HB 723

Department of Legislative Services
Maryland General Assembly
2006 Session

FISCAL AND POLICY NOTE

House Bill 723 (Delegate Hixson, *et al.*)
Ways and Means

Qualified Maryland Housing Tax Credit

This bill creates a tax credit for qualified low-income housing projects. The bill establishes an application and certification procedure and creates a reserve fund to which the Governor can appropriate funds. The amount of credits that the Department of Housing and Community Development can award in each fiscal year cannot exceed the lesser of $3 million or the amount of money in the fund. DHCD is required to adopt regulations to implement the program.

The bill applies to tax year 2007 and beyond.

Fiscal Summary

State Effect: General fund expenditures could increase by $3.0 million annually beginning in FY 2008 due to appropriations to the reserve fund. General fund expenditures would increase by approximately $85,700 in FY 2007, which includes one-time tax form changes and computer programming expenditures at the Comptroller's Office and administrative costs at DHCD. General fund revenues could increase by approximately $504,000 annually beginning in FY 2008, and Transportation Trust Fund (TTF) revenues would decrease by a corresponding amount due to reserve fund transfers for credits claimed against the corporate income tax.

(in dollars)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
GF Revenue	$0	$504,000	$504,000	$504,000	$504,000
SF Revenue	0	(504,000)	(504,000)	(504,000)	(504,000)
GF Expenditure	85,700	3,068,300	3,072,200	3,076,300	3,080,700
Net Effect	($85,700)	($3,068,300)	($3,072,200)	($3,076,300)	($3,080,700)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Local highway user revenues could decrease by approximately $151,200 annually beginning in FY 2008. No effect on local expenditures.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill creates a tax credit for low-income housing projects placed in service by corporations or individuals. A project qualifies if: (1) it is a low-income housing project, as defined under Section 42(G) of the Internal Revenue Code, qualifies for the federal low-income housing tax credit, and is located in a community revitalization area (as designated by DHCD); or (2) is located in a community revitalization area and meets the eligibility standards adopted by DHCD.

Taxpayers seeking the tax credit in each year must submit an application to DHCD and can apply regardless of whether the taxpayer qualifies for the federal credit. DHCD is required to adopt regulations that establish criteria by which the tax credit would be allocated among projects. These regulations must establish the following criteria for projects that do not qualify for the federal credit: (1) at least 20% of the residential units are occupied by individuals whose income is 50% or less of area median income; or (2) at least 40% of the residential units are occupied by individuals whose income is 60% or less of area median income. Any project that receives a State tax credit is restricted in occupancy as specified by regulations adopted by DHCD for four years beginning with the first year the credit is claimed.

The maximum value of the credit is $250,000 and cannot exceed the tax liability for the tax year. Any unused amount of the credit can be carried backward to the prior tax year and forward five tax years. If the project qualifies for the federal credit, the State credit can be claimed in the first tax year for which the federal credit can be claimed. Otherwise, the credit can be claimed in the first tax year the project is placed in service, as defined under the federal credit.

The bill creates a qualified Maryland housing tax credit reserve fund. The total amount of initial credit certificates issued by DHCD in each fiscal year cannot exceed the lesser of $3 million or the amount appropriated to the reserve fund in the State budget. The bill states that the Governor may appropriate money to the reserve fund but does not require or specify a recommended amount that is to be appropriated to the fund. The Governor may not reduce an appropriation to the reserve fund that is approved by the General Assembly. For each fiscal year, if funds are transferred from the reserve fund as a result of any law, the amount of total credits that can be approved by DHCD is reduced by the amount of money transferred. Any amount of money in the fund that is not expended in the fiscal year can be rolled over into the next fiscal year.

Within 15 days of the end of each calendar quarter, DHCD is required to notify the Comptroller the total number of credits that were certified during the quarter, the total amounts of the maximum credit amount stated in the initial credit certificates, and the total amounts of the final certified credit amount. Upon this notification from DHCD, the Comptroller is required to transfer from the reserve fund to the general fund the total amounts stated in the final credit certificates that were certified during the calendar quarter.

Current Law: No similar State tax credit of this type exists.

Background: Under Section 42 of the IRC, a federal credit is available for low-income housing that is constructed, rehabilitated, or acquired after 1986. The credit is claimed over a period of 10 years in a maximum annual amount that depends on whether the low-income units are newly constructed or rehabilitated and whether the construction or rehabilitation is financed by federal subsidies. The credit rates were 9% (the "70% credit rate") or 4% (the "30% credit rate") of the qualifying basis of the low-income units in a project in 1987, but, since February 1988, the IRS has issued substitute rates on a monthly basis that reflect changes in the applicable federal rate. The credit is available on a per-unit basis and a single building may have some units that qualify for the credit and some that do not. To qualify for the credit a low-income housing project must meet the requirements discussed below. Further, the project must continue to meet the requirements for a period of 15 years or recapture of a portion of the credit may occur. Beginning in 1990, owners obtaining new credit allocations must also enter into an agreement with their local housing credit agency to maintain the low-income status of qualifying units for 30 years. Credits may not be claimed for existing buildings unless certain requirements under Section 42(d)(22) are met.

The credit is available for owners of "qualified low-income housing projects." A qualified low-income housing project is any project for residential rental property that meets the following requirements:

1. ***Open to the General Public***. Eligibility for the low-income housing credit is limited to residential rental units that are available for use by the general public. Units provided only for members of a social organization or that are provided by an employer for its employees do not qualify. Further, owners of low-income housing will generally be required to adhere to Department of Housing and Urban Development housing policy on nondiscrimination. Owners will not be in violation of the "general-public" rule, however, if preference is given to classes of tenants such as the disabled or handicapped.

2. ***Minimum Set-aside***. Twenty percent or more of the units in the project must be occupied by tenants whose incomes are 50% or less of the area median gross

income, adjusted for family size (20-50 test), or at least 40% of the units in the project must be occupied by tenants whose incomes are 60% or less of the area median gross income, adjusted for family size (40-60 test). The owner must irrevocably elect to come under either the 20-50 or the 40-60 test. Rental units may not be used on a transient basis except in the case of certain transitional housing for the homeless.

3. ***Rent Restriction***. The gross rent charged to a tenant in a qualified low-income unit may not exceed 30% of the qualifying income level for the tenant's family size. Beginning with projects first obtaining credit allocations after 1989, the allowable rent for low-income units will no longer be based on actual occupancy. A studio apartment will be deemed to be occupied by one person, and larger apartments will be deemed occupied by 1.5 persons times the number of bedrooms in the unit. Gross rent is considered to include utilities paid by the tenant, other than telephone expenses, but does not include payments under Section 8 of the U.S. Housing Act of 1937 or similar rental assistance or supportive payments received on behalf of the tenant.

4. ***State Credit Authority***. Owners of otherwise qualified projects are not entitled to take the credit unless authorized to do so by the appropriate state or local agency. Owners obtaining new credit allocations must also enter into an agreement with their local housing credit agency to maintain the low-income status of qualifying units for 30 years. No credit authority is required for projects financed by tax-exempt bonds subject to the private activity bond volume limitation.

5. ***Certification***. Owners of low-income housing projects are required to file a certification with the IRS before claiming the credit.

DHCD publishes annually the rent and income limits for the federal credit. For the Baltimore Metropolitan Statistical Area (MSA) in tax year 2005, gross rents must not exceed, for a household of three, $32,450 under the 50% test and $38,940 under the 60% test. For Maryland counties in the Washington DC MSA, the limits would be $40,200 and $48,240, respectively. DHCD advises that a total of approximately $10.6 million in federal credits is expected to be awarded in tax year 2006 with an additional $2 to $3 million in credits available for projects financed with tax exempt bonds. Twelve other states provide for some form of low-income housing credits in tax year 2006.

State Fiscal Effect:

Appropriations to the Reserve Fund

The bill provides that the Governor can appropriate funds to the reserve fund. The bill does not require or suggest an amount that should be appropriated. The bill does state, however, that DHCD may not award more than $3 million in credits in each fiscal year. Assuming a fully funded and viable program, State expenditures would increase by $3 million annually beginning in fiscal 2008.

Revenue Effects from Reserve Fund Transfers

The bill requires the Comptroller to transfer money from the reserve fund to the general fund an amount that is anticipated to offset credits that would be claimed during the fiscal year. Based on the amount of federal credits issued to Maryland, it is assumed that the maximum $3 million in credits would be issued in each fiscal year. The Joint Committee on Taxation (JCT) estimates that 70% of the federal credit is claimed by corporations. Twenty-four percent of corporate income tax revenue is distributed to the TTF. All of the money transferred from the reserve fund by the Comptroller in anticipation of credits being claimed is to be deposited in the general fund, and losses to the TTF would not be offset. As a result, it is estimated that general fund revenues would increase and TTF revenues could decrease by approximately $504,000 annually beginning in fiscal 2008 due to money being transferred back to the general fund for tax credits claimed against the corporate income tax.

It is assumed that the amount of credit claimed in each tax year would be equal to the amount stated in the initial credit certificate so that credits claimed in each tax year would be offset by a transfer from the reserve fund. The final amount of the credit, however, could be less than the amount stated on the initial credit certificate if actual expenses are less than the estimated expenditures stated on the approved application. To the extent final credit amounts are less than the amount stated on the initial credit certificate, revenues could increase in these fiscal years.

It is also assumed that taxpayers claim the credit in the tax year that corresponds to the fiscal year in which the Comptroller transfers funds to the general fund on notification of a certified credit. To the extent that taxpayers claim the credit in a tax year after the fiscal year in which the transfer is made, general fund revenues could increase in earlier fiscal years and potentially decrease by a corresponding amount in later fiscal years. The extent of this lag, if any, cannot be reliably estimated at this time. This timing issue, however, does not alter the total cost of the bill.

Administrative Costs

The Comptroller's Office reports that it would incur a one-time expenditure increase of $32,850 to add the tax credit to the personal income tax form. This includes data processing changes to the SMART income tax return processing and imaging systems, and system testing.

DHCD would require an additional full-time administrator to administer the program. Accordingly, general fund expenditures could increase by approximately $52,800 in fiscal 2007. This estimate includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Positions	1
Salary and Fringe Benefits	$49,319
Equipment	2,825
Operating Expenses	705
Total FY 2007 DHCD Expenditures	**$52,849**

Legislative Services advises that DHCD already administers certain aspects of the federal credit. The need for additional staff is premised on the fact that existing staff could not absorb the additional workload that is anticipated as a result of the tax credit program.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office, Department of Housing and Community Development, Internal Revenue Code, Department of Legislative Services

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