

MINIMUM SET-ASIDE ELECTION: AVERAGE INCOME TEST

This policy is intended to provide guidance to any applicant considering the average income test option for their minimum set-aside election. The Ohio Housing Finance Agency (OHFA) may modify this, or any related policies, based on subsequently enacted legislation or guidance provided by regulatory agencies.

BACKGROUND

The Consolidated Appropriations Act of 2018 (the "Act") established a third minimum set-aside election, referred to as the "average income election", as defined in [Internal Revenue Code \(IRC\) 26 USC 42\(g\)\(1\)\(c\)](#). Summary of requirements include:

- **40% Test** – 40% or more of the units in a project are both rent-restricted and occupied by individuals whose income does 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% of area median gross income (AMGI).
- **10% Increments** – The designated imputed income limitations are in 10% increments as follows
 - 20%
 - 30%
 - 40%
 - 50%
 - 60%
 - 70%
 - 80%

Compliance and implementation of the average income election is defined in [Treasury Regulation 1.42-19. \(85 FR 68816\)](#). Summary of clarifications include:

- **Average income test low-income unit** – is a unit that is rent restricted, satisfies the imputed income limitation designated by the owner, is part of a "qualified group of units", and otherwise satisfies requirements of Section 42.
- **Qualified group of units** – includes units that must both satisfy the requirements to be an average income test low-income unit and the average of the imputed income limitations of the units in the group do not exceed 60% of AMGI. Put another way, an income averaging project will maintain compliance with the minimum set-aside as long as at least 40% of its units are low-income units with an average AMI of 60% or less.
- **Qualified group of units** – is used in two contexts in the final IRS regulations to meet the average income test: first, for the minimum set-aside test, and second, for the applicable fraction determination. The same or a different "qualified group of units" may be used for the average income test and the applicable fraction.
- Calculations for meeting tests are based on the designation and are not based on the incomes of individual tenant households.
- Units included in any "qualified group of units" must be identified as part of recordkeeping.

PROJECTS USING 4% TAX CREDITS/TAX-EXEMPT BOND FINANCING

IRC Section 1.42 remains unchanged under the Act. A project subject to Section 1.42 must still meet either the 20/50 or 40/60 minimum set-aside test. The project may elect average income for the Low-Income Housing Tax Credit program (LIHTC) as long as the unit mix selected will also meet the minimum set-aside test for bond compliance purposes. The tax-exempt bond will have a separate restrictive covenant.

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 (AHFA) for the project.
- Owners must disperse unit designations in a manner that does not violate fair housing laws.
- The market study must demonstrate sufficient market demand for each proposed unit designation type contained in the application.
- LIHTC equity commitment letters must explicitly state that they are based upon the average income test.

OHFA REVIEW

- OHFA may require a legal opinion verifying the ability to utilize average income in combination with any other funding source.
- Applications will be underwritten based on each unit's designation as stated in the proposal and final applications and the IRS Form 8609 submission. These proposed designations will be documented in the Carryover Agreement or 42m Letter of Eligibility.

UNIT DESIGNATIONS

The proposed unit designations will be documented in the Carryover Agreement or 42m Letter of Eligibility. The restrictive covenant will contain a general provision of the average required for income and rent designations. Other OHFA specific rent and/or income requirements may be stated separately in the restrictive covenant.

MULTIPLE BUILDING ELECTION

- If the project 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 Form 8609.
- OHFA will permit exceptions to this requirement upon demonstration of a compelling need.

RESYNDICATION RESTRICTIONS

- Projects seeking a resyndication of credits are permitted to elect average income as a new minimum set-aside.
- 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 initial restrictive covenant until the existing extended use period has ended.

REQUEST TO CHANGE SET-ASIDE PRIOR TO 8609 ISSUANCE

- OHFA will permit projects to change their intended election, only if the following requirements have been met:
 - Form 8609 has not been issued;
 - Restrictive covenant has not yet been recorded;
 - Project will be selecting 'yes' to line 8b. on Form 8609;
 - All other affordability requirements are met; and,
 - If applicable, the change would not negatively impact the project's competitive score, such that the project would not have been funded.
- The owner/developer **MUST** contact the project administration analyst prior to the request for Form 8609 to discuss the requirements, submit any needed documentation, and confirm that the project is permitted to change their intended election.
- OHFA may require the owner/developer to submit a re-underwriting fee.

TRAINING AND TECHNICAL ASSISTANCE

- OHFA may require proof that owner/management agent have attended trainings specific to average income requirements and require additional training.

COMPLIANCE WITH AVERAGE INCOME

- The average income test is met in accordance with Treasury Regulation 1.42-19.
- See [Treasury Regulation 1.42-19](#) examples 1-6 for more details.

UNIT DESIGNATIONS

- OHFA allows AMI designations to float between units within the project (i.e., a particular unit is not locked into a specific AMI level).
- OHFA will consider the owner to have “designated” a unit based on the AMI level being (1) recorded on the Tenant Income Certification form in the file and (2) reported through DevCo, OHFA’s online reporting system, as part of the Annual Owner Report of Compliance.
- OHFA allows redesignations based on the changes permitted under [Treasury Regulation 1.42-19\(d\)](#) including bringing a unit or project back into compliance.
 - If the designation changed, a Clarification Record is needed in the tenant file identifying the updated designation.
- Any change in designation on vacant unit(s) will be reported in DevCo with the next occupancy of the unit.
- Unit re-designations for an occupied unit must be updated in DevCo as they occur and must be complete by the end of the taxable year.

APPLICABLE FRACTION DETERMINATION

- Applicable fraction must be maintained in accordance with [Treasury Regulation 1.42-19\(b\)\(3\)\(ii\)](#).
- Each building must maintain the applicable fraction identified for it.
- See [Treasury Regulation 1.42-19](#) examples 1-6 for more details.

COMPLIANCE MONITORING

- Projects must meet the required minimum set-aside election no later than the end of the first year of the credit period.
- Owners of projects must submit the Annual Owner Report and any other required documentation as determined by OHFA.
- OHFA will monitor for violations of the average income minimum set-aside election for year end compliance, and at OHFA’s discretion compliance with the Qualified Allocation Plan.

REPORTING AND CORRECTIONS OF NONCOMPLIANCE

- If an issue is discovered and corrected within the taxable year that the issue occurs, the owner will be allowed to correct the issue to ensure that there is a qualifying group of units and that the Minimum Set-aside test is met by the end of the taxable year.
- 180-Day Rule - If an issue is not discovered and also corrected within the taxable year that the problem occurs, any retroactive correction to designations must be made within 180 days of discovery of an issue by the owner or OHFA. If discovered by the owner, the correction must occur within the next required tenant update. This update must be completed by the 10th of each month through DevCo .
- Household Income Above Income Limit upon Initial Occupancy:
 - Units must be occupied with households that have a gross income less than or equal to the unit’s designation. If the household is not income eligible, the unit is subject to IRS Form 8823 and reported under category 11a.
- Additional detail and guidance regarding noncompliance can be found in the [IRS Guide for Completing Form 8823](#) and [Treasury Regulation 1.42-19](#).