DEPARTMENT OF TAXATION
2022 Fiscal Impact Statement

1. **Patron** Robert S. Bloxom, Jr.

2. **Bill Number** HB 843

   House of Origin:
   X **Introduced**
   ____ **Substitute**
   ____ **Engrossed**

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

3. **Committee** House Finance

4. **Title** Enhancement of the Virginia Housing Opportunity Tax Credit

5. **Summary/Purpose:**

This bill would permit the Virginia Housing Development Authority ("VHDA") to reserve Virginia Housing Opportunity Tax Credits with respect to certain low-income building projects that newly qualify for the credit in a given fiscal year or other 12-month period designated by the VHDA. The amount of credits that VHDA would be permitted to reserve with respect to such projects would be limited to $150 million plus:

- The amount, if any, by which the $150 million reservation cap for the preceding fiscal year or other 12-month period exceeds the tax credits awarded by the VHDA in that year or 12-month period; and

- The amount of tax credits recaptured or otherwise disallowed in the preceding fiscal year.

Each annual group of new qualified low-income building projects would be eligible to receive a separate reservation of credits of $150 million plus any additions as described above. The $150 million per fiscal year or 12-month period reservation cap would replace the $15 million per calendar year cap imposed by current law.

Credits awarded to a given low-income building project would be claimable on the Virginia income tax return in an amount equal to the lesser of the amount of federal low-income housing tax credit ("LIHTC") allocated or allowed by VHDA to such qualified project, except that there would be no reduction in the tax credit allowable in the first year of the credit period due to the calculation under federal law, or one-tenth of the reserved tax credit amount stated in the reservation notice. Taxpayers would continue to be permitted to claim credits for 10 years.

This bill would make other changes to how taxpayers compute their tax credits and how VHDA would be required to administer the tax credit. This bill would repeal language authorizing an election to sell all or any portion of its credits awarded to one or more unrelated taxpayers.

This bill would be effective for fiscal years or other 12-month period designated by the VHDA beginning on and after January 1, 2021, but before July 1, 2025.

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

7. **Fiscal Impact Estimates are:** Unknown. (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 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 a significant unknown negative General Fund revenue impact beginning in Fiscal Year 2024. The extent to which taxpayers with qualified projects would apply for and claim the credit provided by this bill is unknown. This bill would be subject to an annual reservation cap for new projects of $150 million plus any additions as permitted in the bill. Each annual group of new qualified low-income building projects would be eligible to receive a separate reservation of credits of $150 million plus any additions. However, taxpayers would claim reserved credits on their tax return over a 10-year period subject to the limitation that the credit amount equal the lesser of:

- The amount of federal LIHTC allocated or allowed by VHDA to such qualified project, except that there would be no reduction in the tax credit allowable in the first year of the credit period due to the calculation under federal law, or
- One-tenth of the reserved tax credit amount stated in the reservation notice.

In addition, because this bill would provide a unique reservation of credits for each annual group of new qualified low-income building projects, credit claims would be permitted to stack together. This may work to ultimately increase the revenue impact of this bill by $15 million each fiscal year after Fiscal Year 2024 until either:

- A $75 million per fiscal year maximum revenue impact is reached if the sunset date of this bill is not subsequently extended; or
- A $150 million per fiscal year maximum revenue impact is reached if the sunset date of this bill is subsequently extended.

For example, if the reservation of credits is limited to $150 million per fiscal year, the negative revenue impact of this bill would generally be limited to $15 million in Fiscal Year 2024; $30 million in Fiscal Year 2025; $45 million in Fiscal Year 2026; $60 million in Fiscal Year 2027; and $75 million in Fiscal Year 2028. However, this does not account for additional credits that may be added or credits that are not utilized by taxpayers, which could further increase the negative revenue impact in those years.

9. Specific agency or political subdivisions affected:

Department of Taxation
Virginia Housing Development Authority

10. Technical amendment necessary: Yes.

As currently written, the $150 reservation cap under this bill would be increased by the amount of tax credits recaptured or otherwise disallowed in the preceding fiscal year. This recapture and disallowance language would not address the situation where VHDA chooses to use a 12-month period other than a fiscal year, as allowed by this bill. In addition, it is unclear how this aggregate recapture and disallowance amount would be determined. To the extent it is determined based on tax returns filed with the Department reporting recapture and/or credit disallowance, then it would vary depending on when taxpayers choose to file their returns or amended returns, among other factors, and it would be unclear how the aggregate recapture amount could be accurately determined. In addition, even if this amount could be determined, there may be confidentiality issues because state law generally prohibits the Department from sharing confidential taxpayer information.

In addition to the Department's comments above, VHDA provides the following comments regarding Senate Bill 47, which it states may also apply to this bill:

1. The proposed amendments to the Virginia Housing Opportunity Tax Credit statute create a $750 million Virginia Housing Opportunity Tax Credit program with a ten-year "stacking" of credits. (Lines 109-113). We have already received comments from non-profits concerned that this proposed program size may negatively affect state budget contributions to the Virginia Housing Trust Fund.

2. A potential issue in program size is that the amendments provide the Virginia Housing Opportunity Tax Credit award to a development shall "not be less than one-half of the aggregate amount of the federal low-income housing tax credit allocated or allowed to the qualified project" subject to an overall annual program cap of $150 million. (Lines 51-52).

   However, it is possible Virginia Housing could issue more than $300 million (twice the Virginia Housing Opportunity Tax Credit cap) of federal credits in a year, given pending federal legislation to increase the annual federal cap, the recent uptick in our federal 4 percent LIHTC program, and our ability to pre-allocate federal credits.

   It also creates timing and accounting issues for Virginia Housing in administering the Virginia Housing Opportunity Tax Credit program, because we approve 4 percent LIHTC applications on a rolling basis throughout the year and the total federal credits issued per year is not known until the very end of the year.

While exceeding $300 million of federal credits (and therefore more than $150 million of Virginia Housing Opportunity Tax Credits) may not be an issue in the future, it would be helpful for Virginia Housing to have flexibility in the minimum amount of Virginia Housing Opportunity Tax Credits awarded per deal. Also, Virginia Housing would want clarification that it can continue to award federal credits in a fiscal year, even after the Virginia Housing Opportunity Tax Credit cap has been met.

3. By using the word "shall" in Line 48, the amendments provide that all developments receiving an award of federal credits also receive an award of Virginia Housing Opportunity Tax Credits. (Lines 46-50). This would remove flexibility for Virginia Housing to prioritize (in its Qualified Allocation Plan (QAP) and/or Virginia Housing Opportunity Tax Credit regulations) targeted initiatives, development types or locations, tenant populations or other state priorities in selecting federal credit deals to also receive Virginia Housing Opportunity Tax Credits (or to receive standalone Virginia Housing Opportunity Tax Credits). We have already received comments from non-profits also stating this same issue.

   These amendments would also increase administrative work for VH staff, in that more documentation packages would be required than if fewer deals were selected for Virginia Housing Opportunity Tax Credits with higher individual award amounts.

   Virginia Housing has also received comments from developers who insist they could potentially want federal credits and no state credits. This is due mainly to: (i) complexity of finding syndicators/investors interested in both credits or, alternatively, separate syndicators/investors for federal and state credits, and (ii) concern that an allocation of Virginia Housing Opportunity Tax Credits will reduce their award of federal credits, which will likely reduce their overall tax credit equity because federal credits receive a higher per credit price when sold.

4. The amendments strike the option for a "certificated" program. (Lines 104-108). Such a program was the alternative proposal in the HB 810 report on a potential state credit. We have already received comments in opposition to this change from the non-profits that supported the alternative proposal.

5. In 2021, Virginia Housing issued award letters for $15 million of Virginia Housing Opportunity Tax Credits assuming a one-year credit period. The new amendments clarify that the Virginia Housing Opportunity Tax Credit period is ten years. (Lines 10, 15). Virginia Housing thinks that the one-year credit period for deals awarded in 2021 should be specifically grandfathered in any amendments leading to a ten-year credit period for Virginia Housing Opportunity Tax Credits. Note that this does not result in any loss of the proposed $750 million in credits because clause (ii) in Line 115 carries forward any unused credits in prior years.

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 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 ten, 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.

Sunset Dates for New Income Tax Credits and Sales Tax Exemptions

Section 3-5.14 of the 2021 Appropriation Act provides that any new sales tax exemption or tax credit enacted by the General Assembly after the 2019 Session, but prior to the 2024 Session, must have a sunset date of not later than June 30, 2025.

Proposed Legislation

This bill would permit the Virginia Housing Development Authority ("VHDA") to reserve Virginia Housing Opportunity Tax Credits with respect to certain low-income building projects that newly qualify for the credit in a given fiscal year or other 12-month period designated by the VHDA. The amount of credits that VHDA would be permitted to reserve with respect to such projects would be limited to $150 million plus:

- The amount, if any, by which the $150 million reservation cap for the preceding fiscal year or other 12-month period exceeds the tax credits awarded by the VHDA in that year or 12-month period; and

- The amount of tax credits recaptured or otherwise disallowed in the preceding fiscal year.

Each annual group of new qualified low-income building projects would be eligible to receive a separate reservation of credits of $150 million plus any additions as described above. The $150 million per fiscal year or 12-month period reservation cap would replace the $15 million per calendar year cap imposed by current law.

Upon issuance of an eligibility certificate to the owner of a qualified project, a Virginia Housing Opportunity Tax Credit would be allowed for each qualified project for each year of the 10-year credit period, in an amount equal to the lesser of:

- The amount of federal low-income housing tax credit ("LIHTC") allocated or allowed by VHDA to such qualified project, except that there would be no reduction in the tax credit allowable in the first year of the credit period due to the calculation under federal law, or

- One-tenth of the reserved tax credit amount stated in the reservation notice ("one-tenth rule").

Under current law, there is no one-tenth rule.

This bill would provide that VHDA would award Virginia Housing Opportunity Tax Credits for the owner of the qualified project upon approving a federal LIHTC to a qualified project pursuant to the VHDA's qualified allocation plan, as defined under federal tax law. However, this bill would provide that such reservation may not result in exceeding the per fiscal year or per 12-month period reservation cap. The reserved tax credit would not be permitted to be less than one-half of the aggregate amount of the federal LIHTC allocated or allowed to the qualified project under VHDA's qualified allocation plan for all years of the project's 10-year credit period. VHDA would be required to send written notice of the reservation to the owner of the qualified project. The notice would be required to state the aggregate amount of housing opportunity tax credit awarded for all 10 years of the qualified project's credit period and stipulate that receipt of the tax credit is contingent upon issuance of an eligibility certificate.

This bill would repeal language authorizing an election to sell all or any portion of its credits awarded to one or more unrelated taxpayers.

This bill would be effective for fiscal years or other 12-month period designated by the VHDA beginning on and after January 1, 2021, but before July 1, 2025.

Similar Bills

Senate Bill 47 is substantially similar to this bill.

House Bill 824 would expand the Virginia Housing Opportunity Tax Credit so that it applies to certain qualified specialty population projects.

cc : Secretary of Finance

Date: 1/30/2022 JJS
HB843F161