



Housing Tax Credit Program Qualified Contract Process Guide

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Disclaimer

Minnesota Housing is not obligated to undertake an investigation of the accuracy of the information submitted for qualified contract presentation. Minnesota Housing's review shall not constitute a warranty of the accuracy of the information, nor of the quality or marketability of the housing to be purchased, constructed or rehabilitated pursuant to the program. Developers, potential investors and interested parties should undertake their own independent evaluation of the feasibility, suitability and risk of the development.

If any information submitted by building owners to Minnesota Housing is later found to be incorrect in any material respect, it is the responsibility of the building owners to inform Minnesota Housing and to request a reexamination of the information. Minnesota Housing is not, and is not acting in the capacity of, a real estate agent or real estate broker. Its role is limited to implementing the Code requirements and facilitating the presentation of a qualified contract, as defined in the Code.

Interested parties should obtain advice from independent sources, including consultation with knowledgeable tax professionals and legal counsel.

This guide has not been reviewed or approved by the IRS and should not be relied upon for interpretation of federal income tax legislation or regulations.

Chapter 1 – Introduction

The Minnesota Legislature designated Minnesota Housing as the state’s primary apportionment Agency of Housing Tax Credits (HTC). Qualified local cities (Duluth, Rochester, St. Cloud, St. Paul, Minneapolis) and counties (Washington, Dakota) have also been designated by the Legislature as suballocators of HTC.

The initial compliance period for a development receiving an HTC allocation is 15 years. For HTC allocations made in 1990 and later, an extended use agreement required by Internal Revenue Code Section 42(h)(6) extends the compliance period up to a minimum of 15 additional years.

Section 42(h)(6)(E)(i)(II) of the Internal Revenue Code provides that the extended use period shall terminate if a housing credit agency is unable to present a qualified contract to a taxpayer who has requested such a contract.

The Internal Revenue Code (Code) contains some of the basic provisions for handling qualified contract requests. However, there are a number of important questions that have not been answered through federal regulation or other guidance. The purpose of this guide is to set forth the procedures to be followed by Minnesota Housing and the owners of Minnesota tax credit developments who are considering making a request for a qualified contract.

The provisions in the Code are subject to modification and clarification by the Internal Revenue Service (IRS). Minnesota Housing reserves the right to revise this Qualified Contract Process Guide. Compliance with the requirements of Section 42 is the responsibility of the owner of the building for which the credit is allowable.

Requesting a qualified contract is a difficult process that involves substantial time and energy on the part of the owner, the Management Company, and Minnesota Housing. It may not be the best alternative in every situation. Owners are also encouraged to consider other options. An important aspect to take into account when making this decision is to understand that after the compliance period, Minnesota Housing has adopted policies that reduce compliance and redefine some of the eligibility criteria (please refer to Chapter 9 of the Tax Credit Compliance Manual). As a result, compliance can be achieved much easier, but the spirit of the program is not compromised, and the housing will continue to serve the people for whom the program was intended. It is hoped that many owners would choose to continue the development under the existing restrictions through the extended use period. Alternatively, the owner may sell the development outside of the qualified contract process. In this instance, the purchaser would continue to operate the property with the HTC restrictions on the property under the reduced compliance requirements referenced above.

Chapter 2 – Qualified Contract

Section 42(h)(6)(E)(i)(II) of the Internal Revenue Code created a provision that housing credit agencies respond to the request for presentation of a qualified contract for tax credit developments with expiring compliance periods. The request for presentation of a qualified contract may occur after year 14 of the compliance period. The request for presentation of a qualified contract is a request that the housing credit agency find a buyer (who will continue to operate the property as a qualified low-income property) to purchase the property for a qualified contract price (QCP) pursuant to IRS regulations. If the housing credit agency is unable to find a buyer within one year, the extended use period is terminated.

Many owners have chosen to waive the right to request a qualified contract and have committed to 30 years or more of operation as low-income rental housing. Owners should review the respective Qualified Allocation Plan (QAP), development tax credit application, carryover agreement, and declaration of land use restrictive covenants to determine whether the development has waived the right to request a qualified contract prior to contacting Minnesota Housing.

A request for qualified contract may be submitted only once for each development. If an owner rejects an offer presented under the qualified contract or withdraws its request at any time after the notification letter and application materials have been received by Minnesota Housing, no other opportunity to request a qualified contract will be available for the development in question.

2.01 Qualified Contract Process

1. Owners who are contemplating requesting the presentation of a qualified contract should contact the Minnesota Housing tax credit compliance coordinator. Minnesota Housing will verify the development's eligibility.
2. If the property is determined eligible to request a qualified contract, Minnesota Housing will send a letter of acknowledgement to the owner along with:
 - a. A Qualified Contract Notification Letter
 - b. A Qualified Contract Process Guide and related application materials
 - c. Current year dates when requests for qualified contracts will not be accepted by Minnesota Housing (which will generally coincide with the Multifamily Request for Proposals (RFP) schedule).
3. The tax credit team will assign an underwriter to work with the owner to discuss issues pertinent to the development and possible alternatives to the qualified contract process. Owners should be prepared to present a thorough analysis of all current financing and related restrictions.
4. If a property is not eligible to request a qualified contract, Minnesota Housing will issue the owner a letter of denial.

2.02 Qualified Contract Notification Letter

The owner must submit the Qualified Contract Notification Letter along with all required application materials. These materials may be submitted any time after year 14 of the compliance period.

The notification letter contains statements from the owner that the owner will reasonably cooperate with Minnesota Housing and its agents with respect to the marketing of the property and acknowledges that the application materials may be shared with prospective purchasers, real estate brokers and other interested parties and that summary data may be posted on Minnesota Housing's website.

The owner will be asked to acknowledge in the notification letter that it has reviewed the due diligence materials used in the calculation of the qualified contract worksheets and that it is solely responsible for documents and information used in the calculation of The Qualified Contract price (QCP), using the procedure set forth in Section 42(h)(6)(F) of the Internal Revenue Code and CFR 1.42-18.

The owner will be asked in the notification letter to sign a statement verifying the accuracy of the assumptions used in the computation of the QCP to hold Minnesota Housing harmless with respect to the use of the development information and to do all things necessary to keep the property in compliance during the qualified contract process.

Additional information may be requested by Minnesota Housing, including but not limited to, additional rent rolls, income certifications and other Section 42 compliance records, records with respect to repair and maintenance of the development, operating expenses and debt service. Before information is shared with a prospective purchaser, the owner may require that Minnesota Housing and/or the prospective purchaser enter into a commercially reasonable form of nondisclosure agreement.

The owner may also be asked by Minnesota Housing to share, upon request, the documents and other information that were used to prepare the calculation of Form QC-1. The owner will be asked to allow Minnesota Housing, its agents, or prospective purchasers, upon reasonable prior written notice, to visit and inspect the development, including representative apartment units.

2.03 Application Materials

The owner must submit the Qualified Contract Notification Letter along with the following materials:

1. A thorough narrative description of the development, including all amenities, suitable for familiarizing prospective purchasers with the development
2. A description of all income, rental and other restrictions, if any, applicable to the operation of the development

3. A detailed set of photographs of the development, including the interior and exterior of representative apartment units and buildings and the development grounds. Digital photographs should be included so that they may easily be displayed on Minnesota Housing's website.
4. A copy of the most recent 12 months of operating statements for the development, which accurately advises a potential purchaser of the development's operating expenses, debt service, gross receipts, net cash flow and debt service coverage ratio. If available, also include three years of audited financial statements.
5. A current rent-roll
6. All years of tax returns for the ownership entity
7. A copy of the development's ownership agreement (typically an amended and restated Limited Partnership Agreement)
8. Disclosure of Rights of First Refusal, if any
9. If any portion of the land or improvements is leased, include copies of the leases
10. An independent third party appraisal of land and non-low-income portions of the property
11. A third party Physical Needs Assessment
12. A fully completed Form QC-1 Workbook including Worksheets A-E (see Section D below for a brief description of these worksheets) along with copies of the documents and other information used to support the QCP. This form must be completed and certified by a Certified Public Accountant including the valuation of the Non-Low Income Housing Tax Credit Property.
13. A copy of the most recent compliance report
14. Copy of the listing contract, if applicable
15. A qualified contract processing fee of \$5,000

2.04 Calculation of Qualified Contract Price Workbook

Form QC-1 contains accompanying worksheets A-E as described below:

Worksheet A: A summary of all outstanding secured indebtedness on the low-income building(s).

Worksheet B: Calculation of adjusted investor equity in the low-income building(s) by year.

Worksheet C: Other capital contributions made by the investor in the low-income portion of the building(s). These are contributions that are not included in other calculations, specifically in worksheets A and B.

Worksheet D: Cash distributions from the development by year. This calculation also includes a reporting of the cash held in reserve accounts and owner controlled accounts. The owner's non-cash distributions must also be included. These non-cash distributions will not be applied to reduce the QCP, but they must be reported.

Worksheet E: Fair market value of the non-low-income portion of the building(s) and land. This worksheet requires an appraisal, market study or other supporting documentation used to establish the market value of the non-low-income portions of the building(s) and land.

2.05 Review Process

1. Upon receipt of the owner's notification letter and application materials, Minnesota Housing will have 60 days to review the owners' packet of due diligence materials for completeness. Minnesota Housing will send the owner a letter acknowledging that all notification requirements have been met.
2. Once the QCP has been approved, Minnesota Housing will notify the owner that the one-year period to find a prospective buyer for the development has begun.
3. During the one-year period, Minnesota Housing will advertise the property in good faith. Minnesota Housing's process to identify an interested purchaser may include, but is not limited to:
 - a. Posting the property information on Minnesota Housing's website.
 - b. Creating an informational flyer and sending it to a pre-established mailing list. This list will include owners of tax credit properties; contacts at large management companies; other public funding agencies in the state; and local, state, and nationwide nonprofit and for-profit owners interested in preserving housing and tax credit investor contacts.
 - c. Presenting information on the property(s) to regional development and preservation groups, as well as at other stakeholder meetings.
 - d. Acting as a conduit for all requests of prospective purchasers by quickly responding to requests for additional information from the owner and forwarding that information immediately upon receipt.
4. Should the owner fail to maintain the required applicable fraction for each building during the one-year qualified contract period, Minnesota Housing reserves the right to rescind approval of the qualified contract application. Further, if the correction of non-compliance does not take place in a reasonable time frame, the qualified contract will cease to be an option.

2.06 Completion of Qualified Contract Process

It is owner's responsibility to immediately notify Minnesota Housing of all purchase offers made through the end of the last day of the one-year qualified contract period, including the date and terms, and whether an offer was accepted or rejected. This includes any transfer or purchase of

interest in the ownership entity. The qualified contract period is not assignable or transferrable and does not inure to successors in interest.

1. **Termination of the one-year qualified contract period.** The one-year qualified contract period will immediately terminate when a qualified contract as defined in IRC Section 42(h) has been presented to the owner. The owner may either accept or reject such offer; however, the property will remain subject to the Declaration of Land Use Restrictive Covenants for the remainder of the extended use period. No further request for a qualified contract may be made for such property.
2. **Qualified contract request withdrawn.** If an owner accepts an offer that is not a qualified contract, including an offer to transfer or purchase an interest in the ownership entity, Minnesota Housing will consider the qualified contract request withdrawn. The property will remain subject to the Declaration of Land Use Restrictive Covenants for the full term of the extended use period. No further request for a qualified contract may be made for such property.
3. **Expiration of the one-year qualified contract period.** After the end of the one-year qualified contract period, if a qualified contract has not been presented or the request is withdrawn, the owner will be notified by Minnesota Housing that the extended-use period has expired. Pursuant to IRC Section 42(h)(6)(E)(ii), existing low-income residents will continue to have the right to rent at the restricted rent levels and may not be evicted or have tenancy terminated for other than good cause for a period of three years following expiration of the extended use period. During this three-year period, the owner of the property is required to submit an annual report to Minnesota Housing in a form and manner determined by Minnesota Housing. The report will include, but is not limited to: all low-income households that occupied a unit at the expiration of the extended use period, the respective tenant-paid rent, utility allowance, and move-out date, if applicable, along with a certification that no low-income residents have been evicted or had tenancy terminated for other than good cause. The report and certification are due annually on February 15 or the following business day, if the 15th falls on Saturday, Sunday or a holiday. No monitoring fees will be due during this three year period and the property is not subject to inspections by Minnesota Housing.

When a property is sold, including a sale or change in ownership interest during the three-year period after the extended use period has expired, the owner must notify Minnesota Housing of the transfer by submitting the Notice of Intent to Transfer Ownership or Change Owner Name or Status (HTC 27) along with accompanying documentation.

Chapter 3 – Fees and Charges

The fee for processing a qualified contract request is \$5,000. The fee must be submitted at the time the Qualified Contract Notification Letter is presented to Minnesota Housing and is non-refundable. Any charges incurred for submission materials, appraisals, market studies and rent comparability studies will be paid by the owner.

Chapter 4 – Data Privacy

Government Data Practices Act Disclosure Statement: During the qualified contract process, certain development financial and tenant income information will be needed as verification. Minnesota Housing is required to handle data according to the Minnesota Government Data Practices Act (Chapter 13) and its own statute (462A.065). Minnesota Housing is also required to comply with M.S. 138.17, which governs the handling of government records. Minnesota Housing handles all sponsor financial data in a consistent manner that complies with these laws. The Agency is unable to return the data to project sponsors or agree to any conditions regarding use or handling of the data that aren't explicitly required by these laws.