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Memorandum

Attorney Work Product

To: Board of Directors
South Carolina Jobs-Economic Development Authority

From: Parker Poe Adams & Bernstein LLP

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Re: Affordable Housing in South Carolina

In recent years, the South Carolina Jobs-Economic Development Authority ("JEDA") has become a more frequent issuer of tax-exempt bonds to finance affordable housing developments. Additionally, affordable housing has become an increasingly frequent topic of policy discussion in the State of South Carolina ("South Carolina" or "State"). This memo provides:

1. An overview of what types of projects are included within the commonly used term of "affordable housing";
2. A discussion of some of the different financing methods available to owners and operators of affordable housing; and
3. A brief discussion of the current legislation and policies which have resulted in JEDA's increased participation in tax-exempt bond issuances for affordable housing.

I. What is Affordable Housing?

Commonly, the term "affordable housing" encompasses several different types of housing developments. Some people use the term "affordable housing" to mean "workforce housing." Others may use the term to describe projects financed with low-income housing tax credits. The term is also used to describe developments which are covered by Housing Assistance Payment contracts available under Section 8 of the U.S. Housing Act of 1937 ("HAP Contracts").

Ultimately, "affordable housing" includes any housing which is restricted in some way. It could be that the housing is restricted so that:

1. only individuals and families earning at or below a certain income threshold live at the development;
2. the rents that are charged to the tenants living at the development are capped at a certain percentage of the tenant's income; or
3. both the income levels of tenants that may live at the development and the rents charged to those tenants are restricted.

Whatever the restrictions or whatever the type of project, determining affordability is based on a standard called the "area median income" or "AMI" of the county or metropolitan statistical area in which an affordable housing development is located. The AMI of an area is calculated and published annually by the U.S. Department of Housing and Urban Development ("HUD"). HUD's AMI tables are also adjusted for family size. See the table below for an example of an AMI table for the Columbia, South Carolina HUD Metro FMR Area.

Columbia, SC HUD Metro FMR Area
Area Median Income (4-person family): $82,400

Family Size (number of persons)	1	2	3	4	5	6
30% of AMI	$16,950	$19,350	$21,780	$24,180	$ 26,130	$ 28,050
50% of AMI	$28,250	$32,250	$36,300	$40,300	$ 43,550	$ 46,750
60% of AMI	$33,900	$38,700	$43,560	$48,360	$ 52,260	$ 56,100
80% of AMI	$42,500	$51,600	$58,080	$64,480	$ 69,680	$ 74,800
120% of AMI	$67,800	$77,400	$87,120	$96,720	$104,520	$112,200

Determining the percentage of the area median income that individuals or families occupying the project earn will determine the type of affordable housing project. For example, "workforce housing" serves individuals and families that earn between 80% and 120% of the area median income for an area. Therefore, using the numbers from the table above, a workforce housing development in Columbia, South Carolina may have individuals and families residing there that earn between $42,500 (an individual earning 80% of AMI) and $112,200 (a family of six earning 120% of AMI).

Projects financed with low-income housing tax credits or tax-exempt bonds (discussed later in this memo), most frequently serve individuals and families which earn 80% of AMI or less, with additional specific reservations for individuals and families earning either 50% or 60% of the AMI. Projects which are covered by HAP contracts frequently serve individuals and families which earn below 50% of the AMI.

In order to ensure that affordable housing developments serve the intended populations, restrictive covenants are often executed and recorded in the real property records of the county in which the affordable housing project is located. Sometimes – like when an affordable housing project is bond-financed – the covenants are executed with the issuer of and trustee for the bonds. Other times, the covenants may be self-imposed by the owner and operator of an affordable housing development.

II. Methods of Financing Affordable Housing Projects

A. Tax-Exempt Bonds

Affordable housing may be financed with tax-exempt bonds. Tax-exempt bonds that are issued to finance affordable housing are either bonds issued under Section 142(d) of the Internal Revenue Code or under Section 145 of the Internal Revenue Code (which are more commonly known as "qualified 501(c)(3) bonds").

a. Section 142(d) Bonds

Tax-exempt bonds issued under Section 142 of the Internal Revenue Code ("Section 142(d)") are conduit bonds and are issued by conduit issuers – like JEDA, the South Carolina Housing Finance and Development Authority ("SC Housing"), or local housing authorities. The proceeds of the bonds are loaned by the issuers to private entities which acquire, construct, develop, rehabilitate or improve the affordable housing development. The bonds are repaid solely from the revenues generated by the affordable housing development. The credit and resources of the conduit issuer are not pledged or available for the repayment of the bonds.

Bonds to be issued for affordable housing projects under Section 142(d) require an allocation of the state ceiling of volume cap ("State Ceiling")[1] in an amount equal to the amount of tax-exempt bonds. In South Carolina, the State Fiscal Accountability Authority ("SFAA") controls the allocation of the State Ceiling. The SFAA

[1] The amount of State Ceiling allocated to projects in South Carolina is determined annually and is based on the population of the State. This year, the amount of the State Ceiling was approximately $577 million. The State Ceiling must be shared by all tax-exempt bonds issued under Section 142 of the Internal Revenue Code– not just tax-exempt bonds for affordable housing projects under Section 142(d).

determines the amount and time the State Ceiling is available for tax-exempt bonds issued for affordable housing projects.[2]

As noted above, affordable housing projects which are financed with tax-exempt bonds issued under Section 142(d) are required to place restrictions on the project to ensure that the appropriate population resides at the development. The restrictions must require that at least (a) 20 percent or more of the residential units are occupied by individuals whose income is 50 percent or less of AMI, or (b) 40 percent or more of the residential units are occupied by individuals whose income is 60 percent or less of AMI.

Bonds issued under Section 142(d) by JEDA are typically used to finance affordable senior and assisted living facilities that do not also use low-income housing tax credits as a source of financing. JEDA has not historically issued tax-exempt bonds under Section 142(d) for affordable housing apartment facilities because these projects are more traditionally financed by SC Housing and also utilize low-income housing tax credits, which fall within SC Housing's scope (as discussed later in this memo).

b. Qualified 501(c)(3) Bonds

Like tax-exempt bonds issued under Section 142(d), qualified 501(c)(3) bonds, are conduit bonds. However, as the name suggests, qualified 501(c)(3) bonds may only be issued for projects 100% owned by charitable organizations that are exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. JEDA may issue qualified 501(c)(3) bonds for affordable housing projects owned by charitable organizations that have the exempt purpose of providing affordable housing.

Unlike tax-exempt bonds issued for affordable housing projects under Section 142(d), qualified 501(c)(3) bonds do not require an allocation of the State Ceiling before the bonds are issued.

Certain affordable housing projects which are financed utilizing qualified 501(c)(3) bonds must also put restrictions in place in order to ensure that the project is serving the appropriate population. Most often the restrictions are based on the Internal Revenue Service's Revenue Procedure 96-32 which establishes the "safe-harbor" criteria that an organization providing affordable housing must meet to qualify as a charitable organization under section 501(c)(3) of the Internal Revenue Code.[3] These criteria are:

- At least 75% of the units are occupied by individuals or families earning 80% of the AMI or less; AND of those 75% at least,
    - 20% of the units are occupied by individuals or families earning 50% of the AMI or less; OR
    - 40% of the units are occupied by individuals or families earning 60% of the AMI or less.

JEDA regularly finances affordable housing projects using qualified 501(c)(3) bonds because projects financed using qualified 501(c)(3) bonds do not also use low-income housing tax credits as a source of financing. The affordable housing projects JEDA finances through the issuance of qualified 501(c)(3) bonds include both senior and assisted living facilities and traditional multifamily apartment facilities.

B. Low Income Housing Tax Credits

In addition to tax-exempt bond financing as described above, affordable housing projects are also financed using state and federal low-income housing tax credits ("LIHTCs"). LIHTCs are used to finance projects through

[2] The SFAA is charged with allocating the State Ceiling among the different categories of tax-exempt bonds that may be issued under Section 142. As of the date of this memo, the SFAA has not allocated any of the State Ceiling for affordable housing projects. Additionally, the SFAA may limit the time during which an allocation of the State Ceiling may be available for a project. If the tax-exempt bonds for a project are not issued within a certain period of time, the allocation of the State Ceiling for that project may be lost.

[3] The "safe harbor" criteria in Revenue Procedure 96-32 are also the basis of a state property tax exemption available to charitable organizations that own and operate affordable housing in the State. This is another reason why these restrictions are the most common restrictions placed on affordable housing projects financed through qualified 501(c)(3) bonds.

equity investments in the partnership or limited liability company owning the affordable housing development. The equity investment represents the purchase of the LIHTCs (at a discount) by institutions, funds, or individuals that desire to use the LIHTCs generated by the affordable housing projects to offset their federal income tax liability. The amount of LIHTCs generated by a project depends on the cost of the project and the number of units that are set aside for affordable housing.

There are two types of LIHTCs available for affordable housing projects – the 9% credit and the 4% credit. The 9% credit is not typically paired with any debt financing. However, to utilize the 4% credit, at least 50% of the costs of acquiring, constructing or rehabilitating an affordable housing project must be financed using tax-exempt bonds issued pursuant to Section 142(d).

As mentioned above, tax-exempt bonds issued under Section 142(d) must receive an allocation of the State Ceiling prior to issuance. This includes tax-exempt bonds issued in connection with the 4% credit.

SC Housing is the State's only LIHTC allocating agency. Therefore, as noted above, JEDA has not historically issued tax-exempt bonds for projects that also utilize LIHTCs because, as the allocating agency, SC Housing has been best suited for financing transactions involving LIHTCs. However, JEDA has the statutory authority to issue bonds under Section 142(d) and may issue tax-exempt bonds for projects that also utilize LIHTCs if JEDA desires or is directed to do so.

III. Increase in Bond Issuances for Affordable Housing by JEDA

Requests to JEDA to issue bonds for affordable housing projects have increased in recent years due, in part, to several statutory and programmatic changes in South Carolina.

In 2020, in order to decrease the deficit of affordable housing available in the State, the South Carolina legislature adopted a new state LIHTC, which was a dollar for dollar match to the federal LIHTC awarded to an affordable housing project. This provided an increased source of equity available to developers of affordable housing projects, and made affordable housing a more financially feasible and attractive endeavor in South Carolina. Developers and applications for allocations of LIHTCs flooded the South Carolina market.

In 2021, the General Assembly became concerned that the state LIHTC was being utilized more than anticipated. A moratorium was instituted on all affordable housing projects that required allocations of State Ceiling until the General Assembly could review the state LIHTC program.

This review led to the enactment of the Act 202 in 2022 ("Act 202"), which provided for an overhaul of both the state LIHTC program and the procedure for the allocation of State Ceiling. Act 202 placed an annual cap on the amount of the state LIHTCs that may be awarded to affordable housing projects and the SFAA was given the power to create an annual plan which allocated the State Ceiling to different types of projects financed with tax-exempt bonds under Section 142 (which in the current year includes no allocation of the State Ceiling to affordable housing projects). Additionally, Act 202 inserted the South Carolina Joint Bond Review Committee as an additional reviewer of the State Ceiling allocation plan and SC Housing's administration of the LIHTCs.

The additional restrictions and procedural hurdles provided by Act 202 (together with some agency turnover SC Housing has experienced since 2020) have made financing affordable housing with LIHTCs and through the issuance of tax-exempt bonds under Section 142(d) uncertain and costly.

These changes have caused developers of affordable housing to seek alternate methods of financing their projects. JEDA provides that alternative as an issuer of qualified 501(c)(3) bonds. Because qualified 501(c)(3) bonds do not require State Ceiling or LIHTCs, qualifying nonprofit owners can minimize the uncertainty and increased costs caused by the current state of the LIHTC program and State Ceiling allocation process by utilizing JEDA as an issuer. As affordable housing is still very much needed in the State, developers have increasingly applied to JEDA to finance their affordable housing projects.