



Conquering LIHTC Utility Allowances

by Amanda Lee Gross, VP of Training and Compliance Policy

In the seventh and final article of my series on LIHTC utility allowance requirements, I will address updating utility allowances (including the 90-day debate) and record retention.

Utility Allowance Updates

Annual Review Deadline

Although we all wish our utility rates would always stay the same, we are bound to see increases in these rates year to year. Because utility rates change, utility allowances must be updated to account for these changes.

Treasury Regulation 1.42-10 requires that owners conduct an annual review of the utility allowance, but the annual review does not need to occur every 12 months; instead, owners must review utility allowances at least one time during each calendar year — meaning the deadline to conduct the utility allowance review is the end of each calendar year and not 12 months from the last review.

Example: The owner of Cedar Park Apartments last conducted a utility allowance review on March 2, 2020. The owner must complete the next utility allowance review no later than Dec. 31, 2021.

New Buildings

For new buildings, a review of utility allowances or implementation of new utility allowances is not required until the building has reached 90% occupancy for 90 consecutive days or the end of the first year of the credit period, whichever occurs first.



Implementation of New Utility Allowances

Treas. Reg. 1.42-10(c)(1)

(1) In general. If, at any time during the building's extended use period (as defined in section 42(h)(6)(D)), the applicable utility allowance for units changes, the new utility allowance must be used to compute gross rents of the units due 90 days after the change (the 90-day period). For example, if rent must be lowered because a local utility company estimate is obtained that shows a higher utility cost than the otherwise applicable PHA utility allowance, the lower rent must be in effect for rent due at the end of the 90-day period.

If the utility allowance does change, the new utility allowance must be implemented 90 days after the change. This timeframe is referred to in regulation as the "90-day period." After the 90-day period, the new utility allowance must be used. The application of the 90-day period applies somewhat differently, depending on the utility allowance method used.

- **PHA Utility Allowance** – If the building uses the public housing authority (PHA) utility allowance, the owner must implement the new utility allowance 90 days after publication by the PHA. ***See "Decreases In Utility Allowances."*
- **Utility Company Estimate, the HUD Utility Schedule Model, & Energy Consumption Models** – For buildings using the Utility Company Estimate, the HUD Utility Schedule Model, and Energy Consumption Models, the owner must provide the updated utility allowance estimates to the housing finance agency (HFA) and make the estimates available to all tenants 90 days prior to implementing the updated utility allowance.
- **Agency Estimate** – For buildings using the Agency Estimate, the owner must make the new utility allowance estimate available to all tenants 90 days prior to implementing the updated allowance.

Increases in Utility Allowances

Gross Rent Test

When the new utility allowance increases, a gross rent test should be conducted to determine if the gross rents for any unit will exceed the maximum rent once the new utility allowance is



applied. If there are any units where the gross rent will exceed the maximum rent, the tenant portion of the rent must be decreased enough to reduce the gross rent to be at or below the maximum rent by the end of the 90-day period.

Decreases in Utility Allowances

A Gross Rent Test is not necessary when the utility allowance decreases, as the decrease in the utility allowance is also decreasing the gross rent. Although a decrease in the utility allowance may allow room to increase the tenant's rent portion while still remaining under the maximum rent, any rent increase must only be implemented as per the tenant's lease and in accordance with applicable local and state tenant-landlord law.

90-Day Period and Decreases in the PHA Utility Allowance – The 90-Day Debate

Although it is made clear in Treas. Reg. 1.42-10, when using the Utility Company Estimate, the HUD Utility Schedule Model, Energy Consumption Model, or Agency Estimate, the updated utility allowance cannot be used until *after* the 90-day period, it is not made expressly clear if the same restriction applies to owners using the Public Housing Authority Utility Allowance Schedule.

The lack of clarity has prompted the question: Does the building owner need to implement the new PHA utility allowance exactly 90 days after being published, instead of *within* 90 days of publication?

The core of the question lies in the following text found in Treas. Reg. 1.42-10:

*"the applicable utility allowance for units changes, the new utility allowance must be used to compute gross rents of the units **due** 90 days after the change (the 90-day period).*

It is evident that the new Utility Allowance must be used when the 90-day period ends. But can it be implemented *prior* to the conclusion of the 90-day period?

This difference in interpretation only presents a potential compliance issue in instances where the PHA utility allowance for a building decreases, and the owner wants to increase tenant rents prior to the expiration of the 90-day period.



The concern is that if the old Utility Allowance is still considered in effect for the entirety of the 90-day period, then increasing the rent prior to the conclusion of the 90-day period could result in the overcharging of rent.

*Example: The owner of West Shore Apartments utilizes the PHA Utility Allowance. Currently, the **Utility Allowance** for a one-bedroom unit is **\$125**; the owner charges **\$700** per month in **rent** and charges no non-optional fees, resulting in a **gross rent** of **\$825**. The **maximum rent** applicable to the one-bedroom units is **\$830**.*

*The PHA publishes a new utility allowance schedule on Jan. 1, 2021. Based on the new utility allowance estimate, the utility allowance has **decreased** from **\$125 to \$110**. On Jan. 1, 2021, the owner issues a 30-day notice of rent increases to 10 low-income, one-bedroom units that are on a month-to-month lease. The owner **increases** the **rent** from **\$700 per month to \$710 per month**, effective Feb. 1, 2021.*

*If the new utility allowance can be implemented **within** 90 days of publication by the PHA, then the owner of West Shore Apartments is in compliance with the rent restrictions as the gross rent for the units beginning in February is at or below the max rent. (Rent of **\$710 + Utility Allowance of \$110 = Gross rent of \$820**, which is **\$10** under the applicable maximum rent.)*

*If the new utility allowance cannot be used **until the expiration of the 90-day period**, meaning the old utility allowance remains in effect until the 90-day period has concluded, the owner of West Shore Apartments is out of compliance with the rent restrictions beginning Feb. 1, as the gross rent for the units exceeds the applicable maximum rent. (Rent of **\$710 + Utility Allowance of \$125 = Gross rent of \$835**, which exceeds the maximum rent by **\$5**.)*

Because of the lack of clarity weighted with the severe compliance implications, US Housing recommends not increasing tenant rents until the expiration of the 90-day period.



Record Retention

Treas. Reg. 1.42

The building owner must retain any utility consumption estimates and supporting data as part of the taxpayer's records for purposes of § 1.6001-1(a).

§ 1.6001-1 states:

Retention of records. The books or records required by this section shall be kept at all times available for inspection by authorized internal revenue officers or employees, and shall be retained so long as the contents thereof may become material in the administration of any internal revenue law.

It is recommended the utility allowance documentation be maintained for the entirety of the compliance period, plus three years.

Owner/agents must be prepared to provide the utility allowance documentation supporting the utility allowance used during an Agency Monitoring Review.

It is important to check with your HFA to determine what type of documentation and data the agency would like retained.

Conclusion

Although there can be severe tax credit consequences to the owner for failing to comply with the utility allowance requirements, we cannot forget that using the incorrect utility allowance could also result in a household paying a higher rent than what is truly affordable under the program. For the residents that we are dedicated to serving, every single dollar matters, so we must do our part to ensure that households are paying a rent that is truly affordable.

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