SENATE COMMITTEE ON HOUSING
Senator Scott Wiener, Chair
2023 - 2024 Regular

Bill No:	AB 346	**Hearing Date:**	6/20/2023
Author:	Quirk-Silva		
Version:	1/31/2023 Introduced		
Urgency:	No	**Fiscal:**	Yes
Consultant:	Aiyana Cortez		

SUBJECT: Income tax credits: low-income housing: California Debt Limit Allocation Committee rulemaking

DIGEST: This bill allows the California Tax Credit Allocation Committee (CTCAC), for any calendar year in which the California Debt Limit Allocation Committee (CDLAC) has declared a competition for the award of tax-exempt bond authority for qualified residential rental projects, to reallocate some of the $500 million in enhanced state low-income housing tax credits (LIHTCs) made available from 4% federal credit projects to 9% federal credit projects.

ANALYSIS:

Existing law:

1) Authorizes CDLAC to adopt, amend, or repeal rules and regulations as emergency regulations in accordance with the rulemaking provisions of the Administrative Procedures Act (APA).

2) Authorizes TCAC to use a public process that is not the APA to adopt, amend, or repeal rules and regulations for the allocation of LIHTCs.

3) Provides that a low-income housing development that is a new building and is receiving 9% federal LIHTCs is eligible to receive state LIHTC over four years of 30% of the eligible basis of the building.

4) Provides that up to $500 million in enhanced state LIHTC may be allocated to 4% tax credit projects pursuant to an authorization in the annual budget or related legislation, but not to 9% tax credit projects.

5) Requires projects funded by TCAC to begin construction within 180 days of the award. Authorizes the TCAC executive director to extend the 180 days in the event the Governor has declared a state of emergency.

6) Authorizes a taxpayer who receives a tax credit to sell the credit to one or more unrelated parties, as specified.

This bill:

1) Authorizes TCAC, for any calendar year in which CDLAC has declared a competition for the award of tax-exempt bond authority for qualified residential rental projects, to allocate some or all of the $500 million in enhanced state LIHTC for 4% LIHTC projects to 9% LIHTC projects that can begin construction within a reasonable time, as determined by TCAC. Any remainder must then be allocated to qualified new construction projects that are awarded 4% federal LIHTC.

2) Requires projects that receive an enhanced state LIHTC in a calendar year in which CDLAC has not declared a competition for the award of tax-exempt bond authority to begin construction within a reasonable time, as determined by TCAC, rather than 180 days.

3) Provides that if any enhanced state LIHTC remains unallocated after the final CDLAC round in a given calendar year, TCAC may allocate some or all of the remaining credits to 9% LIHTC projects.

4) Revises the definition of "applicable percentage" to eliminate the restriction on certain state LIHTCs only being used for rehabilitation projects, thereby allowing them to be used on any type of project.

5) Authorizes CDLAC to adopt, amend, or repeal rules and regulations without complying with the procedural requirements of the Administrative Procedure Act (APA). These rules and regulations would be effective immediately upon adoption. For rules and regulations not complying with the APA, CDLAC must provide a notice of proposed action to the public at least 21 days before the close of the public comment period, and must schedule at least one public hearing before the close of the public comment period. The final version of the regulations must be accompanied by a final statement of reasons.

6) Authorizes a taxpayer that has purchased a credit to claim the credit commencing in the taxable year the building is placed in service and the federal credit period begins, as specified. The amount of credit claimed by the taxpayer must not exceed the lesser of either of the following:

    a) The applicable percentages for each of the four credit years, as specified, multiplied by the qualified basis of the building set forth in the preliminary reservation; or

b) The amount of credit the project is eligible for as stated in the taxpayer certification.

7) Authorizes TCAC to review the taxpayer certification and other information provided by the taxpayer who originally received the preliminary reservation of credits to confirm both of the following:

   a) The calculations set forth in the taxpayer certification; and
   b) That the amount of credits allocated to the project is consistent with applicable TCAC rules and regulations, as specified.

8) Provides that, in the event TCAC issues a certification that is inconsistent with the taxpayer certification upon which a credit has been claimed, the taxpayer must amend any previously filed tax returns as needed to reflect the credit amount certified by TCAC.

COMMENTS:

1) Author's statement. "AB 346 will increase the impact of the state's additional investment in Low-Income Housing Tax Credits by deploying these credits more effectively. The current pairing of these state credits with 4% federal credits no longer makes sense at a time when there is a massive backlog of developments seeking 4% federal credits. The line just becomes longer. By granting the Tax Credit Allocation Committee the authority to move these credits to the unconstrained 9% federal tax credit program, California can increase the overall production of new affordable homes."

2) *Federal LIHTC program.* The LIHTC is an indirect federal subsidy developed in 1986 to incentivize the private development of affordable rental housing for low-income households. The federal LIHTC program enables affordable housing sponsors and developers to raise financing through the allocation of tax benefits to investors. TCAC administers the program and awards credits to qualified developers who can then sell those credits to private investors who use the credits to reduce their federal tax liability. The developer in turn invests the capital into the affordable housing project.

   Two types of federal tax credits are available: the 9% and 4% credits. These terms refer to the approximate percentage of a project's "eligible basis" a taxpayer may deduct from their annual federal tax liability in each year for 10 years. "Eligible basis" means the cost of development excluding land, transaction costs, and costs incurred for work outside the property boundary. For projects that are not financed with a federal subsidy, the applicable rate is 9%. For projects that are federally subsidized (including projects financed more than 50% with tax-exempt bonds), the applicable rate is 4%. Generally, the 9% tax credit amounts to 70% of a taxpayer's eligible basis and the 4% tax credit amounts to 30% of a taxpayer's eligible basis, spread over a 10-year period.

Each year, the federal government allocates funding to each state for LIHTCs on the basis of a per-resident formula. Only rental housing buildings that are either undergoing rehabilitation or newly constructed are eligible for the LIHTC programs. The 9% credit is generally reserved for new construction, while the 4% credit can be claimed for rehabilitation or new construction. In addition, developments must comply with both rent and income restrictions.

Each state receives an annual ceiling of 9% federal tax credits. Currently, in California they are oversubscribed, meaning for every project that is awarded a LIHTC, there are multiple eligible projects waiting in the queue who did not receive an award. Unlike 9% LIHTC, federal 4% tax credits are not capped; however, they must be used in conjunction with tax-exempt private activity bonds (PABs), which are capped and are administered by CDLAC. PABs are issued by state and local government agencies and are purchased by the private sector, generally a bank (who can use the bond for purposes of federal Community Reinvestment Act compliance). The current state PAB ceiling is $4.68 billion. Therefore, the limiting factor for the 4% credit comes from this overall bond volume cap. As described above, the value of the 4% tax credits is less than half of the 9% tax credits and, as a result, 4% federal credits are generally used in conjunction with another funding source to fill out the developer's "capital stack," like state housing grant awards or local funding sources.

3) *State LIHTC program.* In 1987, the Legislature authorized a state LIHTC program to augment the federal tax credit program. State tax credits can only be awarded to projects that have also received, or are concurrently receiving, an allocation of federal 4% LIHTC. The amount of state LIHTC that may be annually allocated by TCAC is limited to $70 million, adjusted for inflation. In 2020, the total credit amount available for allocation was about $100 million plus any unused or returned credit allocations from previous years.

While the state LIHTC program is patterned after the federal LIHTC program, there are several differences. First, investors may claim the state LIHTC over four years rather than the 10-year federal allocation period. Second, the rates used to determine the total amount of the state tax credit (representing all four years of allocation) are 30% of the eligible basis of a project that is not federally subsidized and 13% of the eligible basis of a project that is federally subsidized, in contrast to 70% and 30% (representing all 10 years of allocation on a present-value basis), respectively, for purposes of the federal LIHTC.

Combining federal 9% credits (which amounts to roughly 70%) with state credits (which amounts to 30%) generally equals 100% of a project's eligible basis. Combining federal 4% credits (which amounts to roughly 30%) with state credits (which amounts to 13%), only results in 43% of a project's eligible basis, again requiring developers to seek additional funding sources to make up the remaining gap.

4) *Enhanced State LIHTC.* In 2019, AB 101 (Budget Committee, Chapter 159), was signed into law, providing an additional $500 million in "enhanced" state LIHTCs in 2020 and future years, subject to appropriation. When the additional $500 million was first made available, the federal tax-exempt bond ceiling of approximately $4 billion had not yet been reached. In 2014, for example, developers only used $80.5 million in annual federal 4% tax credits, significantly less than prior years. This is because there was little supplemental funding from housing bonds or local funding sources available to fill the remaining financing gap. The loss of redevelopment funding and state housing bond funds, which were used in combination with 4% federal credits to achieve higher affordability, had made the 4% federal credits less effective.

   Thus, the additional $500 million was targeted to the 4% credit and coupled with PABs, in part, to encourage developers to fully utilize any remaining PABs that were being left on the table. When the $500 million was made available, there was also a significant uptick in state and local housing construction funding, so 4% credit applications increased rapidly and the bonds became oversubscribed. As a result, CDLAC instituted a competitive process for awarding PABs. The Legislature approved another one-time $500 million allocation in the 2021-22 budget, and a third one-time $500 million infusion in the program in 2022-23.

   As noted earlier, the limitation on the 4% credit comes from the bond volume cap, not the credit. Once the cap is met, the number of additional projects (and, to a certain degree, units) that can be approved under the 4% credit substantially tapers off. Therefore, continuing to provide $500 million in state credits to 4% credit projects under these conditions will not lead to an increase in the number of total units being built. To truly increase the number of projects approved under the 4% credit, modifications would have to be made to the federal tax-exempt bond requirements, and California does not have the authority to make those changes.

This bill allows the state to transfer some or all of the $500 million enhanced LIHTC from the 4% credit to the 9% credit when the PAB cap has been met. Projects under the 9% credit are not limited by the availability of bonds, only by the availability of credits. All things being equal, if the state reallocates more LIHTCs under the 9% credit, more units will be built for the same amount of money.

5) *Administrative Procedures Act.* Current law authorizes CDLAC to adopt regulations pursuant to the APA. With the increased competition for bonds, the committee has embarked on several changes to its regulations in recent years. This bill proposes to remove the requirement for these regulation changes to go through the APA process, thus reducing the overall length of time to make regulatory changes, in alignment with TCAC's regulations process. However, to strike a balance and ensure more transparency and opportunity for stakeholder engagement, this bill sets timelines for notice, hearings, and comments to any future regulation changes.

6) *Certificated Credits.* TCAC awards LIHTCs to qualified developers. Generally, developers do not have sufficient tax liability to use the credits themselves, so they sell those credits to private investors who use the credits to reduce their federal or state tax liability. The developer in turn invests the capital into the affordable housing project. In this case, the investor becomes a co-owner of the property to claim the credits.

   In 2016, the Legislature created an alternative investment structure called "certificated credits." Under this model, developers can sell the credits to an investor without requiring the investor to be part of the ownership entity for the project. This model increased the value of the credits. In recent years, around half of the projects receiving state credits chose to certificate their credits.

   In order to claim certificated credits, the Franchise Tax Board requires certain tax forms to be completed by the investor. According to the bill's sponsor, however, it can take time for CDLAC to provide the appropriate forms to the investor, sometimes up to two years. This bill would allow investors who buy certificated credits to begin claiming them in the year that the development is occupied, increasing the price investors will pay for the credits. According to the sponsor, this will reduce the amount of credits each development needs. This provision is consistent with rules governing federal tax credits.

7) *Seeing double.* This bill is substantially similar to AB 1288 (Quirk Silva, 2021) which was vetoed by the Governor.

My administration, in partnership with the State Treasurer's Office, recently adopted new state tax credit regulations in July of this year. These regulations are meant to create administrative efficiencies, reduce costs, and increase housing production within the state tax credit system.

Changes to this program and the use of state funding for low-income housing tax credits should be considered within the context of state regulatory changes, to ensure we maintain the necessary policy flexibility and predictability needed to improve our state housing finance system.

For these reasons, I cannot sign this bill.

8) *Double-referral.* This bill was double-referred to Senate Governance and Finance Committee.

RELATED LEGISLATION:

AB 1288 (Quirk Silva, 2021) — would have authorized CTCAC to allocate state tax credits to either the nine- or four-percent federal LIHTC. *This bill was vetoed by the Governor.*

AB 101 (Committee on Budget and Fiscal Review, Chapter 159, Statutes of 2019) — included $500 million in enhanced state LIHTC for the federal 4% LIHTC program.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: No

POSITIONS: (Communicated to the committee before noon on Wednesday, June 14, 2023.)

SUPPORT:

California Housing Partnership Corporation (Sponsor)
California Apartment Association
California Coalition for Rural Housing
California Housing Consortium
City and County of San Francisco
Community Corporation of Santa Monica
Community Housing Improvement Program (CHIP)
Community Housingworks
Danco Communities
EAH Housing

East Bay Asian Local Development Corporation
East Bay Housing Organizations
Eden Housing
Housing Authority of The City of Santa Barbara
Housing California
Jamboree Housing Corporation
Many Mansions
Midpen Housing Corporation
Resources for Community Development
San Diego Housing Federation
San Francisco Housing Accelerator Fund
San Joaquin Valley Housing Collaborative
Southern California Association of Non-profit Housing (SCANPH)
Wakeland Housing and Development Corporation

OPPOSITION:

None received.

-- END --