DEPARTMENT OF TAXATION
2022 Fiscal Impact Statement

1. **Patron** Luke E. Torian

2. **Bill Number** HB 824
House of Origin:
X **Introduced**
____ **Substitute**
____ **Engrossed**

Second House:
____ **In Committee**
____ **Substitute**
____ **Enrolled**

3. **Committee** House Finance

4. **Title** Virginia Housing Opportunity Tax Credit; Expansion to Qualified Specialty Population Projects

5. **Summary/Purpose:**

This bill would allow a Virginia Housing Opportunity Tax Credit for qualified specialty population projects. Under current law, the credit is only available to qualified projects.

The bill would define a "qualified specialty population project" as a qualified low-income building, as defined under federal tax law, that is located in Virginia, is placed in service on or after January 1, 2022, and is issued an eligibility certificate that creates housing for individuals who:

- Have been issued an intellectual disability or developmental disability waiver;
- Require behavioral health treatment or services; or
- Require treatment or services for substance use and abuse recovery.

Any Virginia Housing Opportunity Tax Credits allowed to qualified specialty population projects would be subject to the $2.5 million per calendar year cap. This cap would be in addition to the $15 million per calendar year cap currently in place for qualified projects

If enacted during the regular session of the 2022 General Assembly, this bill would become effective July 1, 2022.

6. **Budget amendment necessary:** Yes.
Item(s): Page 1, Revenue Estimates

7. **Fiscal Impact Estimates are:** Preliminary. (See Line 8.)

8. **Fiscal implications:**

Administrative Costs

The Department of Taxation ("the Department") considers implementation of this bill as routine and does not require additional funding. The Virginia Housing Development Authority ("VHDA") states that any costs that it may incur would have no state budgetary impact, as it is permitted by law to charge fees to developers to cover any costs. In addition, VHDA is self-supporting and does not receive state appropriations.

Revenue Impact

This bill would result in an unknown negative General Fund revenue impact beginning in Fiscal Year 2023. The extent to which taxpayers with qualified specialty population projects would apply for and claim the credit provided by this bill is unknown. However, because credits for qualified specialty population projects would be subject to an annual cap, the impact to the General Fund would not exceed $2.5 million per fiscal year.

9. Specific agency or political subdivisions affected:

Department of Taxation
Virginia Housing Development Authority

10. Technical amendment necessary: Yes.

This bill does not currently specify an effective date. As a result, it would become effective July 1, 2022, which would be in the middle of the taxable year for most taxpayers. Accordingly, the Department recommends a technical amendment to make this credit effective for taxable years beginning on or after January 1, 2022.

In addition to the Department's comments above, VHDA has provided the following comments:

- VHDA reads the bill as increasing the current $15 million amount of annual credits by $2.5 million to $17.5 million.

  > "G. The total amount of tax credits authorized under this article shall not exceed $15 million per calendar year for qualified projects and shall not exceed $2.5 million per calendar year for qualified specialty population projects."

  If the $2.5 million is meant to be a subset of the $15 million, VHDA suggests that should be clarified.

- The definition of "Qualified specialty population project" does not set a minimum or maximum number of units to be set-aside for the targeted populations in order to meet the definition. VHDA assumes this is intended to give Virginia Housing flexibility to define that in its regulations or program guides, and could do that.

11. Other comments:

Federal Low-Income Housing Tax Credit

The federal low-income housing tax credit ("LIHTC") is a nonrefundable income tax credit that was created by the Tax Reform Act of 1986 to provide an incentive for the development and rehabilitation of affordable rental housing. LIHTCs are awarded to developers of qualified rental projects via a competitive application process administered by state housing finance authorities. Typically, developers will effectively “sell” their tax credits to outside investors by entering into limited partnerships or limited liability companies with investors, with 99.99 percent of the profits, losses, depreciation, and tax credits being allocated to the investors as a partner in the partnership or member in the limited liability company. This reduces the debt developers would otherwise have to incur and the equity they would otherwise have to contribute. With lower financing costs, tax credit properties can potentially offer lower, more affordable rents.

Two types of LIHTCs are available depending on the nature of the construction project. The so-called 9 percent credit is generally reserved for new construction, while the so-called 4 percent credit is typically used for rehabilitation projects and new construction that is financed with tax-exempt bonds. Each year, for ten years, a tax credit equal to roughly 4 percent or 9 percent of a project’s qualified basis (cost of construction) is claimed. The applicable credit rates have historically not actually been 4 percent and 9 percent. Instead, the credit rates have fluctuated in response to market interest movements so that the program has delivered a subsidy equal to 30 percent of the present value of a project’s qualified basis in the case of the 4 percent credit, and 70 percent in the case of the 9 percent credit. For both the 4 percent and 9 percent credit it is the subsidy levels (30 percent or 70 percent) that are explicitly specified under federal tax law, not the credit rates. Since 1986, the 4 percent rate has ranged between 3.15 percent and 3.97 percent, and the 9 percent credit between 7.35 percent and 9.27 percent. Since 2008, however, there has been a floor under the 9 percent credit below which the new construction credit rate cannot fall.

The process of allocating, awarding, and then claiming the LIHTC is complex and lengthy. The process begins at the federal level with each state receiving an annual LIHTC allocation in accordance with federal law. State housing agencies then allocate credits to developers of rental housing according to federally required, but state created, allocation plans. The process typically ends with developers effectively selling allocated credits to outside investors in exchange for equity.

Taskforce and Report to Study Establishment of Virginia Credit

During the 2020 General Assembly Session, House Bill 810 was enacted, which required the Department of Housing and Community Development (“DHCD”) and the Virginia Housing Development Authority (“VHDA”) to convene a stakeholder advisory group (“Task Force”) to:

- Determine the most effective and efficient way to administer a Virginia housing opportunity tax credit program,
- Develop draft legislation establishing such an affordable housing credit program, and
- Conduct financial modeling to determine the fiscal impact of such a program to Virginia.

Such legislation also required the Task Force to report its recommendations to the Governor, the Secretary of Commerce and Trade, the Director of the DHCD, and the commissioners of the VHDA by September 1, 2020. Such report, the Report of the Virginia Housing Opportunity Tax Credit Task Force, was published in September 2020.

Virginia Housing Opportunity Tax Credit

As a result of this taskforce and report, during its 2021 Special Session I, the General Assembly enacted legislation to establish the Virginia Housing Opportunity Tax Credit for certain low-income building projects. The amount of such credit is substantially similar to the amount of federal LIHTC allocated or allowed by VHDA to such projects. The credit is allowed for each project for each year of the federal credit period, in an amount equal to the amount of federal LIHTC allocated or allowed by VHDA to such project. Therefore, for each qualified project, the credit is allowable for up to 10, consecutive taxable years beginning with the date a building is placed in service or the following year, at the election of the taxpayer. However, there is no reduction in the tax credit allowable in the first year of the credit period due to a calculation based on qualified occupancy under federal tax law.

The credit is subject to a $15 million annual credit cap. To be qualified, the project must be a qualified low-income building, as defined under federal law, that is:

- Located in Virginia;
- Placed in service on or after January 1, 2021; and
- Issued an eligibility certificate.

If a portion of any federal low-income housing credits taken on a qualified project is required to be recaptured or is otherwise disallowed during the credit period, the taxpayer claiming Virginia Housing Opportunity Tax Credit with respect to such project must recapture a portion of such credits. The percentage of credits subject to recapture is equal to the percentage of federal low-income housing credits subject to recapture or otherwise disallowed during such period. Any tax credits recaptured or disallowed will increase the income tax liability of the qualified taxpayer who claimed the tax credits in a like amount and must be included on the tax return of the taxpayer submitted for the taxable year in which the recapture or disallowance event is identified.

VHDA is required to administer the Virginia Housing Opportunity Tax Credit program and is authorized to promulgate the regulations and guidelines necessary to implement and administer it. Such regulations and guidelines may include the imposition of application, allocation, certification, and monitoring fees designed to recoup the costs of VHDA in administering the program. VHDA may also promulgate regulations and guidelines in consultation with the Department to allow a qualified project to elect in its application to the VHDA to sell all or any portion of its credits awarded to one or more unrelated taxpayers. Regulations and guidelines regarding the sale of credits, if promulgated, may not be allowed to take effect prior to January 1, 2023, and may not apply to credits awarded prior to January 1, 2023.

Proposed Legislation

This bill would allow a Virginia Housing Opportunity Tax Credit for qualified specialty population projects. Under current law, the credit is only available to qualified projects. The bill would define a "qualified specialty population project" as a qualified low-income building, as defined under federal tax law, that is located in Virginia, is placed in service on or after January 1, 2022, and is issued an eligibility certificate that creates housing for individuals who:

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Any Virginia Housing Opportunity Tax Credits allowed to qualified specialty population projects would be subject to the $2.5 million per calendar year cap. This cap would be in addition to the $15 million per calendar year cap currently in place for qualified projects

If enacted during the regular session of the 2022 General Assembly, this bill would become effective July 1, 2022.

Similar Legislation

House Bill 843 and **Senate Bill 47** would increase the annual credit cap for the Virginia Housing Opportunity Tax Credit from $15 million per calendar year to a $150 million per year reservation cap that could be claimed over a 10-year period and that would be subject to additions due to prior year unused caps and recapture or disallowance.

cc : Secretary of Finance

Date: 1/30/2022 JJS
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