Back to Basics Part 3: Students

by Scott Michael Dunn, CEO, Costello Compliance

In part three of this series, we will cover basic tax credit compliance rules and principles, as well as how to research answers to questions tax credit professionals have in their daily practice. This Basics article will focus on students, for tax credit properties. Household eligibility for tax credit units is determined based on student status, so this is a crucial topic to understand. How student financial assistance is counted as income is also an important income-related student topic. For this discussion, the 8823 Guide — especially Chapter 17 — provides a useful explanation of the tax code.

It is important to realize that the tax code student rules — and even the 8823 Guide — leave a lot of room for interpretation. Also, state Housing Finance Agencies (HFAs) commonly add provisions. How does all of this apply to your property? We cannot answer this question definitively here, but we will indicate the questions to ask your HFA for several provisions as the article progresses.

Student Status

When examining a household's eligibility for a Low-Income Housing Tax Credit (LIHTC) unit, every household must be asked if any member of the household is a full-time student. If so, it may not be eligible.

- **Question for your state HFA**: Do unborn children qualify as non-students? The IRS has unofficially indicated "yes" at several industry conferences when asked this question, but this is not in writing.

It is also important to realize that the code defines a full-time student as a person who attended "full time" as defined by the school they attend. Also, if they are full time for any part of five months of a calendar year, they are considered students for purposes of the student rules for the rest of the calendar year, even after finishing school. Therefore, a person who was a full-time student as defined by their school from January until May 2 is considered a student for LIHTC purposes until Jan. 1 of the following year.

The statute relating to students at LIHTC properties can be found at § 42(i)(3)(D). Passages in this article in quotation marks for the rest of this subheading are from this section. Although full-time student households are generally not eligible for LIHTC units, the code provides that "a unit shall not fail to be treated as a low-income unit merely because it is occupied" by certain students or groups of students.

First, the code lists persons who qualify because they are "a student who is any of the following."

1. "Receiving assistance under Title IV of the Social Security Act."

This is the old primary federal welfare program.

- **Questions for your HFA**: The program that has replaced federal welfare in most states is Temporary Aid for Needy Families (TANF). What constitutes the "welfare" exception in your state?

2. "Was previously under the care and placement responsibility of the State agency responsible for administering a plan under part B or part E of title IV of the Social Security Act."

This refers to former foster children or adults. A few states put a limit on how long in the past a foster could have been in the system and qualify. The law puts no time restrictions on this, so strictly speaking, former foster members are non-students for life.

- **Questions for your HFA**: Are there any state-rule time limits for how long it has been since a former foster household member was in the foster system and can still qualify for this exception?

3. "Enrolled in a job training program receiving assistance under the Job Training Partnership Act or under other similar Federal, State or local laws."

This is not a reference to just any job training program. An examination of its mission statement demonstrates that the Job Training Partnership Act (JTPA) was designed to provide training to help persons who face serious barriers to employment enter the workforce. As the JTPA is no longer in existence, a state may designate what they consider to be "similar" programs. The Department of Housing and Urban Development (HUD) has indicated that Workforce Investment Act programs have replaced JTPA (HUD 4350.3 Exhibit 5-1), so these federally funded programs clearly qualify. Other state and local programs may as well.

- **Question for your HFA:** Are there any specific programs in our state that have been determined to be JTPA-similar?

The final two exceptions are for households made up "entirely by full-time students if such students are any of the following." IRS officials have often indicated informally, but publicly, that any person or combination of persons who meet the exceptions qualifies a household, even if other members do not. At least the "single parent" section of the IRS sample student form in the 8823 Guide indicates "yes," but opinions on the actual wording of the code differ. Some HFAs require that, for households meeting the following exceptions, every member must individually meet one of the exceptions.

4. **"Single parents and their children and such parents are not dependents (as defined in IRC §152…) of another individual and such children are not dependents (as so defined) of another individual other than a parent of such children."**

- **Question for your HFA**: Do a single parent and child in a household qualify the household, even if someone else (such as a non-parent boyfriend of a single mother in a unit) resides in the unit as well?

5. **"Married and file a joint return."**

Another place in the code indicates that any member who is "entitled" to file a joint tax return qualifies the unit. For several years, the IRS has stated that married people must simply be "entitled to file," but a decreasing number of states impose a stricter definition that requires a couple to have actually filed a tax return.

- **Questions for your state HFA**: Must married students be "filing" a joint return, or simply be "entitled" to do so? Does one person who is entitled to file a joint return qualify the household, even if there are other nonmarried household members?

Student Financial Assistance Income

When Congress made an adjustment to the Section 8 program, they added clarification on how student financial assistance income is counted for Section 8. As LIHTC income is counted in a manner consistent with Section 8, these rules apply to many LIHTC households. HUD's instructions for student financial assistance are found in Chapter 5 and Exhibit 5-1, Inclusions (9) and Exclusions (6) of the 4350.3.

First, it is important to understand which households are subject to this rule. Per the 8823 Guide (Chapter 4, page 18), the IRS has determined that this rule applies very narrowly, only to households receiving Section 8 assistance. Practically speaking, this applies to residents who live at a LIHTC property with project-based Section 8 and those who come to a property holding a Housing Choice Voucher. For other households, all student financial assistance is excluded. Even if the household is receiving Section 8 assistance, all financial assistance *for dependents living with their parents and parents over age 23 with dependents in the household* is excluded.

Next, it is important to understand that the student financial assistance that is counted as income is very specifically defined. It includes assistance provided (1) under the Higher Education Act of 1965 (such as Robert C. Byrd Scholarships or Pell Grants), (2) from private sources (parents or grandparents), or (3) from an institution of higher education (school scholarships). Based on other HUD guidance, other types of student financial assistance not fitting into these categories (such as GI bill benefits not specified for housing) are excluded, per Exhibit 5-1, *Exclusions* (6).

For student members of Section 8-assisted households, the three countable types of student financial assistance are added together, and *tuition is subtracted*. Any remaining amounts are counted as income.

Other Program Student Rules

Many LIHTC professionals are responsible for properties that have LIHTC funding as well as tax-exempt bond, HUD Section 8, Rural Development or HOME funding. These programs all have student rules that must be followed to maintain the funding, in addition to the LIHTC rules. Although a full discussion of these other rules is beyond the scope of this article, a few comments here will be useful to get professionals started in understanding these programs.

In the past, the Section 142 **tax-exempt bond** program also prohibited full-time student households. It had only one exception: for married students entitled to file jointly. In 2008, this was changed, and the bond program adopted all the same exceptions as allowed to LIHTC properties.

For many years, the LIHTC program had the most stringent student status rules. However, strict student eligibility rules were applied to Section 8 housing applicable in 2006. A year later, Rural Development applied the same rules, and HOME followed suit in 2013. The HUD Handbook 4350.3 Chapter 3 provides a thorough explanation of the HUD rules. These rules target individual household members, not entire households. Full- or part-time students through age 23, who attend institutes of higher education, are examined. Many exceptions are provided, but if the students cannot meet one of these, the household is not eligible for Section 8, Rural Development or HOME housing. As the focus for the LIHTC and Section 8-type student rules are completely different, both sets of student rules must be applied independently, and a household must meet both sets of rules to qualify.

As we can see, our “toolbox” of useful guidance serves us well. We have seen how HUD and IRS documents provide a wealth of information on students, a crucial topic to understand for LIHTC professionals. Please read the next Credential, in which we will tackle another compliance basic and see how our regulatory “toolbox” gets us the right answers!

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