AFFORDABLE HOUSING TAX CREDIT

EVALUATION SUMMARY | APRIL 2022 | 2022-TE25

TAX TYPE	Income	REVENUE IMPACT (TAX YEAR 2018)	Not reportable
YEAR ENACTED	2014	NUMBER OF TAXPAYERS	Not reportable
REPEAL/EXPIRATION DATE	December 31, 2024		

KEY CONCLUSION: The tax credit acts as a significant funding source for affordable housing development and appears to be meeting its purpose of encouraging the expansion of affordable housing in Colorado.

WHAT DOES THIS TAX EXPENDITURE DO?

The Affordable Housing Tax Credit [Section 39-22-2102, C.R.S.] provides housing developers and investors a credit against state income tax or insurance premium tax liability for direct capital investment in affordable housing projects in the state. The Colorado Housing and Finance Authority (CHFA) administers the credit and is responsible for awarding credits at the minimum amount necessary to make affordable housing projects financially feasible. CHFA caps the total credit award per project to $1 million per year, which is available to taxpayers each year for a 6-year period, resulting in a maximum total credit of $6 million per taxpayer. Statute limits the total annual amount of credits awarded each year to $10 million.

WHAT IS THE PURPOSE OF THIS TAX EXPENDITURE?

House Bill 14-1017, which reestablished the Affordable Housing Tax Credit and expanded other affordable housing programs, was intended "...to expand the availability of affordable housing in the state."

Additionally, House Bill 22-1051, which was introduced during the 2022 Legislative Session and was under consideration at the time this report was published, would clarify that the credit's purpose is "to address the shortage of affordable housing in the state and increase access to affordable housing by encouraging developers to build units specifically restricted for residents with incomes below the area median income and also to encourage private sector investment into the development and preservation of affordable housing."

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

We did not identify any policy considerations on this evaluation.

AFFORDABLE HOUSING TAX CREDIT

EVALUATION RESULTS

WHAT IS THE TAX EXPENDITURE?

The Affordable Housing Tax Credit [Section 39-22-2102, C.R.S.] provides housing developers and investors a credit against state income tax or insurance premium tax liability for direct capital investment in affordable housing projects in the state. The credit was originally established in 2000 as a 2-year pilot program, which expired in 2002. In 2014, House Bill 14-1017 reestablished the credit, with the first credits under the bill awarded in 2015. Since that time, the credit has been reauthorized through 2024, and is currently set to expire on December 31, 2024. Additionally, House Bill 22-1051, which was under consideration at the time this report was published, would extend the credit until December 31, 2034.

The Colorado Housing and Finance Authority (CHFA), a statutorily created non-state entity, oversees the allocation of the credit. Statute requires that any projects to which CHFA awards the credit must qualify as a low-income housing project under Section 42 of the IRS code, which requires:

- 20 percent of housing units for tenants who earn 50 percent or less of area median income (AMI). For example, a 100 unit development located in an area with a $50,000 AMI would need to contain at least 20 units occupied by individuals whose gross annual income is $25,000 or less.

- 40 percent of units for tenants who earn 60 percent or less AMI. For example, a 100 unit development located in an area with $50,000 gross median income would need to contain at least 40 units occupied by individuals whose gross annual income is $30,000 or less.

- 40 percent or more of the units are, on average, restricted to tenants whose income is less than 60 percent of AMI. For example, a 100 unit development could designate 30 units for tenants with incomes of 50 percent of AMI or less and 10 units for tenants with incomes of 70 percent or less because the average income of all the income restricted units (40 percent of the total units) is less than 60 percent of AMI.

Additionally, CHFA requires that project owners agree to maintain the units' affordable status for at least 30 years, with a preference for 40 years.

The credit is awarded as an annual amount that is available to the taxpayer each year for a 6-tax year period. For example, a taxpayer awarded a $1 million annual credit, would be able to claim a total credit amount of $6 million over 6 years. The 6-year period starts when the development is placed "in service," meaning that tenants occupy the development. According to stakeholders, projects typically are not placed in service until at least 1 to 2 years after the credit is awarded. If a taxpayer's annual credit amount exceeds their tax liability during any tax year, they cannot claim a refund, but may carry forward the credit amount for up to 11 years after the project is placed in service.

Under Section 39-22-2102(2), C.R.S., CHFA is responsible for determining the credit amount it awards to eligible projects, but statute requires that this should be "the least amount necessary to ensure the financial feasibility of a qualified development" and no more than 30 percent of the qualified basis cost related to developing or rehabilitating the units reserved for eligible tenants. Statute limited the aggregate annual credits issued by CHFA to $5 million in Calendar Years 2015 through 2019, increasing to $10 million in 2020 through 2024. This limit applies to the annual credit award amounts, not the aggregate total credits available over the 6-year credit period, which means that if CHFA awards up to the $10 million limit in any given year, taxpayers awarded the credit that year would be able to claim up to a total of $60 million in credits over 6 years. However, credits allocated to housing projects in disaster-relief areas in Boulder, Larimer, and Weld counties were not subject to this limitation in Calendar Years 2015 or 2016. Unallocated credits, if any, from the preceding calendar year can be issued in the following years. Under its administrative authority, CHFA further limits the credit to $1 million annually ($6 million total) per owner or per project. Statute also requires each project to have local government financial support. The financial support can come in the form of land donation, cash, or other contributions.

In order to use the credit availability to leverage a separate federal affordable housing credit, which is also administered by CHFA—known as the 4 Percent Federal Tax Credit—CHFA requires that projects that receive the State's credit apply, and be approved, for the federal credit as well. The 4 Percent Federal Tax Credit, which typically offers a larger tax benefit than the State's Affordable Housing Tax Credit, provides credits against the federal income tax equivalent to approximately 30 percent of a project's development costs.

To apply for the Affordable Housing Tax Credit, project owners submit an application to CHFA, which must include financial information, records of a public hearing being conducted in the community of the development's location, market analysis, environmental report, appraisals, evidence of interest from lenders and equity investors, third party cost estimates, and the resumes of the development and management team. The application should demonstrate that the credit is necessary to allow for the project to move forward and that the project is fully prepared to come to fruition if the credit is granted. CHFA reviews the application and determines the minimum credit amount necessary to make the project financially feasible. If approved, CHFA issues an award letter to the project owner(s) who establishes a partnership with an investor for funding that can be used to pay for project costs. Upon lease-up and stabilization of the project, CHFA issues an allocation certificate to the project. As a partner in the project's ownership, the investor can offset their tax liability with the credits.

To claim the credit, taxpayers must submit the allocation certificate they received from CHFA to the Department of Revenue (Department) when they file their income taxes. Any credits the owner has transferred to investors must be reported to the Department using Form DR 0104CR for individuals, Form DR 0112CR for corporations, Form DR 0106CR for S corporations and other pass through entities, and Form DR 0105 for estates and trusts. Insurance companies that invest in affordable housing projects may also claim the credit; however, they do not file with the Department, but instead claim the credit against their insurance premium tax filed with the Division of Insurance.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURE?

Statute does not directly state the intended beneficiaries of the Affordable Housing Tax Credit. Based on our review of the statutory language and interviews with CHFA staff, we considered the intended direct beneficiaries to be affordable housing development owners and investors. Owners, which include public housing agencies, nonprofit entities, and for-profit entities, use the credit to draw the interest of investors, who help fund construction costs. Although the credit is not available until the development is placed in service, project owners can use it to secure immediate financing for project costs by entering into a partnership with an investor, which then provides project funding in return for being able to claim the credit in future years.

Individuals and families who live in the new affordable housing developments also benefit from the credit to the extent that it encourages the expansion of affordable housing that reduces their housing costs. According to CHFA, the need for affordable housing is a growing concern in Colorado. Population increases, the COVID-19 pandemic, and an existing shortage in affordable housing have all contributed to an increased need for affordable housing across the state. Generally, rents that are less than 30 percent of a household's income are considered affordable. In 2020, CHFA found that about 51 percent of Colorado renters were paying 30 percent or more of their household income on rent, with 24 percent of these renters paying more than 50 percent of their household income on rent.

WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

According to the bill title for House Bill 14-1017, which reestablished the Affordable Housing Tax Credit and expanded other affordable housing programs, the bill was intended "…to expand the availability of affordable housing in the state." Additionally, House Bill 22-1051, which was introduced during the 2022 Legislative Session and was under consideration at the time this report was published, would clarify that the credit's purpose is "to address the shortage of affordable housing in the state and increase access to affordable housing by encouraging developers to build units specifically restricted for residents with incomes below the area median income and also to encourage private sector investment into the development and preservation of affordable housing."

IS THE TAX EXPENDITURE MEETING ITS PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

We found that the Affordable Housing Tax Credit is meeting its purpose by acting as a significant additional incentive to encourage the development of affordable housing projects in the state.

Statute does not provide quantifiable performance measures for this credit. Therefore, we created and applied the following performance measure to determine the extent to which the credit is meeting its purpose.

PERFORMANCE MEASURE: *To what extent does the credit encourage the expansion of affordable housing in the state?*

RESULT: Overall, we found that the credit encourages the development of additional affordable housing in the state by subsidizing a substantial portion of the funding necessary to complete projects. The credit is used to leverage the assistance provided by the larger 4 Percent Federal Tax Credit, and it provides significant additional funding. To quantify the credit's potential impact on encouraging affordable housing projects, we used CHFA data to compare the credit amount awarded to project owners with the total project costs. We also considered the benefit provided by the federal credit since CHFA requires that any project that receives the state credit also have applied and been approved for the 4 Percent Federal Tax Credit in order to leverage available federal support. As shown in EXHIBIT 2, the equity generated from state credits awarded between Calendar Years 2015 through 2020, was equivalent to 14 to 19 percent of the total project costs reported by project owners. When coupled with the federal credit, the credits were equivalent to 50 to 58 percent of project costs.

EXHIBIT 2. AFFORDABLE HOUSING CREDITS AS A PERCENTAGE OF TOTAL PROJECT COSTS FOR PROJECTS AWARDED THE STATE AFFORDABLE HOUSING TAX CREDIT CALENDAR YEARS 2015-2020

Calendar Year	Total Project Costs	State Tax Credit as a Percentage of Total Project Costs	Federal Tax Credit as a Percentage of Total Project Costs	Combined Credits as a Percentage of Total Project Costs
2015	$452 million	19%	31%	50%
2016	$289 million	19%	33%	52%
2017	$358.9 million	16%	35%	51%
2018	$159.3 million	18%	32%	50%
2019	$399.4 million	14%	37%	51%
2020	$257.2 million	14%	44%	58%

SOURCE: Office of the State Auditor analysis of CHFA data.

We also found projects awarded the Affordable Housing Tax Credit have provided a significant number of affordable housing units. As shown in EXHIBIT 3, according to CHFA data, the 70 projects that were awarded the credit between Calendar Years 2015 to 2020, created 6,832 additional affordable housing units in the state.

EXHIBIT 3. NUMBER OF AFFORDABLE HOUSING PROJECTS AND UNITS SUPPORTED BY THE AFFORDABLE HOUSING TAX CREDIT CALENDAR YEARS 2015 TO 2020

Year	Number of Projects	Units Supported
2015	16	1,896
2016	12	1,062
2017	12	1,299
2018	8	535
2019	12	1,272
2020	10	768
Total	**70**	**6,832**

SOURCE: Office of the State Auditor analysis of CHFA data.

Although the projects awarded the credit provided a significant amount of additional affordable housing, it is possible that some of the projects would have gone forward in some form without the credit. As discussed, projects may be able to receive federal credits that are typically larger than the state credit and we could not determine what decisions project owners would have made in the absence of the credit. However, CHFA reviews the financial feasibility of projects that apply for the credit to limit the credit to projects that it determines require additional funding. Therefore, it appears that the availability of the state credit is an important tool to encourage additional investment in affordable housing.

According to the CHFA staff and stakeholders we contacted, projects awarded the state credit require both the state and federal credits in order to make the projects financially feasible because it is difficult to find other sources of funding for affordable housing projects. According to stakeholders we spoke with, when applicants do not receive the state credit, they may abandon the project, delay it, reduce the number of affordable units they include, or increase the rental rates. For example, one developer that applied for both the state credit and 4 Percent Federal Tax Credit, but did not receive the state credit, reported that it was still able to construct the development with the same number of affordable housing units originally planned. However, the developer reduced the number of very low-income units offered and redistributed these units to higher-income units to increase the amount of rental income to make up for not receiving the state credit. The information in EXHIBIT 4 was provided by this developer and illustrates the impact of the state credit on one project.

EXHIBIT 4. EXAMPLE OF UNIT REDISTRIBUTION WITH AND WITHOUT THE STATE AFFORDABLE HOUSING TAX CREDIT

Unit Resident's Income as a Percentage of AMI	Number of Units Available with 4 percent Federal and State Tax Credits	Number of Units Available with 4 Percent Federal Tax Credit Only	Unit Redistribution
20 percent AMI	2	0	-2
30 percent AMI	7	5	-2
40 percent AMI	10	0	-10
50 percent AMI	15	0	-15
60 percent AMI	33	77	+44
70 percent AMI	15	0	-15
Total Units	**82**	**82**	**0**
Average Affordability	54 percent of AMI	58 percent of AMI	N/A

Source: Affordable Housing Developer.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURE?

Although CHFA has issued a substantial amount of credits, we lacked the data necessary to determine the Affordable Housing Tax Credit's impact to state revenue and the benefit it has provided to taxpayers. Specifically, according to Department publications and data, taxpayers claimed $7,000 in credits in Tax Year 2015, there were no claims in Tax Year 2016, and the Department is not able to release the amount claimed for Tax Year 2017 due to the low number of claims. In Tax Year 2018—the most recent year for which the Department was able to provide information— the revenue impact was significant, but because few taxpayers claimed the credit, under Section 39-21-113(4)(a) and (5), C.R.S., which protects the confidentiality of tax information, we cannot provide the annual revenue impact. Additionally, because the credit was first awarded to taxpayers in Tax Year 2015, it is likely that its revenue impact and usage have increased significantly since Tax Year 2018, but we lacked information to quantify this impact.

Based on the amount of credits CHFA awarded during Calendar Years 2015 through 2020, about $209 million in total credits could potentially have been available for taxpayers to claim during those years. However, the revenue impact to the State has likely been less because taxpayers cannot claim the credit until the qualifying project is completed and placed in service, which typically takes at least 1 to 2 years following a credit award. Thus, credits awarded in Calendar Year 2015, would likely not be available to taxpayers until Tax Year 2016 or 2017. Further, to the extent that an available credit exceeds a taxpayer's tax liability in a given year, the taxpayer can carry the credit forward for up to 11 years, meaning that the revenue impact of credits issued from Calendar Year 2015 through 2020, may not be fully realized until Tax Year 2033 (assuming a 2-year delay before the credit can be claimed and 11 years of potential carry forwards). Additionally, it is possible that some taxpayers who have credits available will never claim them, which is common for tax credits in general, although we lacked information necessary to estimate the amount of Affordable Housing Tax Credits for which this may occur.

As discussed, the credit has also supported the development of a significant number of affordable housing units in the state. To assess the credit's cost-effectiveness, we used CHFA data to compare the total credits awarded each year to the total number of affordable housing units created from the projects receiving credit awards. We found that for credits CHFA awarded during Calendar Years 2015 through 2020, about $47,000 in state credits were awarded for each additional unit of affordable housing that was created. Additionally, each of these state credit awards was coupled with the 4 Percent Federal Tax Credit, with a total of about $146,000 in state and federal credits awarded for each unit of affordable housing created. EXHIBIT 5 shows the credits awarded for each unit of housing supported by the credit for Calendar Years 2015 through 2020.

EXHIBIT 5. CREDITS PER UNIT OF AFFORDABLE HOUSING CREATED BY PROJECTS AWARDED TAX CREDITS CALENDAR YEARS 2015 THROUGH 2020

Year	Units Supported	State Tax Credits Awarded (Millions)	State Tax Credits Awarded Per Unit	State and Federal Tax Credits Combined (Millions)	State and Federal Tax Credits Per Unit
2015	1,896	$85.8	$45,238	$226.3	$119,359
2016	1,062	$53.8	$50,614	$150.5	$141,731
2017	1,299	$58.5	$45,066	$183.2	$141,034
2018	535	$28.5	$53,251	$79.6	$148,693
2019	1,272	$56.4	$44,357	$204.6	$160,869
2020	768	$37	$48,155	$150.6	$196,093
Total	6,832	$320	$46,832	$994.8	$145,609

Source: Office of the State Auditor analysis of CHFA data.

According to CHFA, the average market rent for apartments of all sizes in Colorado in 2020 was $1,403 and the average household living in an apartment supported by the Affordable Housing Tax Credit paid $767 in rent. Therefore, we estimate that households received approximately a $636 per month, or $7,632 per year, discount in rent for each affordable housing unit supported by the credit. CHFA requires each project owner to maintain the affordable housing units for which it received credits for a minimum of 30 years. Therefore, if the amount of rental discount per unit was equivalent to $7,632 per year over a 30-year period, the rental discount provided by the credits would be about $229,000 per household. This significantly exceeds the $48,155 in credits provided by the State in Calendar Year 2020 for each unit and also exceeds the $196,093 in state and federal credits combined that were awarded for each unit. Further, the full benefit likely exceeds this estimate because according to CHFA, in practice, project owners typically agree to maintain the affordable housing units for longer than 30 years and market rents are likely to grow, which would increase the rental discount over time.

We also found that projects awarded the credit between Calendar Years 2015 to 2020, were distributed across 11 counties in the state. Credit awards were concentrated in the Denver metropolitan area, with Adams, Arapahoe, Denver, and Jefferson counties receiving about 55 percent of the total credit amount awarded. EXHIBIT 6 provides the number of projects and total credits awarded for projects approved for credits during Calendar Years 2015 through 2020.

EXHIBIT 6. DISTRIBUTION OF AFFORDABLE HOUSING TAX CREDIT AWARDS BY COUNTY CALENDAR YEARS 2015 THROUGH 2020

County	Number of Projects	State Tax Credits Awarded (in millions)
Adams	5	$20.7
Arapahoe	5	$25.4
Boulder[1]	12	$61.7
Chaffee	1	$2.2
Denver	23	$100.1
El Paso	3	$11.5
Jefferson	7	$31.4
Larimer[1]	8	$43.0
Pitkin	1	$2.0
Routt	1	$3.7
Weld[1]	4	$18.1

SOURCE: Office of the State Auditor review of CHFA data.
[1]Boulder, Larimer, and Weld Counties received an additional allocation of credits in Calendar Years 2015 and 2016 as part of disaster recovery efforts in those years.

In addition to reducing housing costs, construction for projects awarded the credit also likely benefits the local economy by supporting construction industry jobs, as well as purchases of materials and land. CHFA uses an input-output economic model to estimate the economic benefit associated with the construction for projects it approves for the credit and estimates that the economic impact of projects awarded the credit in 2020 was $483.3 million. However, because it is unknown what economic activity and investments may have occurred if the projects were not approved, it is difficult to determine the net impact of the credit on the local economy. The credit may also benefit the local economy to the extent that it brings in new residents to an area and by reducing housing costs, which allows residents to spend additional funds in the area. We lacked data necessary to quantify these impacts.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURE HAVE ON BENEFICIARIES?

If the Affordable Housing Tax Credit was eliminated, current beneficiaries would see a significant decrease in funds available to support affordable housing projects. As discussed, the credits awarded during Calendar Year 2020, were equivalent to about 14 percent of total project costs, which would have to be made up through other funding sources. Because CHFA currently targets credit awards to projects that it determines would not be able to go forward without additional support, it is likely that less affordable housing would be constructed in the state without access to the credit. Although the 4 Percent Federal Tax Credit, which CHFA currently couples with the state credit, would still be available, this credit alone may not provide significant enough support to make some projects feasible. Additionally, according to stakeholders, it is possible that some affordable housing projects that would otherwise benefit from the state credit would still go forward, but would offer fewer affordable-housing units or would offer fewer units that would be affordable to residents with very low incomes.

CHFA and stakeholders we spoke with indicated that the credit is necessary to increase the availability of affordable housing in Colorado. They stated that the tax credit program—meaning resources provided by the federal and state credits—is the most important funding stream for affordable housing development, while other resources, such as income from grants, are helpful as "gap" funding, but are generally not sufficient on their own.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

We identified at least 18 other states with a credit similar to Colorado's Affordable Housing Tax Credit. These credits vary in terms of:

- ELIGIBILITY CRITERIA. Although many states have similar eligibility requirements as Colorado, some states, like Utah, set more stringent affordability criteria, such as requiring more units at lower AMIs.

- ANNUAL AWARD PERIOD. The federal annual award period is 10 years, but most states provide annual awards for between 4 to 6 years.

- RELATIONSHIP TO FEDERAL CREDITS. Some states only award their credits in conjunction with the 4 Percent Federal Tax Credit, as is the case for Colorado. However, others, like New Mexico, award credits independently from the federal credit.

- CREDIT AMOUNT. The credit amount in other states may be subject to minimums or caps at both the individual project levels, as well as the statewide level. For example, Maine's state credits match the federal amounts, up to a $10 million statewide cap. Other states, like Hawaii, do not have a state cap, but limit the credits to 50 percent of the federal credit allocation.

ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

A variety of programs exist within Colorado, operated by the State, federal government, or a combination of the two, to support the development of affordable housing. Some of these programs, administered by the Department of Local Affairs (DOLA), include:

- COLORADO HOUSING INVESTMENT TRUST FUND—Provides short-term loans to affordable housing developers and housing authorities. About $36 million has been allocated to the Fund since it was created in 2012.

- HOUSING DEVELOPMENT GRANT—Provides funds through a competitive application process to improve or expand the supply of affordable housing, to finance foreclosure prevention activities, and to fund the acquisition of data necessary to advise the State Housing Board on local housing conditions. Some of the grant funding is specifically designated for rural communities and specific programs, such as developing housing for people with mental and behavioral health disorders.

- PRIVATE ACTIVITY BONDS—These tax-exempt bonds are provided by the federal government and are distributed to states using a population-based formula that determines an annual "bond cap." In accordance with Colorado statute, DOLA allocates nearly 50 percent of the bond cap to CHFA and a majority of the remaining bonds to counties. Bonds are issued by CHFA and counties, which are required to support 4 Percent Federal Tax Credit projects. CHFA uses these in conjunction with the 4 Percent Federal Tax Credit and Affordable Housing Tax Credit awards.

Additionally, the federal government also provides credits that support the development of affordable housing in the state:

- 4 PERCENT FEDERAL TAX CREDIT—As discussed, this credit is equivalent to approximately 35 percent of project owners' costs for the construction or rehabilitation of an affordable housing development. This credit is also administered by CHFA at the state level. Unlike the 9 Percent Federal Tax Credit, discussed in the next bullet, states are not subject to a limitation on the amount of credits they can issue. However, applicants for this credit must have received private activity bonds as part of their project financing, which is annually limited by a per capita amount. Although CHFA requires recipients of the State Affordable Housing Tax Credit to also be approved for the 4 Percent Federal Tax Credit, applicants can still receive the 4 Percent Federal Tax Credit regardless of whether they are awarded the state credit; however, the application process to receive just the 4 Percent Federal Tax Credit is separate from the process to receive both the state and federal tax credits. CHFA awarded about $25.8 million in 4 Percent Federal Tax Credits in Calendar Year 2020.

- 9 PERCENT FEDERAL TAX CREDIT—This credit is equivalent to approximately 70 percent of project owners' costs for the construction or rehabilitation of a affordable housing development. CHFA administers the credit at the state-level, with the federal government allocating a maximum annual aggregate award amount to each state. CHFA awarded about $16.3 million in annual credits during Calendar Year 2020. Because the total annual awards are capped and demand for the credit typically exceeds the cap, CHFA administers a competitive process to select the projects that will receive the credit.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURE?

We did not experience any data constraints that impacted our ability to evaluate the credit.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

We did not identify any policy considerations on this evaluation.