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LIHTC Equity Calculation Overview

Determining the amount of Low Income Housing Tax Credit equity that can be secured is often confusing for developers.

The following paper provides a general overview of the methodology for determining the LIHTC equity that can be delivered to a project.

Step One - Determine "Qualified Basis"

Eligible Basis	X	Applicable Fraction	X	Basis Boost *(not eligible for all properties)*	=	**Qualified Basis**

Let's break down each component.

The Eligible Basis of a project is:

- The total development cost of a project *minus* certain non-depreciable costs such as permanent loan fees/costs, tax credit fees, reserves, grants.
- Land value (or land acquisition cost) is also not included. An existing building's value can generate acquisition credits however it must have been placed in service (or last rehabbed) more than 10 years ago, and be substantially rehabbed as part of the transaction[1].
- Hard costs, architectural and engineering fees, developer's fees, construction interest, and contractor's profit *are* eligible.

For preliminary sizing purposes, a general ballpark of eligible costs is all that is needed. As you progress further in the process, a LIHTC investor partner/syndicator can provide a more granular analysis of eligible versus ineligible costs.

The Applicable Fraction is the percentage of units that will meet LIHTC rent restrictions (unit rents limited to 20-40% *of* 50-60% of Area Median Income or potentially higher if income averaging is used). Put simply, if 100% of the units meet LIHTC rent restrictions, the applicable fraction is 100%. If 50% meet LIHTC rent restrictions, the applicable fraction is 50%, etc. Typically *most LIHTC properties are 100% affordable* or close to 100% affordable as this maximizes the amount of credits available and is preferable for LIHTC investors.

The Basis Boost is a reward given to developments in economically disadvantaged areas called "DDA" or "QCT". If eligible, the property receives a **30% boost** in credit amount (note: acquisition credits are not boosted). Determining these locations is available with free online tools such as this Novogradac map - https://www.novoco.com/resource-centers/affordable-housing-tax-credits/data-tools/qct-dda-mapping-tool

[1] https://lizbramlet.wordpress.com/2012/01/03/qualifying-for-aquisition-credits/

📌*Example:* A project with an eligible basis of $10,000,000, with 100% LIHTC units, in a "DDT/QCT" qualified area, has a $13mm qualified basis. 📌

Step Two - Determine Applicable Percentage

Qualified Basis	X	**Applicable Percentage**	=	Annual Tax Credits

The Applicable Percentage varies depending on financing structure:

- The 9% tax credit applicable percentage is eligible for construction and sub rehab. Securing 9% tax credits requires a competitive application process as it provides higher leverage. The applicable percentage in these transactions is 9.00%. Confusingly, even in a 9% eligible transaction, the lower 4% tax credit rate is used for the acquisition cost of existing buildings to be rehabbed (if applicable). This is done to prevent an inordinate amount of tax credit equity to be generated simply through acquisitions.

- The 4% tax credit applicable percentage is fixed at 4.00% in all 4% LIHTC scenarios. These lower leverage credits are non-competitive. For example, when tax exempt bonds are used to secure LIHTC (which is the method used with HUD financing), the 4% credit rate is used for both construction/rehab and any applicable acquisition costs.

Please see the following chart from Novogradac:

Construction Method

Financing Method

	New Construction	Acquisition/ Rehabilitation
Non-Federally Subsidized (Perm Loan)	9% credits	Acq – 4% Rehab – 9%
Federally Subsidized (TE bonds)	4% credits	Acq – 4% Rehab – 4%

Or put another way by Westmont Advisors:

"A LIHTC property that consists solely of new construction and that does not use bond financing will qualify for the 9% credit. A property that is financed with tax-exempt bond financing will use only the 4% annual credit. A development that includes the purchase of an existing building or buildings for rehabilitation purposes and that does not use tax-exempt bond financing will use a combination of 4% and 9% credits; 4% for the acquisition and 9% for the construction."

📌Example: A tax-exempt bond deal combined with HUD financing qualifies for a (hypothetical) 4% tax credit. At a qualified basis of $13,000,000, this equals $520,000 in annual tax credits per year.📌

Step Three - Multiply Annual Credits by 10

Annual Tax Credits	X	10 Years	=	**Total Tax Credits**

Tax credits investors receive their return on investment for the first 10 years after a project is placed in service.

📌Example: $520,000 in annual tax credits per year multiplied by 10, = $5.2mm in total available tax credits.📌

Step Four - Investor Purchase Price Per Credit

Total Tax Credits	X	Investor Purchase Price Per Credit	=	**Equity delivered to project**

LIHTC investors are interested in purchasing tax credits, because they receive a dollar for dollar tax *credit* over a 10 year period *and* receive real estate losses (depreciation, etc) from the project which derives income. A good ballpark purchase price per credit is anywhere from 85 to 90 cents.

📌Example: Investors purchase the tax credits for a price per credit which is determined by a variety of factors. At 90 cents a credit, the investor would contribute $4,680,000 towards the project. **This is the LIHTC equity available for a project (and would potentially cover a Developer's Fee) at closing.** 📌

The following image from Westmont Advisors showcases the entirety of the calculation under both a 9% and 4% transaction. Of note, the "3.22%" in the right hand column is out of date - this would now be 4%.

	If using conventional financing (9% LIHTC)	If using tax-exempt bonds (4% LIHTC)
Total development costs	$21,000,000	$21,000,000
Less: Ineligible costs, including land	<1,000,000>	<1,000,000>
Eligible basis (Total LIHTC eligible costs)	20,000,000	20,000,000
Applicable fraction	100%	100%
Qualified basis (Eligible basis X Applicable fraction)	20,000,000	20,000,000
Applicable percentage (AFR)*	9.00%	3.22%
Annual credit before basis boost	1,800,000	644,000
Basis boost (130%)	540,000	--
Annual credit after basis boost	**2,340,000**	**644,000**
Total credit (Annual credit X 10)	**23,400,000**	**6,420,000**

*The applicable percentage varies based upon the AFR. The AFRs used in the example above are effective as of January 2016.

How to Calculate the Low Income Housing Tax Credit (LIHTC) - Westmont Advisors