MEMORANDUM

TO: Pete Sprague, Assembly President

Members, Kenai Peninsula Borough Assembly

THRU: Dale Bagley, Mayor

FROM: Shane Horan, Director of Assessing

DATE: October 16, 2003

SUBJECT: Valuation of Low-Income Housing Tax Credit (LIHTC)

Apartment Projects

<u>Introduction:</u>

According to Alaska Statute 29.45.110(d)(1), the assessor is required to value low-income housing tax credit projects existing as of January 1, 2001, the effective date of the legislation, based on the actual income derived from the property. This can result in a value that is less than "full and true value" as defined for other property. These projects must be qualified and recognized under the United States Tax Code, 26 U.S.C. 42.

AS 29.45.110(d)(2) also requires the governing body to determine by ordinance whether projects that qualify after January 1, 2001, shall be assessed based on income derived in the same way as are prequalified LIHTC projects. If the assembly does not exempt newly qualified parcels from the income method, it shall determine on a parcel-by-parcel basis whether the property shall be assessed based on the actual income derived (also known as the restricted rent income approach) or at full and true value.

To date, the Bayview Apartments (18 Units) in Seward has been receiving the benefit of the restricted rent income approach to value for the years 2001, 2002, and 2003. There are two other LIHTC projects (26-Unit Parkview Apartments in Soldotna and the proposed 32-Unit Pacific Park project in Seward) whose owners have expressed an interest in receiving the restricted rent valuation. In accordance with state statute, the assembly may determine whether or not it wishes these two newer projects to receive the preferential assessment based on the restricted rents, to be assessed at traditional full and true value, or to choose the method of taxation on a case-by-case basis.

If adopted, this ordinance would allow all such low-income housing tax credit parcels to be assessed based on the restricted rent income derived from the property.

Background:

The LIHTC program was created as a result of the 1986 income tax reform act (eliminating rapid depreciation). It is a voluntary program whereby the investor/developer agrees to restrict rent charged to tenants in return for distributed tax credits received over ten years. This LIHTC gives investors a dollar-for-dollar reduction in their federal tax liability in exchange for providing financing to develop affordable rental housing.

Rental properties that qualify for the LIHTC tend to have both lower debt service payments and lower vacancy rates than market-rate rental housing. LIHTC properties typically experience a relatively quick lease-up and offer strong potential economic returns, primarily due to the existence of the credit. LIHTC properties are often packaged as limited partnerships because they afford limited liability to their investors.

Tax credit housing is generally located where the land costs are lower and the tax credit allowable rents are sufficient. Economics generally make it more difficult to build LIHTC housing in major cities because land costs are higher and low-income rents are substantially below market rate. With the help of additional federal, state and local subsidies, many developers have made these projects financially feasible.

Program Administration:

Since the LIHTC's inception, states have received $1.25 per resident each year from the federal government. For example, if California has approximately 33 million residents the state would receive $41.25 million in LIHTC volume cap ($1.25 x 33,000,000 = $41,250,000.)

Within guidelines set by the Internal Revenue Service (IRS), state housing agencies such as Alaska Housing Finance Corporation (AHFC) administer the LIHTC program. AHFC reviews tax credit applications submitted by developers and allocates the credits. The IRS requires that state allocation plans prioritize projects that serve the lowest-income tenants and ensure affordability for the longest period.

Once the applicants secure a tax credit reservation, the developer must leverage the financial resources for the development. Under a typical LIHTC transaction, a developer must secure a conventional loan from a private mortgage lender or public agency, gap financing from public or private sources, and equity from the developer or private investor in exchange for the tax credits.

Once the project is built, AHFC ensures that it meets the LIHTC eligibility requirements. AHFC is responsible for monitoring LIHTC property owners by requiring them to certify on an annual basis that they are renting units to qualified low-income tenants. If property owners are found to be out of compliance, they can lose their credits.

Selling Credits:

Most developers sell the tax credits for cash, which is channeled into the development. The developer can either sell the tax credits directly to an investor or to a syndicator, who acts as a broker between the developer and investor.

The LIHTC is a complex income tax area, requiring owners and investors to comply with numerous administrative rules and regulations such as maintaining the required number of income-eligible tenants and ensuring that the appropriate documents and records are filed and maintained.

Findings from other Communities:

Anchorage:

According to Marty McGee, Assessor for the Municipality of Anchorage, an ordinance was submitted in February of 2001 supporting the rent-restricted valuation. The ordinance was postponed, and in May of 2001 was completely rescinded. All LIHTC projects are assessed at their full and true value.

Matanuska-Susitna Borough:

According to Allen Black, Assessor for the Mat-Su Borough, there is no ordinance in place. The restricted rent valuation is provided to those projects that qualify, apply timely and provide all requested financial information.

Fairbanks North Star Borough:

According to Karl McManus, Deputy Assessor, they do have the 1910 Turner Street Associates LIHTC, yet there is no ordinance in place. The value approximates full and true value as this project also had a subsidy by AHFC at 1.5% interest. The lower rents when divided by a lower capitalization rate yielded a value similar to other multi-family projects.

City and Borough of Juneau:

According to Tom Pitts, Assessor, there are six projects (Coho, 52 Units; Chinook, 64 Units; Sleepy Spruce, 24 Units; MacKinnon Apartments, 23 Units; Strasbaugh Place, 7 Units; and Orca Point, 40 Units) receiving the benefit of the lower assessment based on their restricted rents. They are currently working on an ordinance addressing this issue.

Ketchikan:

According to Rupert Henry, Chief Appraiser, they do have the 22-unit Glacier Park Apartments receiving the benefit of a reduced assessment as allowed by their Ordinance 45.11.055 (b).

Sitka:

According to Richard Anderson, Assessor, there are no projects receiving the benefit of the lower assessment based on restricted rents. No ordinance is in place at this time.

Kodiak Island Borough:

According to Pat Carlson, Borough Manager, there are no LIHTC's and no ordinance in place addressing this issue.