

Minimum Set-Aside Election: Average Income Test

This Policy is intended to provide guidance to any applicant considering the average income test option for its minimum set-aside election. Until or unless the Internal Revenue Service or the Treasury Department issue conflicting guidance, OHFA adopts the provisions described herein related to the Average Income Minimum Set-Aside Election. OHFA may modify this or any related policies, based on subsequently enacted legislation or guidance provided by regulatory agencies, or for any other reason that it finds appropriate.

Background

The Consolidated Appropriations Act of 2018 (the “Act”) established a third minimum set-aside election, referred to as “average income” for IRC Section 42. The average income election is defined in Internal Revenue Code (IRC) Section 42(g)(1)(C). Critical requirements for the average income test include:

- 40% test - 40 percent or more of the units in a Project are both rent-restricted and occupied by individuals whose incomes do not exceed the imputed income limitation designated by the taxpayer.
- Designations - The taxpayer has designated the imputed income limitation of each unit.
- Average test - The average of the designated imputed income limitations for the Project does not exceed 60 percent of area median gross income (“AMGI”).
- 10-percent increments - The designated imputed income limitations are in 10 percent increments as follows:
 - 20 percent
 - 30 percent
 - 40 percent
 - 50 percent
 - 60 percent
 - 70 percent
 - 80 percent

The average income election applies to the designated rent and income limits of the units, not the incomes of individual tenant households.

Projects using 4% tax credits/tax-exempt bond financing

IRC Section 142 remains unchanged under the Act. A project subject to IRC Section 142 must still meet either the 20/50 or 40/60 minimum set-aside test. The project may elect average income for LIHTC as long as the unit mix selected will also meet the minimum set-aside test for bond compliance purposes.

Application Requirements

- Applicants that intend to make the average income election must indicate their intent to do so in the initial proposal and final application for the project.
- Unit designations must be equally distributed among bedroom sizes.

- The market study must demonstrate sufficient market demand for each proposed unit designation type contained in the application.
- Equity and debt commitment letters must explicitly state that they are based upon the average income test.
- Owners must disperse unit designations across all unit types in a manner that does not violate fair housing laws.

OHFA Review

- OHFA may require a legal opinion verifying that average income may be used in combination with any other subsidy applicable to the project/application.
- Applications will be underwritten based on each unit's designation as stated in the proposal application, final application, and 8609 submission. These designations will be documented in the Carryover Agreement or 42m Letter of Eligibility.
- OHFA will not permit developments to indicate their intention to elect average income at a later stage if the application was not previously underwritten to that test.

Unit Designations

While unit designations will be documented in the Carryover Agreement or 42m Letter of Eligibility, they will not be recorded in the restrictive covenant. The restrictive covenant will contain a general provision of the average required for income and rent designations. Other OHFA specific rent or income requirements may be stated separately in the restrictive covenant.

Multiple Building Election

- If the development contains more than one building, the project will be treated as a multiple building project and the owner must select "yes" on line 8b of IRS Form 8609.
- OHFA will permit exceptions to this requirement only upon demonstration of a compelling need.

Resyndication Restrictions

- Properties seeking a resyndication of credits are permitted to elect average income as a new minimum set-aside; however, the new election will not release the property from the affordability requirements defined in the original restrictive covenant. The original restrictive covenant, and its incorporated rent and income requirements, will remain in effect until the extended use period has ended.
- Owners resyndicating will record a new restrictive covenant. During the period in which both restrictive covenants are in effect, the owner will have to comply with the more stringent rules applicable to each particular unit.

Projects approved before 2018

- OHFA will permit developments approved in 2015, 2016, or 2017 to change their intended election, only if the following requirements have been met:
 - IRS Form 8609 has not been issued;
 - The development is not collecting credits on any portion of a multi-building project;
 - The restrictive covenant has not yet been recorded;

- The project consists of 100% low-income units;
- The project will be selecting 'yes' to line 8b. on Form 8609;
- All other affordability requirements are met; and
- The change would not impact the project's competitive score.
- The owner/developer MUST contact the Project Administration Analyst prior to requesting their Form 8609 to discuss the requirements, submit any needed documentation, and confirm that the development is permitted to change its intended election.
- OHFA may require the owner/developer to submit a re-underwriting fee.

Training and Technical Assistance

- OHFA may require proof that staff working on the development understand the requirements or have attended trainings specific to average income requirements.

Reporting of Noncompliance

- Project Failed to Meet Minimum Set-Aside Requirement
 - Failure to meet in first year. Failure to properly qualify eligible households to designated limits in 40 percent of the units (40% test), or failure to maintain an average of designations on all units of 60 percent AMI or below (average test), will prohibit the owner from ever claiming credits on the project.
 - Failure to meet after the first year. Failure to properly qualify eligible households in 40 percent of the units (40% test), or failure to maintain an average of designations on all units of 60 percent AMI or below (average test), will prohibit the owner from claiming credits on all units for that year.
- Household Income Above Income Limit upon Initial Occupancy

Each unit must be occupied with households that have a gross income less than or equal to the unit's designation. In the event that the household is not income eligible, the noncompliance will be reported on IRS Form 8823 under category 11a.

Noncompliance related to a specific unit does not impact the owner's ability to claim credits on units that are in compliance.

Additional detail and guidance regarding noncompliance can be found in the [IRS Guide for Completing Form 8823](#).

Compliance Monitoring

- Developments must meet the required minimum set-aside election no later than the end of the first year of the credit period.
- Development owners must submit Annual Owner Certifications, Tenant Data, and any other required documentation.
- OHFA will monitor for violations of the average income minimum set-aside election for year-end compliance to ensure compliance with the Qualified Allocation Plan.