MULTIFAMILY TAX-EXEMPT BONDS FEDERAL TAX REGULATIONS

Residential Rental Projects
The Internal Revenue Service has published regulations ("the Regulations") which set forth certain limitations on the use of municipal bonds to finance residential rental projects to be owned by for-profit persons. A residential rental project is defined as a building or structure or several proximate and interrelated buildings or structures. Under the Regulations, a building or structure means a discrete edifice or other man-made construction consisting of an independent foundation, outer walls, and a roof. While single townhouses are not considered buildings if the foundations and outer walls and roofs are not independent, detached townhouses and row houses would be considered buildings. Thus, scattered-site housing is considered a building or structure, as long as each single-unit facility meets the other requirements set forth below.

A "unit," which must be contained in a "building or structure," means any accommodation containing separate and complete facilities for living, eating, cooking, and sanitation. Thus, an apartment containing a living area, sleeping area, bathing and sanitation facilities, and cooking facilities equipped with a cooking range or microwave, refrigerator and sink, all of which are separate and distinct from the other apartments, would constitute a "unit."

Transient Housing
Hotels, motels, dormitories, fraternity and sorority houses, rooming houses, hospitals, nursing homes, assisted living facilities with continual care, sanitariums, rest homes, and trailer courts and parks used on a transient basis and not as permanent residences, are not considered residential rental projects for federal tax law purposes.

Public Use Test
The units of a residential rental project must be both legally and practically available to the members of the general public. Thus, for example, if an apartment building is constructed next to a factory and the factory employees are given a preference in tenant selection, the facility would not be considered available for use by the general public.

Single Project; Interrelated Buildings
Multiple buildings and structures that are proximate to one another that have similarly-constructed units are considered part of the same project if they are owned for federal tax purposes by the same person and if the buildings are financed pursuant to a common plan. A common plan of financing will be considered to exist if all the buildings are financed by the same bond issue.

Facilities that are functionally-related and subordinate to residential rental projects are deemed to be part of the residential rental projects and thus financeable. Facilities are deemed functionally-related and subordinate if they are reasonably required for the project, such as heating and cooking equipment, trash disposal equipment, or units for residential managers and maintenance personnel. Facilities that are functionally-related and subordinate to residential rental projects also include facilities that are to be used by the tenants as part of the residential rental project, such as swimming pools, other recreational facilities and parking areas. These types of facilities must be commensurate in character and size with the residential rental project.

Cooperatives
Under present law, cooperatives are normally not considered residential rental projects because one or more units typically are occupied by shareholders who own stock in the cooperative corporation. Such units are considered owner-occupied units.

Continuous Rental Requirement

Once a unit in a residential rental project is available for occupancy, each such unit must be rented or available for rental on a continuous basis during the "qualified project period." The qualified project period means a period that begins on the first date on which at least 10% of the units of the project are first occupied. The qualified project period ends on the latest of (1) the date that is 15 years after the date on which at least 50% of the units of the project are first occupied, (2) the date on which any assistance provided with respect to the project under Section 8 of the United States Housing Act of 1937 terminates, or (3) the date on which no tax-exempt bond issued with respect to the project is outstanding.

Federal and Nebraska Set-Asides

In addition to the requirement that the project remain rental property, a specified minimum percentage of the units in each project must be occupied by individuals or families of low income continuously during the qualified project period ("the federal set-aside requirement"). The federal set-aside requirement will be met if at least 20% of the rental units in the project are occupied by individuals and families whose income is 50% or less of the gross area median income (AMI) or if at least 40% of the units are occupied by individuals and families whose income is 60% or less of AMI. Once 10% of the units in the project are occupied, 20% (or 40% under the alternative federal set-aside requirement) of the units must be occupied by individuals or families of low income. Furthermore, the ratio of low income tenants to other tenants (20% @ 50% or 40% @ 60%) must be maintained during the "rent-up" period.

The developer must direct NIFA to irrevocably elect, prior to the issuance of the bonds, the minimum federal set-aside requirement to be used.

Pursuant to Section 142 (d)(2) of the Internal Revenue Code and the regulations promulgated thereunder, individual and family incomes and area median incomes are determined in a manner consistent with Section 8 of the 1937 Housing Act. Median gross incomes for Metropolitan Statistical Areas (MSA's) and counties outside such areas are published annually by the United States Department of Housing and Urban Development (HUD) and are normally readily obtainable from the HUD area Economist. Area median income is required to be adjusted for family size pursuant to Section 8 of the 1937 Act.

The determination of whether a tenant satisfies the income limits must be made at least annually based on the current income of the resident and the current area median income. Therefore, if a tenant's income changes, a tenant's family size changes, or if the area median income decreases, the set-aside requirement may not be satisfied. A tenant is deemed to be a low-income person notwithstanding an increase in income of up to 140% of the maximum qualifying income, adjusted for family size. If the tenant's income increases to a greater extent, the next available comparably-sized or smaller unit, must be rented to a low income person.

The occupants of a unit will not be considered persons of low income if all the occupants are students (as defined in Section 151(e)(4) of the Internal Revenue Code) and none of the students are entitled to file a joint return (for married persons only) under Section 6013 of the Internal Revenue Code. Section 151(e)(4) generally defines student as any person who attends a college or similar institution for at least five months in a year on a full-time basis.

All of the remaining units in the project must be rented to persons of low- and moderate-income as defined by NIFA. Low- and moderate-income means a person or family whose adjusted gross income (when the incomes of all tenants who are parties to the rental agreement for a rental unit in a project are aggregated) does not exceed 150% of the median area income as annually determined by the United States Department of Housing and Urban Development.

Additionally, projects financed by NIFA pursuant to the Multifamily Financing program must participate in and meet the requirements of the Low Income Housing Tax Credit (LIHTC) program.

Rent Limits/Rent-Skewed Projects
Rent restrictions as set forth in the LIHTC program will apply to all projects financed through the Multifamily Financing program.

Developers may also elect to satisfy an alternative federal set-aside requirement for rent-skewed projects. In order for such projects to meet the federal set-aside requirements, at least 15% of the low income units in the project must be occupied by tenants whose income is 40% or less of AMI. The gross rent for each low income unit cannot exceed one-third of the average rent for units of comparable size that are not occupied by low income tenants. An existing tenant will continue to satisfy the low income requirement should the tenant's income increase up to, but not beyond, 170% of AMI adjusted for family size; however, if it increases above 170%, the next available low income unit must be rented to a tenant whose income is 40% or less of AMI, adjusted for family size.

The gross rent charged to tenants in such units must not exceed 30% of the applicable income limitation for the tenants. For example, in an area with a median gross income of $30,300, the maximum monthly rent that could be charged for a unit rented to a family of four would be $303 [($30,300 × .4 × .3) ÷12]. "Gross rent" for this purpose includes payments made directly by the tenant (not rental payments made for the tenant under a program such as Section 8 of the 1937 Act), and the cost of utilities (other than a telephone) paid from the tenant's rent. If the tenant pays utilities directly, the maximum rent that the tenant may pay is to be reduced by a utility allowance determined by the HUD Secretary.

Annual Certification
The owner of the project must certify annually that the requirements of Section 142(d) of the Code, including the federal set-aside requirement, are satisfied. Failure to file the certification will subject the owner of the project to a penalty.

Noncompliance
If a project fails to comply with the rental and low income federal set-aside requirements anytime during the required periods described above (which may sometimes be beyond the maturity of the tax-exempt obligations issued to finance the project), the project will be treated as never having been a project meeting the requirements of Section 142(d), unless the noncompliance is corrected within a reasonable period. If the noncompliance is not corrected within a reasonable period, the project will be deemed to never having complied with the requirements and the bond issue would be retroactively taxable.

The rental and low-income requirements described above will no longer apply to a project (and thus will not cause the related bonds to become retroactively taxable) if the noncompliance is involuntarily caused by fire, seizure, requisition, condemnation, foreclosure, transfer of title by deed in lieu of foreclosure, change in a federal law or an action of a federal agency after the date of issue that prevents an issuer from enforcing the requirements, or a similar event. Within a reasonable period after such an event, either the tax-exempt obligations used to finance the project must be redeemed, or the amounts received consequently of such events must be used to provide a project that does meet the requirements. However, this exception (to meeting the rental and federal low-income requirements) will not apply to a project subject to foreclosure, transfer of title by deed in lieu of foreclosure, or similar event, if the developer on the original defaulted mortgage (or a related person) obtains an ownership interest in the project for tax purposes during the period with respect to which the rental and federal low-income requirements originally applied. Thus, if the developer purchases the project at a sheriff's sale in which such developer's original mortgage is being foreclosed, the rental and federal low-income requirements would not be terminated, and any bonds issued to finance the project would still be retroactively taxable unless the rental or federal low-income requirements continue to be satisfied.

Deed Restriction and Monitoring Duties
To ensure compliance with the various federal tax and state law restrictions, NIFA will require that a deed restriction or a covenant running with the land be filed with the register of deeds so that all subsequent

purchasers of the project must comply with the requirements. The developer is responsible for qualifying tenants and determining, pursuant to the procedures set up by NIFA, that all tenants meet the income restrictions. Compliance by the developer is monitored by NIFA and any lending institution participating in the financing.

Financing of Land and Existing Facilities

No more than 25% of the net proceeds of the bonds may be used to acquire land or an interest in the land.

Pursuant to federal tax laws, none of the proceeds of the bonds may be used to finance the acquisition of existing buildings or other facilities (that is, buildings or facilities already placed in use) unless a minimum amount of rehabilitation is performed to such facilities within the two-year period following the later of the date of the acquisition of the facilities or the date of issuance of the bonds. If the acquisition is of a building and the furniture, fixtures, and equipment therein, the rehabilitation work must equal or exceed an amount equal to 15% of the portion of the cost of acquisition that the bonds financed. However, this 15% rehabilitation requirement is not applied to bond proceeds used to acquire land or an interest in land. Thus, for example, if the acquisition of an apartment complex (including the furniture, fixtures, and equipment therein) costs $10 million, but only $9 million is financed with bond proceeds, and $1 million of the $9 million is used to purchase the land, then 15% of $8 million (or $1.2 million) must be expended for rehabilitation of the building during the next two years.

A rehabilitation expenditure does not include the cost of enlarging or expanding a building or expenditures made by a lessee if the lease term is less than 15 years. A rehabilitation expenditure includes any amount properly chargeable to the capital account of the taxpayer for acquiring the building or additions or improvements to the property. If equipment was used in an integrated operation contained in a building, expenditures to rebuild or replace the equipment with substantially similar equipment qualify as rehabilitation expenditures. Rehabilitation expenditures include expenditures for fixtures such as stoves, refrigerators, and carpeting. The rehabilitation expenses must be incurred by the person acquiring the building. The rehabilitation expenditures may be financed with bond proceeds.

If the bonds finance the acquisition of more than one building in the same project, the acquisition expenditures may relate to any of the buildings in the project. In other words, it is not necessary, for tax-exempt bond purposes, to rehabilitate each building as long as the total rehabilitation expenditures equal or exceed 15% of the entire project acquisition cost financed with bond proceeds. See a description of the LIHTC program for the rehabilitation requirements applicable to tax credit projects.

Nonresidential Building Portions

Bonds may be issued to finance part of a building used as residential rental property, though the balance of the building (not bond-financed) does not qualify as residential rental property (e.g., retail or office space).