



## Homeownership in Post -Year 15 LIHTC Properties

### *General*

In 2006, a developer proposed converting a LIHTC property in Kansas City from rental housing to affordable condos following its 15-year compliance period. Since the IRS has not produced a general revenue ruling on this issue, the Missouri Housing Development Commission (MHDC) asked the owner to submit a request for a private letter ruling (PLR) seeking approval. MHDC supported the owner in the submission of the request for the PLR. On January 19, 2007, the IRS issued a PLR approving the request to convert the property to affordable condos based on the conditions proposed by the developer. Although a PLR does not carry the weight of a revenue ruling, it does give us insight into the thinking of the IRS on this topic.

### *The Private Letter Ruling*

The IRS issued PLR 200703024 on January 19, 2007. They ruled that the conversion of the property to affordable condominiums was permissible based on the following conditions:

- The owner includes a statement in all leases that a condominium conversion may occur following the end of the compliance period.
- The owner provides a notice to the residents describing the conversion process and saying when it will begin.
- The purchase price is not less than the minimum price described in Section 42(i)(7) of the Code. The purchase price for each unit is affordable to the residents because it is based on mortgage payments and condo fees that can be paid by the maximum allowable LIHTC rents at the time of sale.
- The owner offers each resident a discount on the purchase price for their unit equal to 1% for each year the resident has lived in their unit during the ten years preceding the year of the conversion. To receive the benefit of the discount, the tenant must reside in their unit at the time of conversion and must elect to purchase their unit within 6 months of the date of conversion.
- The current renters have the right of first refusal to purchase their units. Each resident has 6 months from the start of the conversion process to exercise this right. If a tenant elects not to purchase their unit, it will continue as rental property and the tenant has the right to remain in the unit for as long as they choose. The owner will be limited to charging no more than the maximum LIHTC rents for any remaining rental units.

- The owner signs a new LURA with MHDC providing for homeownership after the 15-year compliance period which also complies with the requirements found in the Code for extended use agreements. The period and affordability restrictions of the new commitment will last for 30 years beginning on the date the new commitment is recorded. The new commitment will have 2 parts: One part governing the part of the property still operating as rental units and a second part governing the management of the condominium units.
- At resale, the price does not exceed the gross sales price paid by the seller plus a 10% increase for each year they have owned the unit.
- The owner keeps the state agency informed of their progress implementing the sales program and provides the agency with 60-days notice prior to notifying the residents of the condo conversion process.

### *The Prototype*

McCormack Baron Salazar is the developer who requested the PLR for the property in Kansas City. Sun America is the syndicator. McCormack Baron Salazar has met with 28 of the 60 residents. In November 2007 it was reported that fourteen (14) of the residents were proceeding to homeownership. Fifty percent of the residents expressing an interest in buying their units receive rental subsidy through the housing choice voucher program. ([www.mccormackbaron.com](http://www.mccormackbaron.com))

### *The State of Wisconsin*

The Wisconsin Housing and Economic Development Authority (WHEDA) discussed the possibility of converting LIHTC properties to homeownership at their annual conference in November 2007. They have established the following requirements for owners wanting to convert their LIHTC properties to affordable condominiums following their 15-year compliance period.

- The owner must pay a conversion request fee to WHEDA.
- The owner must submit a capital needs assessment and feasibility study.
- The owner must fund a reserve to address any outstanding items listed in the capital needs assessment.
- The conversion must be financially feasible and affordable to the current residents.
- The monthly cost of ownership (principal, interest, taxes, insurance plus condo fees) must be no more than the rent currently paid by the residents.

- The owner must provide homebuyer education or contract with another organization to provide homebuyer training.
- The owner must submit a schedule of sources and uses of funds for the conversion process.
- The owner must provide notification to the local government.
- The property manager must have LIHTC experience.
- The owner must use an approved formula for calculating the sales price for the condo units.
- For residents who elect not to purchase their units, the owner may not increase rents more than 10% per year nor charge more than the LIHTC maximum allowable rent.
- The owner must sign a new LURA lasting 30 years. Everyone buying a unit during the 30-year period must meet the income limit for the LIHTC program.

Wisconsin is likely to require an owner to seek a PLR unless the IRS issues a general revenue ruling addressing condo conversions for LIHTC properties.

### *Issues*

Anyone considering converting a LIHTC property to affordable condominiums should begin the process by exploring the following issues.

- What is the state housing finance agency's position on converting an LIHTC property to affordable condos following its 15-year compliance period? Meet with the representatives of the HFA to find out if you can win their approval for your plan to convert.
- Read the partnership agreement. What does it indicate about the obligation of the GP to share in the appreciation in value when the property is sold? This will impact the feasibility of the conversion process for the GP. The developer must be able to generate enough proceeds through the sale of the units to pay off the property's debt for a conversion to condos to work.
- Do the renters at the property want to be homeowners? Do they want to be homeowners where they have been renters? Do they want to be homeowners in a low income property that will continue to include renters? A developer should meet with the residents very early in the planning to process to find if there is enough interest in homeownership to proceed.

- Are there current residents with income well below the LIHTC maximum making them unable to afford to purchase their units?
- Does the local public housing authority (PHA) offer a homeownership option through their housing choice voucher program and are they interested in supporting homeownership at the property? Would they provide a project-based voucher?
- Etc ...

### *Other Funding Sources*

The financial structure for most LIHTC properties includes other types of subsidies. Do these other funding sources allow for a conversion to homeownership and if so, when?

- Does the property have HOME funding? If yes, has it completed its period of affordability? If no, is the PJ willing to sign a new regulatory agreement allowing for the conversion to homeownership and under what conditions?
- Will the local PHA allow current residents with housing choice vouchers to convert to homeownership and keep their vouchers? The program allows for homeownership but under certain conditions and not every PHA is required to provide a homeownership option through its voucher program.
- Are there other funding sources that could be utilized to support the conversion process? E.g., could funds from the local HOME program be used to provide a soft-second mortgage for the resident-purchasers, making the units affordable to a wider variety of residents? The second mortgage could be payable upon resale of the unit and allow for the developer to experience part of the increase in value.
- Etc...

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