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LOW-INCOME HOUSING TAX CREDIT

Actions Needed to Strengthen Oversight and Accountability

Statement of Daniel Garcia-Diaz, Director, Financial Markets and Community Investment

GAO-17-784T

GAO Highlights

Highlights of GAO-17-784T, a testimony before the Committee on Finance, U.S. Senate

Why GAO Did This Study

The LIHTC program, established under the Tax Reform Act of 1986, is the largest source of federal assistance for developing affordable rental housing and will represent an estimated $8.5 billion in forgone revenue in 2017. LIHTC encourages private-equity investment in low-income rental housing through tax credits. The program is administered by IRS and allocating agencies, which are typically state or local housing finance agencies established to meet affordable housing needs of their jurisdictions. Responsibilities of allocating agencies (in Section 42 of the Internal Revenue Code and regulations of the Department of the Treasury) encompass awarding credits, assessing the reasonableness of project costs, and monitoring projects.

In this testimony, GAO discusses (1) how allocating agencies implement federal requirements for awarding LIHTCs, assess reasonableness of property costs, and monitor properties' ongoing compliance; and (2) IRS oversight of the LIHTC program. This statement is based primarily on three reports GAO issued in July 2015 (GAO-15-330), May 2016 (GAO-16-360), and February 2017 (GAO-17-285R). GAO also updated the status of recommendations made in these reports by reviewing new or revised IRS policies, procedures, and reports and interviewing IRS officials.

View GAO-17-784T. For more information, contact Daniel Garcia-Diaz at (202) 512-8678 or garciadiazd@gao.gov.

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What GAO Found

In its May 2016 report on the Low-Income Housing Tax Credit (LIHTC) program of the Internal Revenue Service (IRS), GAO found that state and local housing finance agencies (allocating agencies) implemented requirements for allocating credits, reviewing costs, and monitoring projects in varying ways. Moreover, some allocating agencies' day-to-day practices to administer LIHTCs also raised concerns. For example,

- qualified allocation plans (developed by 58 allocating agencies) that GAO analyzed did not always mention all selection criteria and preferences that Section 42 of the Internal Revenue Code requires; and
- allocating agencies could increase (boost) the eligible basis used to determine allocation amounts for certain buildings if needed for financial feasibility. However, they were not required to document the justification for the increases. The criteria used to award boosts varied, with some allocating agencies allowing boosts for specific types of projects and one allowing boosts for all projects in its state.

In its 2015 and 2016 reports, GAO found IRS oversight of the LIHTC program was minimal. Additionally, IRS collected little data on or performed limited analysis of compliance in the program. Specifically, GAO found that

- Since 1986, IRS conducted seven audits of the 58 allocating agencies we reviewed. Reasons for the minimal oversight may include LIHTC being viewed as a peripheral program in IRS in terms of its mission and priorities for resources and staffing.
- IRS had not reviewed the criteria allocating agencies used to award discretionary basis "boosts," which raised concerns about oversubsidizing projects (and reducing the number of projects funded).
- IRS guidance to allocating agencies on reporting noncompliance was conflicting. As a result, allocating agencies' reporting of property noncompliance was inconsistent.
- IRS had not participated in and leveraged the work of the physical inspection initiative of the Rental Policy Working Group—established to better align the operations of federal rental assistance programs—to augment its databases with physical inspection data on LIHTC properties that the Department of Housing and Urban Development (HUD) maintains.

In its prior reports, GAO made a total of four recommendations to IRS. As of July 2017, IRS had implemented one recommendation to include relevant IRS staff in the working group. IRS has not implemented the remaining three recommendations, including improving the data quality of its LIHTC database, clarifying guidance to agencies on reporting noncompliance, and evaluating how the information HUD collects could be used for identifying noncompliance issues. In addition, because of the limited oversight of LIHTC, in its 2015 report GAO asked that Congress consider designating certain oversight responsibilities to HUD because the agency has experience working with allocating agencies and has processes in place to oversee the agencies. As of July 2017, Congress had not enacted legislation to give HUD an oversight role for LIHTC.

Chairman Hatch, Ranking Member Wyden, and Members of the Committee:

I am pleased to be here today to discuss our work on the Low-Income Housing Tax Credit (LIHTC) program administered by the Internal Revenue Service (IRS) and allocating agencies, which typically are state or local authorities established to meet the affordable housing needs of the residents of their states. LIHTC, established under the Tax Reform Act of 1986, is the largest source of federal assistance for developing affordable rental housing. Each state receives an annual allocation of LIHTCs, determined by statutory formula. Allocating agencies then competitively award the tax credits to owners of qualified rental housing projects that reserve all or a portion of their units for low-income tenants. In 2017, LIHTC will represent an estimated $8.5 billion in forgone revenue to the federal government.[1]

My statement today will focus on (1) how allocating agencies implement federal requirements for awarding LIHTCs, assess reasonableness of property costs, and monitor properties' ongoing compliance; and (2) IRS's oversight of the LIHTC program. This statement is based primarily on three reports we issued in July 2015, May 2016, and February 2017.[2] To conduct the work for the three reports, among other methodologies, we reviewed IRS regulations and guidance, including how allocating agencies and taxpayers are selected for review. We also conducted a structured analysis of 58 Qualified Allocation Plans (QAP), which outline processes for awarding LIHTCs and compliance monitoring responsibilities.[3] We selected a nonprobability, nongeneralizable sample of nine allocating agencies for site visits, and during these visits, we reviewed files for randomly selected housing developments to determine how each agency addressed federal requirements for awarding LIHTCs, assessed the reasonableness of development costs, and monitored properties' compliance with program requirements. We also interviewed

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[1]Joint Committee on Taxation, *Estimates of Federal Tax Expenditures for Fiscal Years 2016-2020* (Washington, D.C.: Jan. 30, 2017).

[2]See GAO, *Low-Income Housing Tax Credit: The Role of Syndicators*, GAO-17-285R (Washington, D.C: Feb 16, 2017); *Low-Income Housing Tax Credit: Some Agency Practices Raise Concerns and IRS Could Improve Noncompliance Reporting and Data Collection*, GAO-16-360 (Washington, D.C.: May 11, 2016); and *Low-Income Housing Tax Credit: Joint IRS-HUD Administration Could Help Address Weaknesses in Oversight*, GAO-15-330 (Washington, D.C.: July 15, 2015).

[3]Our review examined plans from 2013 or the most recent QAP available.

officials from IRS, the Department of the Treasury (Treasury), the Department of Housing and Urban Development (HUD), the National Council of State Housing Agencies (NCSHA), and selected allocating agencies. For our 2017 report, we gathered data for 32 syndicators in total—31 through a no-cost contract with CohnReznick, a national accounting firm—and one survey response directly from a syndicator.[4] More detailed information on our scope and methodology can be found in each of the reports cited throughout this testimony. To update the status of recommendations from our 2015 and 2016 reports, we reviewed new or revised IRS policies, procedures, and reports and interviewed IRS officials.

We performed the work on which this statement is based in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Overview of IRS Administration of LIHTC Program

IRS administration of the LIHTC program involves overseeing compliance on the part of allocating agencies and taxpayers and developing and publishing regulations and guidance. IRS is responsible for reviewing LIHTC information on three IRS forms that are the basis of LIHTC program reporting and then determining whether program requirements have been met. Taxpayer noncompliance with LIHTC requirements may result in IRS denying claims for the credit in the current year or recapturing—taking back—credits claimed in prior years.

Published guidance may include revenue rulings and procedures, notices, and announcements. Other guidance for the program includes an Audit Technique Guide for Completing Form 8823 that includes specific instructions for allocating agencies, including when site visits and file reviews are to be performed, and guidelines for determining

[4]CohnReznick completed a survey to capture requested data on behalf of the 31 syndicators for which it had information. It then sent the completed surveys to the syndicators to review and, if necessary, correct before transmitting the data to us.

noncompliance in areas such as health and safety standards, rent ceilings, income limits, and tenant qualifications.

Role of Allocating Agencies

State and local allocating agencies are responsible for day-to-day administration of the LIHTC program based on Section 42 of the Internal Revenue Code and Treasury regulations. More specifically, allocating agencies are responsible for

Awarding tax credits. Each state receives an annual allocation of LIHTCs, determined by statutory formula. Allocating agencies then competitively award the tax credits to owners of qualified rental housing projects that reserve all or a portion of their units for low-income tenants, consistent with the agencies' QAPs.[5] Developers typically attempt to obtain funding for their projects by attracting third-party investors willing to contribute equity to the projects; the project investors then can claim the tax credits.

Monitoring costs. Section 42 states that allocating agencies must consider the reasonableness of costs and their uses for proposed LIHTC projects, allows for agency discretion in making this determination, and also states that credits allocated to a project may not exceed the amount necessary to assure its feasibility and its viability as a low-income housing project. However, Section 42 does not provide a definition or offer guidance on determining how to calculate these amounts.

Monitoring compliance. After credits are awarded, Treasury regulations state that allocating agencies must conduct regular site visits to physically inspect units and review tenant files for eligibility information. The agencies also have reporting and notification requirements. For example, allocating agencies must notify IRS of any noncompliance found during inspections and ensure that owners of LIHTC properties annually certify they met certain requirements for the preceding 12-month period.

[5]An allocating agency develops the QAP and receives approval of the plan by the governmental unit of which the allocating agency is a part. The agency then evaluates the proposed projects against the approved QAP. The QAP also must be developed in accordance with Section 42 requirements for such plans. Section 42 requires that QAPs give preference to certain projects; specifically, those that (1) serve the lowest-income tenants, (2) are obligated to serve qualified tenants for the longest periods, and (3) are located in qualified census tracts and the development of which contributes to a concerted community revitalization plan.

Role of Investors and Syndicators

Developers of awarded projects typically attempt to obtain funding for their projects by attracting third-parties willing to invest in the project in exchange for the ability to claim tax credits. The developer sells an ownership interest in the project to one or more investors, or in many instances, to a fund managed by a syndicator who acts as an intermediary between the developer and investors.

Investors and syndicators play several roles in the LIHTC market. For example, syndicators help initially connect investors and developers and oversee acquisition of projects. Once a project is acquired, syndicators perform ongoing monitoring and asset management to help ensure the project complies with LIHTC requirements and is financially sound. Syndicators attempt to identify potential problems and intercede if necessary, such as replacing under- or nonperforming general partners, and may use their own reserves to help resolve problems. In exchange for these services, syndicators typically are compensated through an initial acquisition fee—usually a percentage of the gross equity raised—and an annual asset management fee.

Syndicators that we surveyed for our 2017 report were nonprofit or for-profit entities, generally had multistate operations, and averaged more than 20 years of experience with the LIHTC program.[6] Of the 32 syndicators we surveyed, the syndicators collectively had raised more than $100 billion in LIHTC equity since 1986, helping to fund more than 20,000 properties and about 1.4 million units placed-in-service through 2014. Projects for which these syndicators raised equity in 2005–2014 represented an estimated 75 percent of all LIHTC properties placed-in-service in that period.[7]

[6]For more information on the role of syndicators and their characteristics, see GAO-17-285R.

[7]We collected data through calendar year 2014 because that was the most current available at the time of our 2017 report.

Selected Allocating Agencies Implemented Differing Practices for Key LIHTC Requirements

As we reported in 2016, allocating agencies implemented requirements for QAPs in varying ways and had processes in place to meet requirements for credit awards. Allocating agencies also had procedures to assess costs, but determined award amounts for projects differently, used various cost limits and benchmarks to determine reasonableness of costs, and used widely varying criteria for basis boosts. Agencies also had processes in place to monitor compliance. However, some of these practices raised concerns.

Agencies Implemented Requirements for Allocation Plans and Award Credits in Varying Ways

In our 2016 report, we generally found that allocating agencies implemented requirements for QAPs in varying ways and had processes in place to meet requirements for awarding the tax credit.

- Based on our 2016 review of 58 QAPs and our nine site visits, we found the QAPs did not always contain, address, or mention preferences and selection criteria required in Section 42. Rather, some allocating agencies incorporated the information into other LIHTC program documents, or implemented the requirements in practice.
- While Section 42 specifies some selection criteria (such as project location or tenant populations with special housing needs), it also more broadly states that a QAP set forth selection criteria “appropriate to local conditions.” As a result, allocating agencies have the flexibility to create their own methods and rating systems for evaluating applicants. We found that nearly all the allocating agencies that we reviewed used points or a threshold system for evaluating applicants. They used criteria such as qualifications of the development team, cost effectiveness, or leveraging of funds from other federal or state programs.
- According to Section 42, allocating agencies must notify the chief executive officer (or the equivalent) of the local jurisdiction in which the project is to be located. However, some agencies imposed an additional requirement of letters of support from local officials. Specifically, as of 2013, we found that of the 58 agencies in our review,12 agencies noted that their review or approval of applications was contingent on letters of support, and another 10 agencies awarded points for letters of local support. HUD officials have cited fair housing concerns in relation to any preferences or requirements for local approval or support because of the discriminatory influence these factors could have on where affordable housing is built. In

December 2016, IRS issued a revenue ruling that clarified that Section 42 neither requires nor encourages allocating agencies to reject all proposals that do not obtain the approval of the locality where the project developer proposes to place the project.[8]

Allocating agencies we visited for our 2016 report had processes in place to meet other Section 42 requirements, including awarding credit to nonprofits and long-term affordability of projects. Allocating agencies must allocate at least 10 percent of the state housing credit ceiling to projects involving qualified nonprofit organizations. All nine allocating agencies we visited had a set-aside of at least 10 percent of credits to be awarded to projects involving nonprofits. Section 42 also requires allocating agencies to execute an extended low-income housing commitment of at least 30 years before a building can receive credits. For example, one allocating agency we visited required developers to sign agreements for longer extended-use periods, while some agencies awarded points to applications whose developers elect longer periods.

Agencies We Reviewed Had Procedures to Assess Costs and Used Widely Varying Criteria for Basis Boosts

Allocating agencies we reviewed for our 2016 report had procedures to assess costs, but determined award amounts for projects differently and used various cost limits and benchmarks to determine reasonableness of costs. All nine allocating agencies we visited required applicants to submit detailed cost and funding estimates, an explanation of sources and uses, and expected revenues as part of their applications. These costs were then evaluated to determine a project's eligible basis (total allowable costs associated with depreciable costs in the project), which in turn

[8]IRS, Rev. Rul. 2016–29.

determined the qualified basis and ultimately the amount of tax credits to be awarded.[9]

Reasonableness of costs. We found that allocating agencies had different ways for determining the reasonableness of project costs. Based on our analysis of 58 QAPs and our nine site visits, agencies had established various limits against which to evaluate the reasonableness of submitted costs, such as applying limits on development costs, total credit awards, developer fees, and builder's fees.[10] Section 42 does not provide a definition of reasonableness of costs, giving allocating agencies discretion on how best to determine what costs are appropriate for their respective localities.

Discretionary basis boosts. Allocating agencies commonly "boosted" the basis for projects, but used widely varying criteria for doing so. Section 42 notes that an increase or "boost" of up to 130 percent in the eligible basis can be awarded by an allocating agency to a housing development in a qualified census tract or difficult development area.[11]

[9]The credit the taxpayer can claim each year is determined by the following calculations: (1) eligible basis x applicable fraction = qualified basis; and (2) qualified basis x applicable percentage = annual credit amount. Qualified basis is the portion of a project's total costs—excluding the costs of land, obtaining permanent financing, rent reserves, syndication, and marketing—allocable to units that meet Section 42 requirements for rent, tenant income, and habitability. The applicable fraction is the lesser of the portion of qualified low-income units in relation to total rental units or the portion of total floor space dedicated to low-income units in relation to the total floor space of residential rental units. The applicable percentage is the discount factor needed to limit the present value of the credit available over a 10-year period to either 70 percent or 30 percent of the qualified basis, depending on the characteristics of the housing. The credit percentages are adjusted monthly by IRS based on current interest rates. Under a special rule first enacted in 2008 and made permanent in 2015, the minimum percentage is 9 percent for the buildings eligible for the 70 percent credit.

[10]Our review examined plans from 2013 or the most recent QAP available. Allocating agencies we observed that did not describe cost limits in their QAPs still may have used cost limits or other factors as a measure of reasonableness in their actual application reviews and these may have been documented elsewhere.

[11]A difficult development area is "any area designated by the Secretary of Housing and Urban Development as an area which has high construction, land, and utility costs relative to area median gross income." 26 U.S.C § 42(d)(5)(B)(iii)(I). The Housing and Economic Recovery Act of 2008 amended Section 42 and gave allocating agencies the discretion to designate any building, regardless of location, as eligible for a boost of up to 130 percent of the eligible basis. Although the boost is applied to the total eligible basis (as opposed to the total credit amount), the credit amount awarded increases (the actual increase to the credit award is less than 30 percent because the award is determined by multiplying the applicable fraction by the total eligible basis, which is increased by the boost).

According to our QAP analysis, 44 of 58 plans we reviewed included criteria for awarding discretionary basis boosts, with 16 plans explicitly specifying the use of basis boosts for projects as needed for financial or economic feasibility. The discretionary boosts were applied to different types of projects and on different scales (for example, statewide or citywide).

- For example, we found one development that received a boost to the eligible basis for having received certain green building certifications, although the applicant did not demonstrate financial need or request the boost. The allocating agency told us that all projects with specified green building certifications received the boost automatically, as laid out in its QAP. At the time of our review, agency officials said that the agency had changed its practices to prevent automatic basis boosts from being applied and required additional checks for financial need.
- In another QAP we reviewed, one agency described an automatic 130 percent statewide boost for all LIHTC developments. According to the officials, the automatic statewide boost remained in effect because officials made the determination that nearly all projects would need it for financial feasibility.

Section 42 requires that allocating agencies determine that "discretionary basis boosts" were necessary for buildings to be financially feasible before granting them to developers.[12] Section 42 does not require allocating agencies to document their analysis for financial feasibility (with or without the basis boost). However, legislative history for the Housing and Economic Recovery Act of 2008 included expectations that allocating agencies would set standards in their QAPs for which projects would be allocated additional credits, communicate the reasons for designating such criteria, and publicly express the basis for allocating additional credits to a project.[13] In addition, NCSHA (a nonprofit advocating for state allocating agencies) recommends that allocating agencies set standards in their QAPs to determine eligibility for discretionary basis boosts and make the determinations publicly available.[14]

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[12]We use "discretionary basis boosts" to describe boosts awarded to developments outside of qualified census tracts or difficult development areas.

[13]H. Rept No. 110-606, at 25 (2008).

[14]National Council of State Housing Agencies, *Report of the National Council of State Housing Agencies' Housing Credit Task Force on Recommended Practices in Housing Credit Allocation and Underwriting* (December 2011).

Agencies We Visited Had Processes for Monitoring Compliance

In our 2016 report we found that the allocating agencies we visited had processes for and conducted compliance monitoring of projects consistent with Section 42 and Treasury regulations. Treasury regulations require allocating agencies to conduct on-site physical inspections for at least 20 percent of the project's low-income units and file reviews for the tenants in these units at least once every 3 years. In addition, allocating agencies must annually review owner certifications that affirm that properties continue to meet LIHTC program requirements.

- Allocating agencies we visited followed regulatory requirements on when to conduct physical inspections and tenant file reviews.
- Allocating agencies we visited generally used electronic databases to track the frequency of inspections, file reviews, and certifications, although most of these agencies documented these reviews on paper.
- All the allocating agencies we visited had inspection and review processes in place to monitor projects following the 15-year compliance period, as required under Section 42. Allocating agencies must execute an extended low-income housing commitment to remain affordable for a minimum of 30 years before a tax credit project can receive credits. After the compliance period is over, the obligation for allocating agencies to report to IRS on compliance issues ends and investors are no longer at risk for tax credit recapture.

IRS Oversight of LIHTC Has Been Minimal

Our prior reports found IRS conducted few reviews of allocating agencies and had not reviewed how agencies determined basis boosts. Data on noncompliance were not reliable and IRS used little of the reported program information. IRS had not directly participated in an interagency initiative to augment HUD's databases with LIHTC property inspection data. Both our 2015 and 2016 reports concluded that opportunities existed to enhance oversight of the LIHTC program, specifically by leveraging the knowledge and experience of HUD.

IRS Conducted Few Reviews of Allocating Agencies and Had Not Reviewed How Agencies Determined Basis Boosts

Few reviews of allocating agencies. In our 2015 report, we found that IRS had conducted seven audits (reviews) of allocating agencies from 1986 (inception of the program) through May 2015. In the audits, IRS found issues related to QAPs, including missing preferences and selection criteria.

But in both our 2015 and 2016 reports, IRS officials stated that they did not regard a regular review of QAPs as part of their responsibilities as outlined in Section 42 and therefore did not regularly review the plans.[15] IRS officials said that allocating agencies have primary responsibility to ensure that the plans meet Section 42 preferences and selection criteria. IRS officials noted that review of a QAP to determine if the plan incorporated the elements specified in Section 42 could occur if IRS were to audit an allocating agency.

No review of agencies' discretionary basis boosts. In our 2016 report, we found IRS had not reviewed the criteria allocating agencies used to award discretionary basis boosts. The use of basis boosts has implications for LIHTC housing production because of the risk of oversubsidizing projects, which would reduce the amount of the remaining allocable subsidies and yield fewer LIHTC projects overall within a state.

IRS also had not provided guidance to agencies on how to determine the need for the additional basis to make projects financially feasible. IRS officials told us that Section 42 gives allocating agencies the discretion to determine if projects receive a basis boost and does not require documentation of financial feasibility. Additionally, IRS officials explained that because the overall amount of subsidies allocated to a state is limited, the inherent structure of the program discourages states from oversubsidizing projects. However, during our 2016 review, we observed a range of practices for awarding discretionary basis boosts, including a blanket basis boost that could result in fewer projects being subsidized and provide more credits than necessary for financial feasibility. We concluded that because IRS did not regularly review QAPs, many of which list criteria for discretionary basis boosts, IRS was unable to determine the extent to which agency policies could result in oversubsidizing of projects.

[15] In GAO-15-330, we reported that IRS did not regularly review QAPs as it was the agency's view that regular reviews of QAPs were outside the scope of its compliance responsibilities.

Some Program Data Were Not Reliable and IRS Used Little of Reported Program Information

Unreliable data. We reported in 2015 that IRS had not comprehensively captured information reported for the program in its Low-Income Housing Credit database and the existing data were not complete and reliable. IRS guidance requires the collection of data on the LIHTC program in an IRS database, which records information submitted by allocating agencies and taxpayers on three forms. The forms include

- **Credit allocation and certification (Form 8609).** The two-part form is completed by the allocating agency and the taxpayer. Agencies report the allocated amount of tax credits available over a 10-year period for each building in a project. The taxpayer reports the date on which the building was placed-in-service (suitable for occupancy).
- **Noncompliance or building disposition (Form 8823).** Allocating agencies must complete and submit this form to IRS if an on-site physical inspection of a LIHTC project finds any noncompliance. The form records any findings (and corrections of previous findings) based on the inspection of units and review of the low-income tenant certifications.
- **Annual report (Form 8610).** IRS staff review the reports to ensure allocations do not exceed a statutorily prescribed ceiling for that year.

Based on our analysis of the information in the database, we found in 2015 that the data on credit allocation and certification information were not sufficiently reliable to determine if basic requirements for the LIHTC program were being achieved. For example, we could not determine how often LIHTC projects were placed-in-service within required time frames. We concluded that without improvements to the data quality of credit allocation and certification information, it was difficult to determine if credit allocation and placed-in-service requirements had been met by allocating agencies and taxpayers, respectively. Thus, we recommended that IRS should address weaknesses identified in data entry and programming controls to ensure reliable data are collected on credit allocations.

At the time of our 2015 report, IRS acknowledged the need for improvements in its controls and procedures (including data entry and quality reviews). IRS officials agreed that these problems should be corrected and data quality reviews should be conducted on an ongoing basis. As of March 2017, in response to our recommendation, IRS officials said that they had explored possibilities to improve the database, which not only houses credit allocation information, but also data from noncompliance and building disposition forms. Specifically, IRS is working to move the database to a new and updated server, which will address weaknesses identified in data entry and programming controls. IRS expects to complete the data migration step by early fall of 2017. Until IRS implements its plan to improve the data, this recommendation will remain open.

Limited noncompliance data, analysis, and guidance on reporting. We found in our 2015 and 2016 reports that IRS had done little with the information it collects on noncompliance. IRS had captured little information from the Form 8823 submissions in its database and had not tracked the resolution of noncompliance issues or analyzed trends in noncompliance. As of April 2016, the database included information from about 4,200 of the nearly 214,000 Form 8823s IRS received since 2009 (less than 2 percent of forms received).

For our 2015 report, officials told us the decision was made during the 2008–2009 timeframe to input information only from forms that indicated a change in building disposition, such as a foreclosure. IRS focused on forms indicating this change for reasons including the serious nature of the occurrence for the program and impacts on taxpayers' ability to receive credit. Officials also stated it was not cost effective to input all the form information and trend analysis on all types of noncompliance was not useful for purposes of ensuring compliance with the tax code.

In addition, as we reported in both 2015 and 2016, IRS had assessed little of the noncompliance information collected on the Form 8823 or routinely used it to determine trends in noncompliance. Because little information was captured in the Low-Income Housing Credit database, IRS was unable to provide us with program-wide information on the most common types of noncompliance. Furthermore, IRS had no method to determine if issues reported as uncorrected had been resolved or if properties had recurring noncompliance issues.

In our 2016 report, we also found inconsistent reporting on the noncompliance forms, the reasons for which included conflicting IRS guidance, different interpretations of the guidance by allocating agencies, and lack of IRS feedback about agency submissions.

- IRS developed guidelines for allocating agencies to use when completing the Form 8823, the "fundamental purpose" of which was identified as providing standardized operational definitions for the noncompliance categories listed on the form. The IRS guide adds that it is important that noncompliance be consistently identified, categorized, and reported and notes that the benefits of consistency included enhanced program administration by IRS.

- Allocating agencies we visited had various practices for submitting Form 8823 to IRS, including different timing of submissions, reporting on all violations (whether minor or corrected during inspections) or not, and amounts of additional detail provided. Partly because of these different practices, the number of forms each of the nine agencies told us they sent to IRS in 2013 varied from 1 to more than 1,700.

We concluded that without IRS clarification of when to send in the Form 8823, allocating agencies will continue to submit inconsistent noncompliance data to IRS, which will make it difficult for IRS to efficiently distinguish between minor violations and severe noncompliance, such as properties with health and safety issues. We recommended that IRS should clarify what to submit and when—in collaboration with the allocating agencies and Treasury—to help IRS improve the quality of the noncompliance information it receives and help ensure that any new guidance is consistent with Treasury regulations.

In August 2016, IRS stated it would review the Form 8823 Audit Technique Guide to determine whether additional guidance and clarification were needed for allocating agencies to report noncompliance information on the form. If published legal guidance is required, IRS stated that it will submit a proposal for such guidance for prioritization. IRS indicated an expected implementation date by November 2017. In addition, in March 2017, officials stated that IRS Counsel attended an industry conference with allocating agencies at which issues related to the Form 8823 were discussed.

Lack of participation in data initiative. Moreover, in our 2016 report we found IRS had not taken advantage of the important progress HUD made through the Rental Policy Working Group (working group)—which was established to better align the operation of federal rental policies across the administration—to augment its databases with LIHTC property inspection data.[16] This data collection effort created opportunities for HUD to share inspection data with IRS that could improve the effectiveness of reviews for LIHTC noncompliance. However, the IRS Small

[16]The Rental Policy Working Group comprises representatives from the White House Domestic Policy Council, National Economic Council, Office of Management and Budget, HUD, Treasury, the Department of Agriculture, and the Department of Justice.

Business/Self-Employed Division managing the LIHTC program had not been involved in the working group. We concluded that such involvement would allow IRS to leverage existing resources, augment its information on noncompliance, and better understand the prevalence of noncompliance.

We recommended that staff from the division participate in the physical inspection initiative of the working group and also recommended that the IRS Commissioner evaluate how IRS could use HUD's real estate database, including how the information might be used to reassess reporting categories on Form 8823 and reassess which categories of noncompliance information to review for audit potential. As of March 2017, IRS had implemented our recommendation to include the appropriate staff at the working group meetings. However, IRS officials stated that since HUD's database with property inspection data was not complete as of March 2017 and contained data from 30 states, it was unclear how the database could be used. IRS officials said they would continue exploring the HUD database if the data for all LIHTC properties were included and it was possible to isolate the LIHTC property data from other rental properties in the HUD database.

Leveraging Experience of HUD May Augment IRS's Capacity to Oversee Program

Both our 2015 and 2016 reports found that opportunities existed to enhance oversight of the LIHTC program, specifically by leveraging the knowledge and experience of HUD. We found in 2015 that while LIHTC is the largest federal program for increasing the supply of affordable rental housing, LIHTC is a peripheral program in IRS in terms of resources and mission. Oversight responsibilities for the program include monitoring allocating agencies and taxpayer compliance. However, as we have discussed previously, IRS oversight has been minimal and IRS has captured and used little program information. As we previously stated, such information could help program managers and congressional decision makers assess the program's effectiveness.

HUD—which has a housing mission—collects and analyzes information on low-income rental housing, including LIHTC-funded projects. As we reported in 2015, HUD's role in the LIHTC program is generally limited to the collection of information on tenant characteristics (mandated by the Housing and Economic Recovery Act of 2008). However, it has voluntarily collected project-level information on the program since 1996 because of the importance of LIHTC as a source of funding for affordable housing. HUD also has sponsored studies of the LIHTC program that use these data. HUD's LIHTC databases, the largest federal source of information on the LIHTC program, aggregates project-level data that allocating agencies voluntarily submit and information on tenant characteristics that HUD must collect. Since 2014, HUD also has published annual reports analyzing data it must collect on tenants residing in LIHTC properties. As part of this report, HUD compares property information in its tenant database to the information in its property database to help assess the completeness of both databases.

In our 2015 report, we also discussed HUD's experience in working with allocating agencies. While multiple federal agencies administer housing-related programs, HUD is the lead federal agency for providing affordable rental housing. Much like LIHTC, HUD's rental housing programs rely on state and local agencies to implement programs. HUD is responsible for overseeing these agencies, including reviewing state and local consolidated plans for the HOME Investment Partnership and Community Development Block Grant programs—large grant programs that also are used to fund LIHTC projects. HUD also has experience in directly overseeing allocating agencies in their roles as contract administrators for project-based Section 8 rental assistance. HUD has processes, procedures, and staff in place for program evaluation and oversight of state and local agencies that could be built upon and strengthened.

In our 2015 report, we concluded that significant resource constraints affected IRS's ability to oversee taxpayer compliance and precluded wide-ranging improvement to such functions, but that IRS still had an opportunity to enhance oversight of LIHTC. We also concluded that leveraging the experience and expertise of another agency with a housing mission, such as HUD, might help offset some of IRS's limitations in relation to program oversight. HUD's existing processes and procedures for overseeing allocating agencies could constitute a framework on which further changes and improvements in LIHTC could be effected. However, enhancing HUD's role could involve additional staff and other resources. An estimate of potential costs and funding options for financing enhanced federal oversight of the LIHTC program would be integral to determining an appropriate funding mechanism.

We asked that Congress consider designating HUD as a joint administrator of the program responsible for oversight. As part of the deliberation, we suggested that Congress direct HUD to estimate the costs to monitor and perform the additional oversight responsibilities, including a discussion of funding options. Treasury agreed that it would be useful for HUD to receive ongoing responsibility for, and resources to perform, research and analysis on the effectiveness of LIHTCs in increasing the availability of affordable rental housing. Treasury noted that such research and analysis are not part of IRS's responsibilities or consistent with its expertise in interpreting and enforcing tax laws. However, Treasury stated that responsibility for interpreting and enforcing the code should remain entirely with IRS. Our report noted that if program administration were changed, IRS could retain certain key responsibilities consistent with its tax administration mission.

In our 2016 report, we concluded that IRS oversight of allocating agencies continued to be minimal, particularly in reviewing QAPs and allocating agencies' practices for awarding discretionary basis boosts. As a result, we reiterated the recommendation from our 2015 report that Congress should consider designating HUD as a joint administrator of the program responsible for oversight due to its experience and expertise as an agency with a housing mission.

In response to our 2016 report, HUD stated it remains supportive of mechanisms to use its significant expertise and experience administering housing programs for enhanced effectiveness of LIHTC. HUD also stated that enhanced interagency coordination could better ensure compliance with fair housing requirements and improve alignment of LIHTC with national housing priorities. As of July 2017, Congress had not enacted legislation to give HUD an oversight role for LIHTC.

Chairman Hatch, Ranking Member Wyden, and Members of the Committee, this concludes my prepared statement. I would be happy to respond to any questions that you may have at this time.

GAO Contact and Staff Acknowledgments

For further information about this testimony, please contact me at 202-512-8678 or garciadiazd@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals making key contributions to this testimony include Nadine Garrick Raidbard, Assistant Director; Anar N. Jessani, Analyst in Charge; William R. Chatlos; Farrah Graham; Daniel Newman; John McGrail; Barbara Roesmann; and MaryLynn Sergent.

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