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Back to Basics Part 2: Income Limits

by Scott Michael Dunn, CEO of Costello Compliance

This series covers the basics of tax credit compliance and how to research answers to questions tax credit professionals have in their daily practice. This Basics article will focus on income limits for tax credit properties. This is a crucial topic to understand as household eligibility for units, as well as rents, are determined based on the income limits.

Originally, the tax credit program shared the Department of Housing and Urban Development's (HUD's) section 8 income limits. However, the Housing and Economic Recovery Act of 2008 (HERA) created a new process to determine income limits for tax credit and tax-exempt bond properties. HUD still publishes the limits, so to differentiate them from the HUD section 8 limits, HUD dubbed the new limits Multi-family Tax Subsidy Program (MTSP) limits.

Once the data are secured from HUD, there are a few options for tax credit properties that must be understood to select the correct limits for a specific property. Some commonly asked questions will provide much of the framework for the discussion. This infographic, with screenshots to the HUD and U.S. Department of Agriculture (USDA) websites, may also prove useful.

MTSP Program Implementation Dates

The tax credit program has a provision in Rev. Rul. 94-57 that states that an owner may rely on last year's income limits published by HUD until 45 days after HUD releases the new limits, or HUD's effective date for those limits, whichever is later. However, because of the tax credit income limit "hold harmless" provision that is discussed below, this 45-day period only matters in actual practice to a limited number of properties that have a first building that is placed in service during the 45-day period following publication of the new limits. IRS guidance is that the owner may select whichever set of limits provides the best advantage if a project places in service during this period, and "hold harmless" to those limits going forward.

Frequently Asked Questions

The income limits went down for my area this year. What happens now?

The tax credit law changed with 2008's HERA. One new provision was that, starting in 2009, the limits that a specific tax credit property uses do not have to go down from one year to the next. This starts when the first building in a project places in service. This principle is referred to as the limits "holding harmless." For example, assume that the first building in a project was placed in service in 2016, and limits went down in 2017 and again in 2018. The 2016 income (and rent) limits should be used for all those years. They will continue to be used until the published limits exceed the 2016 limits. At that time, the owner will use the new limits and will "hold harmless" to the new limits.

A prior year's MTSP limit may be used if:

1. The published income limits for the project's area have gone down from a prior year, and
2. The project had at least one building that was in service during the applicable prior year.

Are "HERA Special" or rural limits an option for my property?

HERA created the "hold harmless" provision discussed in the last question. It also created additional options for properties that face special challenges. These are "HERA Special" options for certain older properties and the rural national non-metropolitan average limits for rural projects with exceptionally low published income limits. Selecting these may seem a bit tricky, but the limit to select is based on a few simple factors. The following will help determine if the special limits apply.

"HERA Special" limits may be used if:

1. HUD lists this option for the property's area.
2. At least one building in the project was placed in service in 2008 or earlier.

"National non-metro" limits may be used if:

1. The project is not funded with tax-exempt bonds.

2. The project is in an area determined by USDA Rural Development to be "rural," and the published MTSP limits for the area are lower than the national non-metro limits.

Note: Use the USDA website to determine if a project is rural. The national non-metro limits can be found in the HUD FAQ. For 2021, it was part of the answer to FAQ No. 14. Also note that HUD only publishes the 50% limits in the FAQ. The 60% limits for 40-60 or Average Income Test minimum set-aside properties needs to be calculated from the 50% limits. One way to do this is by multiplying the supplied 50% limits by 1.2.

Income Limits and the Income Average Test

The *2018 Omnibus Tax Act* created a new minimum set-aside, the Income Average Test. A full discussion of this new provision is beyond the scope of this article. However, one aspect of the Income Average Test is that new tax credit properties may have up to seven designations that can be assigned to units (20% - 80% MTSP, in even increments of 10%). People who move into these units must be below the designated income limit. Rents will be calculated based on these income limits as usual for the tax credit program. How are these new designations calculated? Revenue Ruling 89-24 already established how to calculate 60% and 40% designations based on HUD 50% (very low) income limits. Based on this regulated model, Revenue Ruling 2020-4 extrapolated the calculations across the remaining four designations that 89-24 did not cover, reflected in the chart at right.

Based on Rev. Rul. 89-24
and Rev. Rul. 2020-4

Designation	Multiply the 50% (very-low) income limit by:
20	40%
30	60%
40	80%
50	100%
60	120%
70	140%
80	160%

Do MTSP limits apply to the HOME program?

No, HOME Income and rent limits are not the same as the MTSP limits; they are published later and are subject to HOME-specific regulations. The Low Income Housing Tax Credit (LIHTC) "hold harmless" provisions do not apply to HOME units for HOME income limit purposes. This is true even if the property is also tax credit.

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The 2008 HERA and 2018 Omnibus Tax Act income limits added some complexity to the selection of limits, but each of the new options created assists tax credit properties with stable income and rent limits. Learning to select the correct limits is a vital skill for tax credit professionals.

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