Qualified Contract Process

In order to receive the full benefit of the Low Income Housing Tax Credits that a property may generate, the property must satisfy all low income requirements for the applicable compliance period. For properties receiving Tax Credits in 1987, 1988, and 1989, this compliance period is for a 15 year period. For owners receiving an award of Tax Credits in 1990 or later years, a change in federal law requires an additional 15 years of compliance, to a total of 30 years. This increased period of time is commonly known as the extended use period.

Provided the owner did not waive such rights in the Indenture of Restrictive Covenants (extended use agreement), Section 42(h)(6)(E) of the Internal Revenue Code (IRC) allows the extended use period to terminate after the original 15 year compliance period, if the housing credit agency (PHFA) is unable to present a qualified contract (QC) for the acquisition of the low income portion of the Tax Credit property by any person who will continue to operate such portion as a qualified low income building. The housing credit agency has a one year period to respond to a formal request from the owner.

The process for making a formal request to PHFA for a qualified contract is detailed below.

Eligibility

In order for the owner to request a qualified contract from PHFA, the following minimum criteria must be met:

1. The Tax Credit property must have completed the 14th year of its compliance period. For projects with multiple buildings that were placed in service in different years, this means the end of the 14th year of the last building in the development that was placed in service.

2. The Tax Credit property must be in compliance with all Section 42 requirements. Owners must correct all such violations prior to submitting a request. (Owner must certify that it has not been notified of any audit or investigation or disallowance pertaining to Section 42 by the IRS and must provide any copies of IRS audit findings or disallowances which it has received during the tax credit period.)

3. The owner must have secured a complete, unconditional waiver of all purchase options, including the right of first refusal of a nonprofit general partner.

4. Owner must have consent, evidenced in writing, of all of its limited partners to negotiate on behalf of the partnership for a QC.

5. The owner may only request a Qualified Contract from the Agency one time.

Fees

1. PHFA will assess the owners a non-refundable fee of $2,500 for processing qualified contract requests.

2. Owners will be required to cover all costs incurred by PHFA in processing and evaluating a QC request. In addition to executing an agreement to reimburse all costs, owners must deposit with PHFA $30,000 to cover anticipated third party costs. This deposit may be used by PHFA to pay for such third party costs as:

   a. A physical needs assessment of the property
   b. An appraisal of the property
   c. A market study of the property
   d. A Phase I environmental study and if necessary Phase II environmental study
   e. PHFA retention of an accounting firm to recalculate and confirm the qualified contract price requested by the Owner in the application.

   If third party costs exceed the original deposit from the owner, the Agency shall make a request for additional deposits. The processing of the qualified contract request will be suspended during any time an additional deposit has been requested from the owner until such funds have been received by PHFA. If requested funds are not received within 15 days of notice to the owner, the processing of the qualified contract request will be terminated. Suspension in accordance with this paragraph or any requirement set forth herein shall also suspend the one year time period for Agency action.

Notice of Intent to File a Request (Preliminary Application)

The Agency will require an advance notice of intent to file, in the form of a Preliminary Application (Exhibit A), before an owner may submit a qualified contract request. This notice will not bind owners to submit a request and does not start the one year period for response from PHFA. After receiving the Preliminary Application, the Agency will determine the eligibility of the owner to submit a qualified contract request by confirming it has met the eligibility requirements indicated above and the owner did not waive its right in the Indenture of Restrictive Covenants to request a qualified contract.

Upon review of the Preliminary Application and eligibility of the property, the Agency will notify the owner in writing of its eligibility to submit a qualified contract request. The Agency will send specific instructions for a Qualified Contract Request (outlined below) and will provide a form of the reimbursement agreement. The Agency may waive some or all of the following requirements for properties consisting of twenty (20) or less units.

Qualified Contract Request

To file a qualified contract request with PHFA, the following documentation must be submitted to and received by PHFA:

   a. A cover letter indicating the intentions of the owner along with the proposed qualified contract price;
   b. All fees for processing the request and all initial deposits for third party costs;
   c. An executed Reimbursement Agreement (executed by an authorized representative of the owner);
   d. Certification that no IRS audit, investigation or inquiry is pending or underway, and copies of the findings of any final audits, investigations or reports of the IRS which have been received;

e. Certification that the property is in compliance with all Section 42 requirements;
f. An opinion from an independent certified public accountant setting forth the calculation of the qualified contract price requested by the owner and certifying that the owner is entitled to the qualified contract price requested;
g. All 8609s related to the project, showing part II completed;
h. Annual audited financial statements for each year of project operation;
i. Annual partnership or ownership entity tax returns for each year of project operation;
j. Loan documents for all secured debt during the compliance period (and evidence that the Owner is in good standing, is not in default; and is not aware of any event, which but for the passage of time, would constitute default under the outstanding mortgages, liens or indentures securing the real property);
k. Partnership agreement, with all amendments;
l. Evidence of consent of all partners and lenders to seek a qualified contract (or proof consent is not necessary);
m. Any third party bone fide offers to purchase the property received within one year of the date of request;
n. Title report showing all outstanding liens and encumbrances on title; and

The one year period for response from the Agency will not begin until the Agency determines that the owner has met all of the submission requirements.

Qualified Contract

The qualified contract is defined in Section 42 (h)(6)(F) of the IRC as a bona fide contract to acquire the non-low income portion of the building for fair market value and the low income portion of the building for an amount not less than the applicable fraction of:

(i) The sum of:
  (I) The outstanding indebtedness secured by, or with respect to, the building, plus
  (II) The adjusted investor equity in the building, plus
  (III) Other capital contributions not reflected in the amounts described in subclause (I) or (II), reduced by
(ii) Cash distributions from (or available for distribution from) the project.

“Adjusted investor equity” is defined in Section 42 (h)(6)(G) as the aggregate amount of cash taxpayers invested with respect to the project increased by the amount equal to:

(i) Such amount, multiplied by
(ii) The cost of living adjustment for such calendar year. Cost of living increases in excess of 5 percent should not be taken into account.

Presentation of a Qualified Contract

PHFA will have a one year period to find a buyer for the property. Upon determination by the Agency that all submission requirements have been received, the Agency will forward a letter to the owner notifying the owner that the one year period has commenced. The Agency may require a form of notification to be provided to the residents alerting them to the possible disposition of the property. (Owners are advised that the property will remain subject to all requisite IRS restrictions, including tenant protections enunciated in Rev Proc. 2004-82, throughout the processing period and may continue to be subject to such requirements throughout the project's extended use period.)

By submitting a qualified contract request, the owner grants PHFA the authority to market the development and provide applicable information to interested parties. Any and all information, including property and partnership financial statements and tax returns may be provided to third parties or otherwise used by the Agency as it deems appropriate in its discretion. The Agency must have continuous cooperation from the owner. Lack of cooperation will cause the processing of the qualified contract request to be terminated.

If at any time, during the Agency's processing of a qualified contract request, the partnership receives notification of audit or investigation by the IRS regarding the tax credit property, the one year period will be suspended and processing will stop until the investigation or audit is complete. In addition, any event of default or material noncompliance with the terms of any of the mortgages, liens or encumbrances on the property or any material noncompliance with Section 42 will result in suspension of the processing of a QC and will disqualify the Owner from seeking a QC or extend the one year period the Agency has to respond.

In the event processing is suspended or terminated due to any noncompliance or audit, the property must continue to be maintained and operated under the extended use agreement.