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Affordable Housing Alert

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Treasury publishes far easier rules for using ARPA funds in LIHTC projects

By Forrest David Milder

Treasury no longer requires complicated formulas to determine treatment of loans of ARPA funds to Section 42 projects, provided certain requirements are met.



What's the Impact?

- / The new rules significantly reduce administrative complexity and encourage the use of ARPA funds for affordable housing
- / Compliance with the new rules is likely to be easy for most borrowers

Many of you will remember that the American Rescue Plan Act of 2021 (ARPA) provided for State and Local Fiscal Recovery Funds (SLFRF) that could be provided to assist in responding to the COVID-19 pandemic. Under applicable law, these ARPA funds had to be fully expended by the end of 2026. In general, for Section 42 low-income housing tax credit (LIHTC) projects, loans of these funds made sense from a tax perspective. This is because loans of these funds avoided making their receipt taxable to the recipient, and loans also made the amount advanced eligible for inclusion in LIHTC-eligible basis. At the same time, there was great concern that the mere loan of ARPA funds to a project did not amount to "expending" the funds, as required by the enabling law, because someday, the loan would be repaid. Instead, the present value of the loan

repayment had to be computed, and somewhat complicated algebra (and additional funds from the lender) were required to show that the ARPA funds had been fully spent.

Treasury has now decided to treat 20-year (or longer) loans of ARPA funds to Section 42 projects (as well as certain other housing) as “expended,” provided certain requirements are met. In other words, the math part of these loans is no longer required. The Treasury’s full “[Coronavirus State and Local Fiscal Recovery Funds Final Rule: Frequently Asked Questions](#)” is available online—but here’s the relevant portion for Section 42 projects:

Loans to fund investments in affordable housing projects

Notwithstanding the above requirements for loans with maturities beyond **December 31, 2026**, Treasury has determined that SLFRF funds may be used to finance certain loans that finance affordable housing investments, as it is typical for state and local governments to finance such investments through loans and because the features of these loans significantly mitigate concerns about funds being deployed for purposes of recycling funds, potentially for ineligible uses, following the SLFRF program’s expenditure deadline. Specifically, under the “public health and negative economic impacts” eligible use category, recipients may use SLFRF funds to make loans to finance affordable housing projects, funding the full principal amount of the loan, if the loan and project meet the following requirements:

- / The loan has a term of not less than 20 years;
- / The affordable housing project being financed has an affordability period of not less than 20 years after the project or assisted units are available for occupancy after having received the SLFRF investment; and
- / For loans to finance projects expected to be eligible for the low-income housing tax credit (LIHTC) under section 42 of the Internal Revenue Code of 1986 (the Code), the project owner must agree, as a condition for accepting such a loan, to waive any right to request a qualified contract (as defined in section 42(h)(6)(F) of the Code); and the project owner must agree to repay any loaned funds to the entity that originated the loan at the time the project becomes non-compliant, including if such project ceases to satisfy the requirements to be a qualified low-income housing project (as defined in section 42(g) of the Code) or a qualified residential rental project (as defined in section 142(d) of the Code), or if such project fails to comply with any of the requirements of the extended low-income housing commitment that are described in section 42(h)(6)(B)(i)-(iv) of the Code.

Loans that fund investments in affordable housing projects under the public health and negative economic impacts eligible use category and meet the above criteria may be considered to be expended at the point of disbursement to the borrower, and repayments on such loans are not subject to program income rules. Loan modifications are permitted if the modifications do not result in repayment of all or substantially all funds to the lender prior to the end of the affordability period. To reduce administrative

complexity, the start date of the 20-year affordability covenant may conform to the start date of other covenants on the same project or units that are required by another source of federal or state funding associated with the project or units.¹

Takeaways

These rules should be easy enough for LIHTC projects to comply with, since most of this is just living with the LURA that applies to Section 42 anyway. Note that there is one notable addition: the borrower must agree to waive any right to request a qualified contract.

The “qualified contract process” is a way for a developer in year 15 to ask a state agency to either find a buyer for the project who will continue to apply the affordable housing restrictions or remove the restrictions if a buyer cannot be found. The price the buyer has to pay is a formula that can sometimes turn out to be higher than fair market value, thereby discouraging the continuation of the restrictions. In other words, in some situations, it may give a developer a way to get the state agency to remove the restrictions after year 15. The new Treasury rules require an owner of a project that benefits from a loan of ARPA funds to not take advantage of that year 15 process.

Also, note that projects that are not subject to Section 42 but which serve households at or below 65% of the area median for at least 20 years are presumed eligible for ARPA/SLFRF funds. This is welcome news for affordable projects that don’t benefit from LIHTCs.

Nixon Peabody’s [Community Development Finance](#) and [Affordable Housing](#) teams have been following this provision and will continue to provide updates on developments. For more information on the content of this alert, please contact your Nixon Peabody attorney or:

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¹ See “[Coronavirus State and Local Fiscal Recovery Funds Final Rule: Frequently Asked Questions](#)” at page 35.