307

** Less utility payment allowance*

EXHIBIT 9: Rent Paid Out-of-Pocket

Tenant Out-of-Pocket Rent Range	Number of Units
$1 - 299	2
$300 - 499	212
$500 - 699	80
$700 and Above	13
	307

[4] Only 307 of the total 472 units contained data deemed acceptable for analysis. Data was considered reliable if the sum of tenant paid out-of-pocket rent, additional subsidy, and utilities were equal to total rent. Data on rents is provided directly to the North Carolina HFA by the owners, and is subject to mis-interpretation and data entry error.

Tenants' Length of Tenure

A majority of tenants have lived in their units for four years or less. Without a control group of similar multi-family rental housing, it is difficult to determine if the units' single-family structure correlates with longer durations of tenure.

EXHIBIT 10: Length of Tenure

Move-In Year	Tenure (years)	Number of Units	% of Total
1900*		1	0.2%
1990	18	0	0.0%
1991	17	0	0.0%
1992	16	3	0.6%
1993	15	3	0.6%
1994	14	8	1.7%
1995	13	8	1.7%
1996	12	6	1.3%
1997	11	14	3.0%
1998	10	11	2.3%
1999	9	18	3.8%
2000	8	13	2.8%
2001	7	22	4.7%
2002	6	35	7.4%
2003	5	34	7.2%
2004	4	53	11.2%
2005	3	91	19.3%
2006	2	72	15.3%
2007	1	80	16.9%
		472	

Error in data.

More than 10% of tenants have lived in their units for more than 9 years, and more than 20% of tenants have lived in their units for 6 years or more. It is unknown for what reason these long-term tenants have remained in their units (do they like their units or location, or are they simply unable to move?), but we may hypothesize that they have developed structural and social attachments to the unit and/or its location that could increase their interest in remaining in the unit as a homeowner. Tenants' length of tenure in their respective units is listed in Exhibit 10.

Response Rate and Feedback

Owners' Views

As of February 29, 2008, 16.5% of contacted owners have responded. These owners represent 23.4% of all sample properties for which an owner was contacted. Two of the envelopes were returned undeliverable. Twenty of the responding owners have expressed at least some interest in selling their property to the tenant(s) and the remaining 8 responding owners have indicated that they are not interested in selling at this time.

In addition to asking owners for their general interest in the possibility of selling to their tenant(s), the letters asked if they had any outstanding mortgage, if they had an asking price in mind, and if they had considered the tax implications of a sale. Responses to these questions were voluntary, and were designed in part for them to begin thinking about their needs in selling. Any comments that the owners made in regards to these comments in their written or verbal communication were documented and can be summarized as follows:

- Owners expressed varying levels of interest in selling their unit to the existing tenant. The first respondents were those who were most eager to dispose of their properties, and we can assume that owners who are not interested in selling were least likely to respond at all.
- At least one owner was not interested in selling at this time, but was grateful to learn of homeownership conversion as a possible future exit strategy.
- Eighteen respondents remarked upon their outstanding mortgage. Eight owners had no remaining mortgage and 8 owners did, although six of them did not provide an amount. One owner owed $71,000 on a two-unit property, and another owner owed $1 million on a mixed-income Planned Unit Development with multiple single-family units.
- Fourteen respondents remarked upon a possible asking price. Some respondents had no asking price in mind and some referred simply to any price that "the market will bear." Many referenced their current tax value, which ranged from $40,000 to $81,000, although one owner remarked that current tax values were unrealistic in light of the current market downturn and speculated that market rates in his/her neighborhood were approximately $20,000 below his/her tax value. Some owners implied that their intended sales price was flexible, and some required tax value "at a minimum."
- Several owners expressed concern that their current tenants would not be able to afford to purchase the property, due to their low incomes and/or a history of late payments.
- Several owners indicated that their properties are currently vacant. At least one property has been vacant for an entire year, and a few owners cited a need to turn down prospective tenants who made too much income to qualify.
- Some owners have already begun the process of finding a qualified buyer. At least two owners have offered to sell or donate their properties to Habitat for Humanity, who has refused the offer. One owner has begun to contact area churches as well.
- One owner has partnered with Community Affordable Housing and Equity Corp., a non-profit LIHTC syndicator, and has already begun discussing homeownership conversion as a possible exit strategy.

Owners who were interested in selling raised a number of questions over regulations surrounding a sale, including what steps they could take next to begin the process. Their questions can be summarized as follows:

- What guarantee(s) do owners have that they will be freed from liability once their property is sold?

- If the existing tenant can't be approved for a mortgage, or the property is currently vacant, who can the owner sell to?
- Can the HFA provide a list of qualified buyers?
- Can homeownership conversion take place prior to Y15?

Tenants' Views

Although a low response rate was expected from the tenants, it was much lower than anticipated. Only two percent (8 tenants) of the contacted tenants responded. Of those who responded, 7 expressed at least some interest in purchasing their rental unit. Tenants tended to respond by voicemail, whereas owners tended to respond by email, and as such, there are three additional tenants who have left voicemails, but whom I've been unable to reach. These tenants have not been included in the 2% response rate.

One contributing factor to the low response rate from tenants is that 16% of the mailed letters were returned undeliverable. The most likely explanation is that the data provided by the North Carolina HFA was old enough that some tenants had already moved by the time of the mailing. As a result of the low response rate, the tenants' views are best described in a qualitative manner.

In addition to asking tenants for their general interest in the possibility of purchasing their units, the letters asked if they had ever been a homeowner, if they intended to become a homeowner in the foreseeable future, and if they liked the appearance and location of their rental unit. Responses to these questions were voluntary. Any comments that tenants made in their written or verbal communication were documented and can be summarized as follows:

- Tenants who were interested in purchasing their unit expressed a desire to become a homeowner in general, versus a desire to purchase their specific unit. As evidence, one tenant asked if it were possible to obtain a list of all similar LIHTC units that were up for sale so that she could compare.
- At least one tenant complained that her unit was not properly maintained by the owner, and would only consider purchasing it if it were repaired.
- At least one tenant was an undergraduate student who was happy with her existing unit and had not immediate plans to move. She was planning on becoming a homeowner at some point after graduating.

Originally, it was hoped that response rates would be large enough that "matched pairs" could be passed onto the North Carolina HFA, who could take the next steps in facilitating the homeownership conversion process. Unfortunately, only one such matched pair emerged.

The owner of the property indicated that the tax value of his unit was approximately $80,000, which he considered to be an unrealistic asking price based on the recent downturn in home sales nation-wide. A review of the property's tax records available on the county's online tax records database indicated that the property was purchased for a similar amount.

The tenant also responded to the letter, and stated that she was interested in becoming a homeowner and that she would be interested in purchasing her specific unit. Based on information available in the North Carolina HFA database, the tenant makes a very low income, and would be qualified for a FirstHome Mortgage offered through the North Carolina HFA[5] with down payment assistance as long as she can meet additional credit history criteria, as required by a participating private lender.

Example of a Potential Home Purchase

If we proceed from the tenant's current out-of-pocket rent, from which a monthly utility payment has already been deducted, we can further deduct a monthly property tax and insurance payment, estimated at $190 a month. She will then have only $130 left over for a monthly mortgage payment. Based on a 30-year fixed-rate FirstHome Mortgage, which is currently offering rates as low as 6.275%, she can receive a mortgage in the amount of approximately $21,100. With down payment assistance, she can afford a maximum asking price of $35,000 (without consideration of closing costs). Her loan-to-value ratio is 75% and her front-end debt-to-income ratio will be approximately 35%.

EXHIBIT 11: Matched Pair Tenant Mortgage Qualification Estimation

Rent Out-of-Pocket*	$320.00
- Monthly Property Tax	$90.00
- Monthly Insurance	$100.00
	$130.00
Mortgage	$20,837.68
$7,000 down payment	$7,000.00
Max Purchase Price	**$27,837.68**
LTV:	75%
Debt-to-income:	Approx. 35%

** excludes utility payments*

The tenant in question makes well below the maximum 60% AMI, however, and so we can also compare this to the maximum price that the owner would receive if it were being purchased by a low-income person with the maximum income designated by HUD (by county and household size). For example, the maximum annual income for a 2-person household earning 60% of the AMI would be $34,380, and the maximum monthly rent for a 2-bedroom house would be $1,117 (including utilities) in the same county. A person with this income would not be eligible for down payment assistance, however, but can qualify for the much larger loan amount of $122,622.06 at a 100% loan-to-value.

[5] See the Appendix for a detailed list of mortgage products and services offered by the North Carolina HFA to first-time homebuyers.

EXHIBIT 12: Maximum Mortgage Qualification Estimation

Rent Out-of-Pocket	$1,117.00
- Monthly Property Tax	$90.00
- Monthly Insurance	$100.00
- Utilities	$170.00
	$757.00
Mortgage	**$122,622.06**
LTV:	100%
Debt-to-income:	52%

Analysis

Homeownership conversion is a potentially beneficial exit option in North Carolina, even though its applicability will be limited by the low incomes of the tenants and by regulatory uncertainty. Owners motivated to dispose of their LIHTC properties will be the driving force behind any conversions.

The first step in facilitating homeownership conversion in North Carolina is to inform owners of the option. Educating the tenants is also important, yet is relatively premature if the owner is not ready to proceed with disposition. Informing the owners will require that questions be answered in regards to the process for this transaction. For this purpose, it is most useful to use guidelines set forth by the Missouri's Housing Development Commission to outline the possible policies to put in place. Among the states, Missouri has been perhaps the most progressive in terms of allowing and planning for homeownership conversion. The LIHTC program is administered in that state by the Missouri Housing Development Commission (MHDC).

Missouri Housing Development Commission's Homeownership Policy & Homeownership Commitments

The MHDC Homeownership Policy regulates the process of homeownership conversion through an additional legal document called a Homeownership Commitment, which must be proposed when the developer submits an application for LIHTC credits, and which becomes attached to the LURA and all tenant leases. Essentially, if an owner would like to consider the use of homeownership conversion as an exit strategy, they must request that option at the outset of the project, and agree to give the tenant the right-of-first-refusal to purchase the property.

Each Homeownership Commitment (HC) may be individually crafted, but will include several criteria established by the MHDC that must be addressed in all agreements. Those elements include (but are not limited to) the following:

- The HC forbids the owner from applying for a Qualified Contract.

- The property must have completed the initial 15 year compliance period prior to initiating the sales process.
- The buyer must occupy the house as their primary residence.
- **Minimum Price**: any outstanding debt associated with the property (not including physical improvements necessary to sell the property in good condition) plus taxes (as defined in IRC Section 42(i)(7)(B)).
- **Maximum Price**: the sales price at which the buyer's monthly mortgage payment (including principal and interest), property taxes, property & mortgage insurance, and utilities, *less a 1% discount for each year the purchasing resident has leased the unit* does not exceed the maximum monthly rent established for that unit.

Each HC will detail a general sequence for selling the property to the tenant:

EXHIBIT 13: Timeline for Homeownership Conversion of Single-Family Units in Missouri

Step 1:	**Housing Inspection** Each house must pass a Housing Quality Standards inspection and undergo a physical needs assessment. The owner must address any needed improvements identified by the Physical Needs Assessment prior to notifying the tenant of their desire to sell.
Step 2:	**Y15**
Step 3:	**Conversion Date** The owner must notify the tenant of their desire to sell within 12 months of the unit's Y15 date. The date upon which the owner delivers this notification is referred to as the "Conversion Date."
Step 4:	**Accept or Decline** The tenant has up to 6 months after the Conversion Date to accept of decline the offer. Any tenant who is in "good standing" at the time of the offer has the right to exercise the option.

If a tenant does not accept the offer within 6 months, the owner has several options for disposing of the property:

"a. The owner can choose to sell the remaining units of the project to a non-profit partner or another entity that will continue to operate the units as affordable housing in accordance with the LURA. The sale must include 100% of the remaining rental units, not a portion thereof.

b. The owner can choose to maintain the remaining units of the project as rental units, adhering to all MHDC Extended Use Period guidelines. The remaining units after this initial 6 month selling period may at any time be offered for sale to the current or subsequent qualified residents.

c. The owner can offer vacant units for sale to a buyer whose household income does not exceed 80% of the area medium income. A potential purchaser who qualifies under this income restriction is not required to lease the unit before they purchase it." (MHDC Homeownership Policy, 4)

In addition to structuring the requirements and process involved in homeownership conversion of single-family LIHTC units, the MHDC has also required numerous tenant rights and protections to be included in each HC, including the following:

- The owner must include an addendum to all signed leases, which must document the definition of "right-of-first-refusal", "good standing", the minimum sales price as defined by IRC Section 42, and the Conversion Date.
- The owner must provide information on available homeownership training to the tenant 5 years prior to the Conversion Date, and must be included with any lease signed within the 5 year period up to the Conversion Date.
- One year prior to the Conversion Date, the owner must provide the resident with information detailing the dates, timeline and more detailed information regarding the right-of-first refusal process.
- Tenants who fail to qualify for a mortgage or who do not wish to purchase may not be evicted or otherwise removed without just cause as determined within the lease.
- Tenants who do not wish to purchase the unit may not be discriminated against in the leasing process.
- In general, tenants who experience an increase in income will not be disqualified from the right-of-first refusal to purchase.

In order for homeownership conversion to become a common exit option, tenant education and notification of this form is necessary. As was demonstrated by the low response rate and feedback from tenants in North Carolina, tenants may be entirely unaware of their unit's LIHTC status and the potential for homeownership. Deb Giffin, the Director of Asset Management at MHDC has emphasized that notification and tenant assistance is necessary when the fundamental goal of the process is to preserve the quality and affordability of LIHTC housing for the target population.

Even when homeownership conversion is proactively promoted as it is in Missouri, only a "handful" of eligible properties have been converted so far. The MHDC acknowledges that this process is experimental, and that many states are observing the effects of Missouri's policies before following suit (Giffin).

Application to North Carolina

Since the North Carolina HFA has not required any agreement similar to Missouri's Homeownership Commitment, homeownership conversion of the remaining small-scale LIHTC units in North Carolina will necessarily take a more organic and unstructured form, if pursued. Legally, the North Carolina HFA is limited to enforcing IRC Section 42 and the LURA. They have no further authority to require additional action on behalf of the owner in regards to such items as property improvements or tenant notification. The guidelines and requirements set forth in Missouri can, however, serve as a starting point from which to discuss the potential of a homeownership conversion process in North Carolina.

Minimum & Maximum Sales Price

The minimum sales price of a LIHTC unit upon a Y15 exit is already established in Section 42 (i)(7)(B) of the IRC, which is set to the sum of the outstanding debt attributed to the property (minus debt secured within 5 years of the sale of the property) plus any Federal, State and local taxes attributable to the sale.

A maximum sales price is outside of the HFA's jurisdiction to regulate, yet owners are limited in their asking price to the amount that private lenders will issue to prospective homebuyers. We can attempt to evaluate tenants' ability to afford a mortgage based on the criteria set forth in Missouri's Homeownership Policy; namely that the maximum sales price is determined by the monthly mortgage payment, property taxes, property & mortgage insurance, and utilities (less a 1% discount for each year the purchasing resident has leased the unit), which cannot exceed the maximum monthly LIHTC rent for that unit.

For example, let's assume a $60,000 asking price, and a tenant with an annual income of $20,000.[6] Assuming that the tenant meets private lender criteria necessary to receive a mortgage, they will be eligible for $7,000 in down payment assistance through the North Carolina HFA, reducing the needed mortgage to $53,000, an 88% loan-to-value. Currently, the North Carolina HFA is offering interest rates as low as 6.375% to first-time homebuyers through their FirstHome Mortgage. Since all FirstHome Mortgages are fixed-rate with a 30-year term, the homebuyer's monthly mortgage payment would be $330.65. The average utility allowance in our dataset is $150 per month, and we'll assume that tax and insurance payments average around $120 per month. Total monthly expenses therefore equal $601.

If this tenant lived in Wake County, they would be very low-income in comparison to the median income household, but could possible "afford" to purchase their unit depending on the number of persons in the household, based on maximum income and housing expense limits. If the tenant is a one-person household, then their $20,000 annual income sets them at less than 40% of the AMI, and their $601 monthly housing expense would meet the limits of a two or three bedroom house (see chart below). They could, of course, "afford" a smaller house, except that the housing expense limits simply set the cost of $601 per month as too high for that size of structure. If the tenant is a two-person household, then their annual income sets them at less than 35% of the AMI, and their monthly housing expense would meet the limits of a three bedroom household only. If the tenant is a three-person household, then their annual income is less than 30% of the AMI, and their monthly housing expense is too great to qualify the purchase of any sized structure.[7]

[6] The average tenant in our sample dataset makes $18,059 annually.

[7] Based on Missouri's maximum sales price policy, which has no effect on sales prices in North Carolina, and is only used for comparison.

Exhibit 14: Wake County Income Limits and Maximum Housing Expense

Wake County	Income Limit for Family Size Median Income: $69,800[1]					Maximum Housing Expense[2]			
% of Median Income	One Person	Two Person	Three Person	Four Person	Five Person	Effi-ciency	One BR	Two BR	Three BR
30%	15,050	17,200	19,350	21,500	23,200	376	403	484	559
35%	17,535	20,055	22,540	25,060	27,355	438	470	564	651
40%	20,040	22,920	25,760	28,640	30,920	501	537	644	745
45%	22,545	25,785	28,640	32,220	34,785	564	604	725	838
50%	25,050	28,650	32,200	35,800	38,650	626	671	805	931
60%	30,060	34,380	38,640	42,960	46,380	752	806	966	1,117

[1] *From March 20, 2007 HUD Section 8 Income Limits*
[2] *Maximum Housing Expense includes rent and utility allowance, and is based on 1.5 persons per bedroom. Source: North Carolina Housing Finance Agency 2007 Income Limits and Maximum House Expense. Effective 3/20/07. Available: www.nchfa.org*

Also note that the above calculation did not take into account the 1% reduction in sales price set forth in Missouri's homeownership conversion policy. To determine the effect of this reduction, let's take the average tenant among our sample properties, who has lived in their unit for 5 years (since 2003), which qualifies them for a 5% reduction in sales price. The sales price is thus reduced to $57,000, and if we keep all other assumptions the same, the tenant's monthly housing expense is reduced to $582 per month (or a $19 per month reduction in housing expenses).

<u>New Tenants or Homebuyers</u>

Section 42 of the IRC does not dictate a maximum sales price because it was unclear at the time whether or not properties would appreciate, or if tenant incomes would rise. In the case that both value and incomes increased, there was no desire to restrict the benefit awarded to the owner, who had enabled that growth through their provision of affordable housing. Generally, access to low-income housing has not resulted in significantly appreciated incomes, however, and so the HFA does not necessarily need to address maximum sales prices when the purchaser is an existing tenant. At the very least, tenants are unlikely to be approved for mortgages that are unaffordable based on their income. A better approach may be to encourage owners to consider asking prices that may be below tax value, yet affordable to low-income tenants.

Due to the large percentage of returned envelopes that were sent to the study sample tenants, it is possible that a number of our sample units are currently vacant. In this case, it is still unclear how an owner might proceed with a sale. It is generally assumed that the homebuyer would first need to qualify for the LIHTC program, based on maximum income and that the sales price would need to reflect maximum housing expenses. This has yet to be clarified, however, and warrants further discussion.

<u>Regulating Homeownership</u>

Homeownership conversion will require that HFAs nullify the original LURA attached to the property. In Missouri, a new LURA with language more appropriate to owner-occupancy will replace the old one, yet it is unclear if this is federally mandated. Section

42(h)(6) of the IRC provides that tax credits may not be awarded to a LIHTC unit unless a LURA is attached to the property, but this provision means little after Y15, at which point the property, and owner, are held to be in compliance with all portions of the program related to receipt of the tax credits.

HFAs may be tempted to consider a homeownership conversion as a final and successful completion of the property's affordable life-purpose, without concern for future uses or sales of the property. So far, it is unclear if this is allowed, or if an HFA must continue to monitor the affordability of the property for the remainder of the extended use period. Staff at MHDC, for example, were concerned that tenants may attempt to purchase their LIHTC unit at an affordable price, and then resell the property for a profit. This option was considered contrary to the spirit of the LIHTC program, and provisions for retaining affordability are thus placed in the new LURA (Giffin). Although questions remain regarding affordability post-conversion, it is clear that HFAs can continue to use the LURA document as a method for regulation, if so desired.

Conclusion

Homeownership conversion is a viable option for exiting LIHTC properties, yet little information is available to determine the widespread potential of this option. The main deterrent to this process is a lack of information on allowable procedures and restrictions, since the process has not been explicitly detailed in the language of the LIHTC program.

Secondly, this case study has also shown that there may be a tenuous negotiation between an owner's asking price and the ability of the target population to afford that price. Many owners of the study's small-scale LIHTC properties are poorly informed of the extended use period, or their exiting options during that period. One owner even acknowledged that she was unaware of what documents she signed at the time of application, since she was competing so fiercely to receive a tax credit allocation. Even those owners with adequate information tended to express a desire to receive market rate returns from a sale, despite the contradiction of receiving such returns on housing established for the purpose of housing a low income population.

The most direct method of addressing many of the unknowns listed above is for state HFAs to establish their own policies, and to insert any restrictions into the application process, before the structure is built. Certain documents are required as a result of the federal legislation that created the LIHTC program, but state's may require or encourage owners to accept additional provisions. The State of Missouri has anticipated many of the obstacles to homeownership conversion by requiring a Homeownership Commitment that mandates a standard process for homeownership conversion and several tenant protections. Any state that seeks to regulate the exit process in a similar manner will be most successful if they can leverage agreements as a condition of receiving the tax credits.

Since the North Carolina HFA has not required any commitments from their small-scale LIHTC property owners beyond what is mandated by the program, they are limited in their ability to guide the exit process in a manner similar to that in Missouri. For this reason, it is difficult for them to issue a specific policy statement to assist current owners with the conversion process, since each transaction (if any) will likely take on its own organic form. Therefore, in April of 2008, the North Carolina HFA will issue a general memo to all current owners of small-scale LIHTC units in the state, publicizing their general acceptance of homeownership conversion, and inviting interested owners to contact the HFA for more information.

North Carolina no longer allocates tax credits to single-family housing units, however, and so this issue does not hold the prominence that it may in other states that continue to allocate credits to single family, or similarly small-scale developments. Those states may want to consider the following:

Should homeownership conversion be encouraged? Why?
All states will benefit from an analysis of their existing LIHTC stock, regardless of the homeownership conversion issue. Addressing current and future affordability depends on a number of factors including supply & demand, local incomes, and physical characteristics of the housing stock. Valid questions remain as to the physical quality of 15-year old rental housing and government promotion of homeownership among populations that cannot sustain the expense. For example:

- What percentage of the LIHTC stock is small-scale?
- Where are the properties located?
- What is the physical condition of the properties?

If it is decided that homeownership conversion should be encouraged, staff at the HFA may want to familiarize themselves with any and all federal code that relates to the process, and with case studies of successful/failed homeownership conversion attempts. Is homeownership a desirable option in this state simply because it facilitates the exit process, or because there is a desire to regulate the process in such a manner that preserves affordability in the long-term?

If so, what additional regulations should be attached to the process?
If a state currently allocates tax credits to small scale developments, they may want to consider including documents in the approval process that will serve to allow and/or regulate the homeownership conversion process. Those items that may be regulated include:

- Maximum sales prices,
- A timeline regulating notification and acceptance deadlines,
- Secondary disposition options in the case that a sale is not feasible or desired,
- Characteristics of qualified buyers,
- Physical upkeep standards,
- Restrictions on resales within the extended use period, and
- First-time homeownership training.

APPENDIX A

Owners of Properties That Have Passed Y15

The University
of North Carolina
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Department of City and Regional Planning

Campus Box 3140
New East Building
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T 919-962-3983
F 919-962-5206
www.planning.unc.edu

January 23, 2008

<name and address>

Dear <name>,

My name is Laura Turner, and I am a graduate student at the University of North Carolina at Chapel Hill in the Department of City & Regional Planning. I am writing to you in regards to my graduate research project, which is concerned with preserving the affordability of small-scale Low Income Housing Tax Credit (LIHTC) properties. Public records indicate that you are the owner of a LIHTC rental property at <building address> in <city> that has recently turned 15 years in age.

As you may already know, the rents you are permitted to charge your tenants are likely restricted for a total of 30 years (15 years plus an additional 15 year extended use period) or more. You may sell the property after 15 years, but the standard options available to "exiting" owners are not well suited to individual investors of small-scale LIHTC properties.

With the permission of the North Carolina Housing Finance Agency (HFA), I am writing to inform you of a **new exit option** that the North Carolina HFA is willing to consider: **a sale of your LIHTC property to your tenant at an affordable price**. If feasible, this new option will allow the HFA to offer more flexibility to LIHTC investors and encourage affordable homeownership among low income tenants at the same time. My task is to collect feedback from owners and tenants to determine if there is sufficient interest, and to inform the HFA of my findings.

Please respond to this letter (contact information provided below) and inform me as to whether or not you are willing to consider a sale of your property to your tenant. Please include your preferred contact information regarding this issue, since there may be periodic updates. It may also be helpful for you to provide any information pertinent to why this option would or would not work for you, including, but not limited to the following:

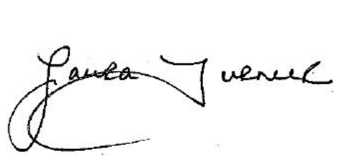
> *Do you wish to "exit" your property?*
> *Do you have an outstanding mortgage balance on the property?*
> *Do you have a sales price in mind?*

Have you determined the tax liability you may incur from a sale of the property?

Your response is voluntary, and will not be shared with your tenant(s) without your permission.

Please feel free to contact me with any questions or comments. I would appreciate it if you could respond by February 15th, 2008. In advance, I'd like to thank you for your time.

Sincerely,



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University of North Carolina at Chapel Hill
tvlaura@email.unc.edu
Work Phone: (919) 843-4615
Fax: (919) 843-2080

Ms. Turner is neither a real estate agent, nor a real estate broker, and is contacting you as a part of her graduate research with the permission of the North Carolina Housing Finance Agency. She does not work for the North Carolina Housing Finance Agency, nor is she conducting this inquiry with any direct assistance from them. Neither she nor any employee of the Housing Finance Agency will receive any compensation as the result of any sale that may be completed.

APPENDIX B

Owners of Properties That Have Not Passed Y15

UNC
COLLEGE OF
ARTS & SCIENCES

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of North Carolina
at Chapel Hill

Department of City and Regional Planning

Campus Box 3140
New East Building
Chapel Hill, NC 27599-3140

T 919-962-3983
F 919-962-5206
www.planning.unc.edu

January 28, 2008

<name and address>

Dear <name>,

My name is Laura Turner, and I am a graduate student at the University of North Carolina at Chapel Hill in the Department of City & Regional Planning. I am writing to you in regards to my graduate research project, which is concerned with preserving the affordability of small-scale Low Income Housing Tax Credit (LIHTC) properties. Public records indicate that you are the owner of a LIHTC rental property at <building address> in <city> that will turn 15 years of age within the next few years.

As you may already know, the rents you are permitted to charge your tenants are likely restricted for a total of 30 years (15 years plus an additional 15 year extended use period) or more. You may sell the property after 15 years, but the standard options available to “exiting” owners are not well suited to individual investors of small-scale LIHTC properties.

With the permission of the North Carolina Housing Finance Agency (HFA), I am writing to inform you of a **new exit option** that the North Carolina HFA is willing to consider: **a sale of your LIHTC property to your tenant at an affordable price**. If feasible, this new option will allow the HFA to offer more flexibility to LIHTC investors and encourage affordable homeownership among low income tenants at the same time. My task is to collect feedback from owners and tenants to determine if there is sufficient interest, and to inform the HFA of my findings.

Please respond to this letter (contact information provided below) and inform me as to whether or not you are willing to consider a sale of your property to your tenant. Please include your preferred contact information regarding this issue, since there may be periodic updates. It may also be helpful for you to provide any information pertinent to why this option would or would not work for you, including, but not limited to the following:

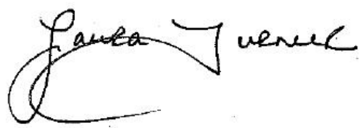
> *Do you wish to “exit” your property?*
> *Do you have an outstanding mortgage balance on the property?*
> *Do you have a sales price in mind?*

Have you determined the tax liability you may incur from a sale of the property?

Your response is voluntary, and will not be shared with your tenant(s) without your permission.

Please feel free to contact me with any questions or comments. I would appreciate it if you could respond by February 15th, 2008. In advance, I'd like to thank you for your time.

Sincerely,



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APPENDIX C

Tenants of Properties That Have Passed Y15

UNC COLLEGE OF ARTS & SCIENCES

The University
of North Carolina
at Chapel Hill

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Chapel Hill, NC 27599-3140

T 919-962-3983
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www.planning.unc.edu

January 23, 2008

<name and address>

Dear <name>,

My name is Laura Turner, and I am a graduate student at the University of North Carolina at Chapel Hill in the Department of City & Regional Planning. My graduate research project is on preserving the affordability of Low Income Housing Tax Credit (LIHTC) properties. I am writing you because public records indicate that you are the tenant of a LIHTC rental property that has recently turned 15 years in age.

As you may already know, the rent that you pay is likely restricted for a total of 30 years or more starting from the date that the building was placed into service. Under certain circumstances the LIHTC program allows the owner of a LIHTC property to exit the program (to sell) after 15 years. Please keep in mind that the rent you pay is probably NOT in jeopardy of increasing beyond current affordability limits, regardless of whether or not you experience a change of landlords.

I am writing simply to inform you that the North Carolina Housing Finance Agency (HFA) is considering a new exit strategy for owners that may also interest you, the tenant: allowing the owner to sell their property at an affordable price to the tenant.

With the permission of the North Carolina HFA, **I am writing to ask if you are interested in purchasing your property**. At this time, I am only asking if you are interested in the *possibility* of purchasing; you are not committing yourself to any transaction. My task is to collect feedback from owners and tenants to determine if there is sufficient interest, and to inform the HFA of my findings.

Please respond to this letter (contact information provided below) and inform me as to whether or not you are willing to consider purchasing your property. Please include your preferred contact information regarding this issue, since there may be periodic updates. It may also be helpful for you to provide any information pertinent to why this option would or would not work for you, including, but not limited to the following:

Have you ever owned a home?
Do you plan on becoming a homeowner in the near future?
Do you like your unit's location and appearance?

Your response is voluntary, and will not be shared with your landlord without your permission. If you would like more information on homeownership products and services offered by the North Carolina HFA, please visit their website at **http://www.nchfa.com**.

Please feel free to contact me with any questions or comments. I would appreciate it if you could respond by February 15th, 2008. In advance, I'd like to think you for your time.

Sincerely,

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APPENDIX D

Tenants of Properties That Have Not Passed Y15

The University
of North Carolina
at Chapel Hill

Department of City and Regional Planning

Campus Box 3140 T 919-962-3983
New East Building F 919-962-5206
Chapel Hill, NC 27599-3140 www.planning.unc.edu

January 25, 2008

<name and address>

Dear <name>,

My name is Laura Turner, and I am a graduate student at the University of North Carolina at Chapel Hill in the Department of City & Regional Planning. My graduate research project is on preserving the affordability of Low Income Housing Tax Credit (LIHTC) properties. I am writing you because public records indicate that you are the tenant of a LIHTC rental property that will turn 15 years of age in <year>.

As you may already know, the rent that you pay is likely restricted for a total of 30 years or more starting from the date that the building was placed into service. Under certain circumstances the LIHTC program allows the owner of a LIHTC property to exit the program (to sell) after 15 years. Please keep in mind that the rent you pay is probably NOT in jeopardy of increasing beyond current affordability limits, regardless of whether or not you experience a change of landlords.

I am writing simply to inform you that the North Carolina Housing Finance Agency (HFA) is considering a new exit strategy for owners that may also interest you, the tenant: allowing the owner to sell their property at an affordable price to the tenant.

With the permission of the North Carolina HFA, **I am writing to ask if you would be interested in purchasing your property once it reaches 15 years in age**. At this time, I am only asking if you are interested in the *possibility* of purchasing; you are not committing yourself to any transaction. My task is to collect feedback from owners and tenants to determine if there is sufficient interest, and to inform the HFA of my findings.

Please respond to this letter (contact information provided below) and inform me as to whether or not you are willing to consider purchasing your property. Please include your preferred contact information regarding this issue, since there may be periodic updates. It may also be helpful for you to provide any information pertinent to why this option would or would not work for you, including, but not limited to the following:

Have you ever owned a home?
Do you plan on becoming a homeowner in the near future?
How long do you plan on staying in your current unit as a renter?
Do you like your unit's location and appearance?

Your response is voluntary, and will not be shared with your landlord without your permission. If you would like more information on homeownership products and services offered by the North Carolina HFA, please visit their website at **http://www.nchfa.com**.

Please feel free to contact me with any questions or comments. I would appreciate it if you could respond by February 15th, 2008. In advance, I'd like to think you for your time.

Sincerely,

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APPENDIX E

North Carolina Housing Finance Agency - Mortgage Products and Services[8]

The North Carolina HFA has access to several mortgage products aimed at assisting first-time homeowners, which they may use in facilitating any future homeownership conversion sales. The HFA is not a lender, but has access to a large network of preferred state mortgage lenders that participate in HFA mortgage programs, and they can provide products that can assist a low-income homebuyer in obtaining a mortgage in the private market. These programs include:

- FirstHome Mortgages,
- Down payment assistance up to $7,000, and
- Mortgage Credit Certificates (MCC)

FirstHome Mortgage

A FirstHome Mortgage is a fixed-rate, 30-year, low interest rate mortgage made available to low-income first-time homeowners. To qualify, the prospective buyer's income and the purchase price may not exceed limits based on the county within which the sale takes place.

Maximum income limits for the 13 counties containing our sample properties range from $53,000 to $71,000. For all counties within which our sample properties are located, the maximum purchase price for FirstHome mortgages with or without down payment assistance is $190,000. All tenants make less than the maximum income limits, listed in Exhibit 11.

Although our current data does not tell us if the tenants have ever been homeowners, tenants who have not owned a home within 3 years can qualify as a first-time homebuyer. Additionally, the HFA has indicated that all tenants within the LIHTC program will qualify as first-time homebuyers.

Down Payment Assistance

Potential homebuyers may also be eligible for down payment assistance up to $7,000. The assistance takes the form of an interest-free, deferred second mortgage with a balloon principal payment due after 30 years. To qualify for down payment assistance, the homebuyer must meet even more restrictive income limits than would otherwise be required for a FirstHome Mortgage, delineated below.

Twenty nine tenants do not meet the income limits to receive down payment assistance.

---

[8] Products and services offered by the North Carolina HFA to low-income homebuyers are detailed on their website at http://www.nchfa.com.

EXHIBIT 14: Maximum Income Limits and Maximum Purchase Price Limits for First Time Homebuyers to Receive FirstHome Mortgages

County	Income Limits (max)		Purchase Price Limits (max)	
	FirstHome Mortgage	FirstHome Mort. w/ Downpayment	FirstHome Mortgage	FirstHome Mort. w/ Downpayment
Wake	71,000	40,100	190,000	190,000
Wilson	53,000	27,800	190,000	190,000
Guilford	56,000	31,550	190,000	190,000
Vance	53,000	26,400	190,000	190,000
Franklin	71,000	40,100	190,000	190,000
Granville	53,000	30,150	190,000	190,000
Warren	53,000	26,400	190,000	190,000
Gaston	64,000	36,050	190,000	190,000
Craven	53,000	27,800	190,000	190,000
Durham	61,500	39,950	190,000	190,000
Catawba	53,000	28,850	190,000	190,000
Harnett	53,000	27,250	190,000	190,000
Mecklenburg	64,000	36,050	190,000	190,000
Nash	53,000	27,350	190,000	190,000

Mortgage Credit Certificates

The North Carolina HFA can also assist homebuyers who meet the FirstHome Mortgage income limits, yet do not qualify because of other issues, by issuing Mortgage Credit Certificates directly to eligible tenants. Upon receipt of a Mortgage Credit Certificate, a homebuyer may claim a special tax credit on their federal income tax return in addition to the standard mortgage interest deduction. The amount of the Certificate is equal to 25% of the annual interest paid on the recipient's mortgage for standard single family homes. Essentially, a Mortgage Credit Certificate is designed to free up income to be used towards housing costs by decreasing the recipient's tax burden.

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