DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Office of the Secretary

[Docket No. FR–3956–N–01]

Statutorily Mandated Designation of Difficult Development Areas for Section 42 of the Internal Revenue Code of 1986

AGENCY: Office of the Secretary, HUD.

ACTION: Notice.

SUMMARY: This document provides revised designations of ''Difficult Development Areas'' for purposes of the Low-Income Housing Tax Credit (''LIHTC'') under section 42 of the Internal Revenue Code of 1986, and provides the methodology used by the United States Department of Housing and Urban Development (''HUD''). The new Difficult Development Areas are based on FY 1995 Fair Market Rents (''FMRs''), FY 1995 income limits and 1990 census population counts as explained below. The corrected designations of ''Qualified Census Tracts'' under section 42 of the Internal Revenue Code published May 1, 1995, at 60 FR 21246 remain in effect.

FOR FURTHER INFORMATION CONTACT: Harold J. Gross, Senior Tax Attorney, Office of the General Counsel, Department of Housing and Urban Development, 451 Seventh Street, S.W., Washington, D.C. 20410, telephone (202) 708–3260, or Kurt G. Usowski, Economist, Division of Economic Development and Public Finance, Office of Policy Development and Research, Department of Housing and Urban Development, 451 Seventh Street, S.W., Washington, D.C. 20410, telephone (202) 708–0426, e-mail Kurt—G.—Usowski@hud.gov. A telecommunications device for deaf persons (TDD) is available at (202) 708–9300. (These are not toll-free telephone numbers.)

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SUPPLEMENTARY INFORMATION:

Background

The U.S. Treasury Department and the Internal Revenue Service are authorized to interpret and enforce the provisions of the Internal Revenue Code of 1986 (the ''Code''), including the Low-Income Housing Tax Credit (''LIHTC'') found at section 42 of the Code, as enacted by the Tax Reform Act of 1986 [Pub. L. 99–514], as amended by the Technical and Miscellaneous Revenue Act of 1988 [Pub. L. 100–647]; the Omnibus Budget Reconciliation Act of 1989 [Pub. L. 101–239]; the Omnibus Budget Reconciliation Act of 1990 [Pub. L. 101–508]; the Tax Extension Act of 1991 [Pub. L. 102–227]; and as amended and made permanent by the Omnibus Budget Reconciliation Act of 1993 [Pub. L. 103–66]. The Secretary of HUD is required to designate Difficult Development Areas by section 42(d)(5)(C) of the Code.

In order to assist in understanding HUD's mandated designation of Difficult Development Areas for use in administering section 42 of the Code, a summary of section 42 is provided. The following summary does not purport to bind the Treasury or the IRS in any way, nor does it purport to bind HUD as HUD has no authority to interpret or administer the Code, except in those instances where it has a specific delegation.

Summary of Low Income Housing Tax Credit

The LIHTC is a tax incentive intended to increase the availability of low income housing. Section 42 provides an income tax credit to owners of newly constructed or substantially rehabilitated low-income rental housing projects. The dollar amount of the LIHTC available for allocation by each state (the ''credit ceiling'') is limited by population. Each state is allocated credit based on $1.25 per resident. Also, states may carry forward unused or returned credit for one year; if not used by then, credit goes into a national pool to be allocated to states as additional credit. State and local housing agencies allocate the state's credit ceiling among low income housing buildings whose owners have applied for the credit.

The credit allocated to a building is based on the cost of units placed in service as low-income units under certain minimum occupancy and maximum rent criteria. In general, a building must meet one of two thresholds to be eligible for the LIHTC: either 20 percent of units must be rent-restricted and occupied by tenants with incomes no higher than 50 percent of the Area Median Gross Income (''AMGI''), or 40 percent of units must be rent restricted and occupied by tenants with incomes no higher than 60 percent of AMGI. The term ''rent-restricted'' means that gross rent, including an allowance for utilities, cannot exceed 30 percent of the tenant's imputed income limitation (i.e., 50 percent or 60 percent of AMGI). The rent and occupancy thresholds remain in effect for at least 15 years, and building owners are required to enter into agreements to maintain the low income character of the building for an additional 15 years.

The LIHTC reduces income tax liability dollar for dollar. It is taken annually for a term of ten years and is intended to yield a present value of either (1) 70 percent of the ''qualified basis'' for new construction or substantial rehabilitation expenditures that are not federally subsidized (i.e., financed with tax-exempt bonds or below-market federal loans), or (2) 30 percent of the qualified basis for the acquisition of existing projects or projects that are federally subsidized. The actual credit rates are adjusted monthly for projects placed in service after 1987 under procedures specified in section 42. Individuals can use the credit up to a deduction equivalent of $25,000. This equals $9,900 at the 39.6 percent maximum marginal tax rate. Individuals cannot use the credit against the alternative minimum tax. Corporations, other than S or professional service corporations, can use the credit against ordinary income tax. They cannot use the credit against the alternative minimum tax. These corporations can also deduct the losses from the project.

The qualified basis represents the product of the ''applicable fraction'' of the building and the ''eligible basis'' of the building. The applicable fraction is based on the number of low income units in the building as a percentage of the total number of units, or based on the floor space of low income units as a percentage of the total floor space in the building. The eligible basis is the adjusted basis attributable to acquisition rehabilitation, or new construction costs (depending on the type of LIHTC involved). These costs include amounts chargeable to capital account incurred prior to the end of the first taxable year in which the qualified low income building is placed in service. In the case of buildings located in designated Qualified Census Tracts or designated Difficult Development Areas, eligible basis can be increased up to 130 percent of what it would otherwise be. This means that the available credit also can be increased by up to 30 percent. For example, if the 70 percent credit is available, it effectively could be increased up to 91 percent.

Under section 42(d)(5)(C) of the Code, a Qualified Census Tract is any census tract (or equivalent geographic area defined by the Bureau of the Census) in

which at least 50 percent of households have an income less than 60 percent of the AMGI. There is a limit on the Qualified Census Tracts in any Metropolitan Statistical Area (''MSA'') or Primary Metropolitan Statistical Area (''PMSA'') that may be designated to receive an increase in eligible basis: all of the designated census tracts within a given MSA/PMSA may not together contain more than 20 percent of the total population of the MSA/PMSA. For purposes of HUD designations of Qualified Census Tracts, all non-metropolitan areas in a state are treated as if they constituted a single metropolitan area. This Notice does not redesignate Qualified Census Tracts. The corrected designation of Qualified Census Tracts published May 1, 1995, at 60 FR 21246 remains in effect. Qualified Census Tracts will not be redesignated until year 2000 census data become available.

Section 42 defines a Difficult Development Area as any area designated by the Secretary of HUD as an area that has high construction, land, and utility costs relative to the AMGI. Again, limits apply. All designated Difficult Development Areas in MSAs/PMSAs may not contain more than 20 percent of the aggregate population of all MSAs/PMSAs, and all designated areas not in metropolitan areas may not contain more than 20 percent of the aggregate population of all non-metropolitan counties.

Explanation of HUD Designation Methodology

A. Difficult Development Areas

In developing the list of Difficult Development Areas, HUD compared incomes with housing costs. HUD used 1990 Census data and the MSA/PMSA definitions as published by the Office of Management and Budget (''OMB'') in OMB Bulletin No. 94–07 on July 5, 1994, *with the exceptions described in section C., below.* The basis for these comparisons was the fiscal year (''FY'') 1995 HUD income limits for Very Low Income households (''VLILs'') and Fair Market Rents (''FMRs'') used for the section 8 Housing Assistance Payments Program. The procedure used in making these calculations follows (Note that while the description of HUD's selection methodology differs from previous designations of Difficult Development Areas, the methodology is mathematically equivalent):

1. For each MSA/PMSA and each non-metropolitan county, a ratio was calculated. This calculation used the FY 1995 two-bedroom FMR and the FY 1995 four-person VLIL. The numerator of the ratio was the area's FY 1995 FMR. The denominator of the ratio was the monthly LIHTC income-based rent limit calculated as 1/12 of 30 percent of 120 percent of the area's VLIL (where 120 percent of the VLIL was rounded to the nearest $50 and not allowed to exceed 80 percent of the AMGI in areas where the VLIL is adjusted upward from its 50 percent of AMGI base).

2. The ratios of the FMR to the LIHTC income-based rent limit were arrayed in descending order, separately, for MSAs/PMSAs and for non-metropolitan counties.

3. The Difficult Development Areas are those with the highest ratios cumulative to 20 percent of the 1990 population of all metropolitan areas and of all non-metropolitan counties.

B. Application of Population Caps to Difficult Development Area Determinations

In identifying Difficult Development Areas, HUD applied various caps, or limitations, as noted above. The cumulative population of metropolitan Difficult Development Areas cannot exceed 20 percent of the cumulative population of all metropolitan areas and the cumulative population of nonmetropolitan Difficult Development Areas cannot exceed 20 percent of the cumulative population of all nonmetropolitan counties.

In applying these caps, HUD established procedures to deal with how to treat small overruns of the caps. The remainder of this section explains the procedure. In general, HUD stops selecting areas when it is impossible to choose another area without exceeding the applicable cap. The only exceptions to this policy are when the next eligible excluded area contains either a large absolute population or a large percentage of the total population, or the next excluded area's ranking ratio as described above was identical (to three decimal places) to the last area selected, *and* its inclusion resulted in only a minor overrun of the cap. Thus for both the designated metropolitan and non-metropolitan Difficult Development Areas there are minimal overruns of the caps. HUD believes the designation of these additional areas is consistent with the intent of the legislation. Some latitude is justifiable because it is impossible to determine whether the 20 percent cap has been exceeded, as long as the apparent excess is small, due to measurement error. Despite the care and effort involved in a decennial census, it is recognized by the Census Bureau, and all users of the data, that the population counts for a given area and for the entire country are not precise. The extent of the measurement error is unknown. Thus, there can be errors in both the numerator and denominator of the ratio of populations used in applying a 20 percent cap. In circumstances where a strict application of a 20 percent cap results in an anomalous situation, recognition of the unavoidable imprecision in the census data justifies accepting *small* variances above the 20 percent limit.

C. Exceptions to OMB Definitions of MSAs/PMSAs and Other Geographic Matters

As stated in OMB Bulletin 94–07 defining metropolitan areas: OMB establishes and maintains the definitions of the [Metropolitan Areas] MAs solely for statistical purposes * * * OMB does not take into account or attempt to anticipate any nonstatistical uses that may be made of the definitions * * * We recognize that some legislation specifies the use of metropolitan areas for programmatic purposes, including allocating Federal funds.

HUD makes exceptions to OMB definitions in calculating FMRs by deleting counties from metropolitan areas whose OMB definitions are determined by HUD to be larger than their housing market areas. In addition, HUD is required by statute to calculate a separate FMR and VLIL for Westchester County, New York, which OMB includes as part of the New York, NY PMSA. Thus the following counties are assigned their own FMRs and VLILs and evaluated as if they were separate metropolitan areas for purposes of designating Difficult Development Areas.

Metropolitan Area and Counties Deleted

Atlanta, GA—Carrol, Pickens, and Walton Counties.
Chicago, IL—DeKalb, Grundy, and Kendall Counties.
Cincinnati-Hamilton, OH-KY-IN—Brown County, Ohio; Gallatin, Grant, and Pendleton Counties in Kentucky; and Ohio County, Indiana.
Dallas, TX—Henderson County.
Lafayette, LA—St. Landry and Acadia Parishes.
New York, NY—Westchester County.
New Orleans, LA—St. James Parish.
Washington, DC-MD-VA-WV—Clarke, Culpeper, King George, and Warren Counties in Virginia; and Berkeley and Jefferson Counties in West Virginia.
Affected MSAs/PMSAs are assigned the indicator ''(part)'' in the list of Metropolitan Difficult Development Areas.

Finally, in the New England states (Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, and Vermont) OMB defines MSAs/PMSAs according to county subdivisions or Minor Civil Divisions (''MCDs'') rather than county boundaries. Thus, when a

New England county is designated as a Nonmetropolitan Difficult Development Area, only that part of the county (the group of MCDs) not included in any MSA/PMSA is the Nonmetropolitan Difficult Development Area. Geographic definitions of the nonmetropolitan parts of New England counties can be found in HUD's Rule establishing FY 1995 FMRs at 60 FR 42230 or 24 CFR Part 888. Affected counties are assigned the indicator ''(part)'' in the list of Nonmetropolitan Difficult Development Areas.

Future Designations

Difficult Development Areas are designated annually as updated income and FMR data become available. Qualified Census Tracts will not be redesignated until year 2000 census data become available.

Effective Date

The list of Difficult Development Areas is effective for allocations of credit made after December 31, 1995. In the case of a building described in Internal Revenue Code section 42(h)(4)(B), the list is effective if the bonds are issued and the building is placed in service after December 31, 1995. The corrected designations of Qualified Census Tracts published May 1, 1995, at 60 FR 21246 remain in effect.

Other Matters

Environmental Impact

In accordance with 40 CFR 1508.4 of the CEQ regulations and 24 CFR 50.20 of the HUD regulations, the policies and actions in this document are determined not to have the potential of having a significant impact on the quality of the human environment and therefore further environmental review under the National Environmental Policy Act is not necessary.

Regulatory Flexibility Act

In accordance with 5 U.S.C. § 605(b) (the Regulatory Flexibility Act), the undersigned hereby certifies that this notice does not have a significant economic impact on a substantial number of small entities. The notice involves the designation of ''Difficult Development Areas'' for use by political subdivisions of the States in allocating the LIHTC as required by section 42 of the Code, as amended. This notice places no new requirements on the States, their political subdivisions, or the applicants for the credit. This notice also details the technical methodology used in making such designations.

Executive Order 12612, Federalism

The General Counsel, as the Designated Official under section 6(a) of Executive Order 12612, *Federalism*, has determined that the policies contained in this notice will not have any substantial direct effects on States or their political subdivisions, or the relationship between the Federal government and the States, or on the distribution of power and responsibilities among the various levels of government. As a result, the notice is not subject to review under the order. The notice merely designates ''Difficult Development Areas'' for use by political subdivisions of the States in allocating the LIHTC as required by section 42 of the Code, as amended. The notice also details the technical methodology used in making such designations.

Executive Order 12606, The Family

The General Counsel, as the Designated Official under Executive Order 12606, *The Family*, has determined that this notice does not have potential for significant impact on family formation, maintenance, and general well-being, and, thus, is not subject to review under the Order. The notice involves the designation of ''Difficult Development Areas'' for use by political subdivisions of the States in allocating the LIHTC as required by section 42 of the Code, as amended. The notice also details the technical methodology used in making such designations.

Dated: September 11, 1995.

Henry G. Cisneros,

Secretary.

IRS SECTION 42(D)(5)(C) DIFFICULT DEVELOPMENT AREAS—METROPOLITAN AREAS

State	Metropolitan area	Metropolitan area	Metropolitan area	Metropolitan area
AZ	Yuma, AZ.			
CA	Chico-Paradise, CA.	Los Angeles Long Beach, CA	Salinas, CA	San Francisco, CA.
	San Luis Obispo-Atascadero-Paso Robles, CA.	Santa Barbara-Santa Maria Lompoc, CA.	Santa Cruz-Watsonville, CA	Santa Rosa, CA
	Ventura, CA.			
CT	Bridgeport, CT	New Haven-Meriden, CT	Stamford-Norwalk, CT	
FL	Daytona Beach, FL	Fort Lauderdale, FL	Fort Myers-Cape Coral, FL	Fort Pierce-Port Lucie, FL.
	Miami, FL	Punta Gorda, FL	Sarasota-Bradenton, FL	West Palm Beach-Boca Raton, FL.
HI	Honolulu, HI.			
MA	Barnstable-Yarmouth, MA	Fitchburg-Leominster, MA	Worcester, MA–CT	
ME	Portland, ME.			
NH	Portsmouth-Rochester, NH–ME.			
NJ	Atlantic-Cape May, NJ	Jersey City, NJ	Monmouth-Ocean, NJ	Vineland-Millville-Bridgeton, NJ.
NY	Nassau-Suffolk, NY	New York, NY (part)	Newburgh, NY–PA	
OR	Eugene-Springfield, OR.			
PR	Aguadilla, PR	Arecibo, PR	Caguas, PR	Mayaguez, PR.
	Ponce, PR	San Juan-Bayamon, PR.		
RI	Providence-Fall River-Warwick, RI–MA..			
SC	Myrtle Beach, SC.			
TX	Brownsville-Harlingen-San Benito, TX.	El Paso, TX	Laredo, TX	
WA	Bellingham, WA	Yakima, WA.		

IRS SECTION 42(D)(5)(C) DIFFICULT DEVELOPMENT AREAS—NONMETROPOLITAN AREAS

State	County	County	County	County
	Pacific Islands.			
AK	Bethel Census Area	Dillingham Census Area	Fairbanks North Star Borough	Haines Borough.
	Juneau Borough	Ketchikan Gateway Borough	Kodiak Island Borough	Lake And Peninsula Borough.
	Nome Census Area	North Slope Borough	Northwest Arctic Borough	
AL	Coffee County	Macon County		
AR	Baxter County	Conway County	Garland County	Madison County.
	Mississippi County.			
AZ	Cochise County	Coconino County	Gila County	Santa Cruz County.
	Yavapai County			
CA	Alpine County	Amador County	Calaveras County	Del Norte County.
	Humboldt County	Imperial County	Inyo County	Kings County.
	Lake County	Mariposa County	Mendocino County	Mono County.
	Nevada County	Plumas County	San Benito County	Sierra County.
	Siskiyou County	Tuolumne. County		
CO	Eagle County	Garfield County	Gilpin County	Grand County.
	La Plata County	Lake County	Ouray County	Pitkin County.
	Routt County	San Miguel County.		
CT	Litchfield County (part)	Middlesex County (part)	New London County (part)	Windham County (part).
DE	Sussex County.			
FL	Citrus County	Desoto County	Franklin County	Glades County.
	Hardee County	Hendry County	Highlands County	Indian River County.
	Monroe County	Okeechobee County	Taylor County.	
GA	Bulloch County	Butts County	Camden County	Dawson County.
	Liberty County	Union County.		
HI	Hawaii County	Kauai County	Maui County	
ID	Bonner County	Kootenai County		
KS	Riley County.			
KY	Adair County	Bell County	Estill County	Floyd County.
	Johnson County	Lincoln County	Morgan County	Nicholas County.
	Perry County	Pike County	Pulaski County.	
LA	Morehouse Parish.	Natchitoches Parish	Tangipahoa Parish	Vernon Parish.
	West Feliciana Parish.			
MA	Barnstable County (part)	Dukes County	Franklin County (part)	Hampden County (part).
	Hampshire County (part)	Nantucket County	Worcester County (part).	
MD	St. Mary's County	Wicomico County.		
ME	Androscoggin County (part)	Aroostook County	Cumberland County	Franklin County.
	Hancock County	Kennebec County	Knox County	Lincoln County.
	Oxford County	Penobscot County (part)	Piscataquis County	Sagadahoc County
	Somerset County	Waldo County (part)	Washington County	York County (part).
MO	Camden County.			
MS	Adams County	Bolivar County	Claiborne County	Coahoma County.
	Copiah County	George County	Issaquena County	Lafayette County.
	Lauderdale County	Leflore County	Sunflower County	Tate County.
	Washington County	Yazoo County.		
MT	Missoula County.			
NC	Camden County	Dare County	Pasquotank County	Watauga County.
NH	Belknap County	Carroll County	Cheshire County	Grafton County.
	Hillsborough County (part)	Merrimack County (part)	Rockingham County (part)	Strafford County.
	Sullivan County.			
NM	Chaves County	Curry County	Lincoln County	Mckinley County.
	Quay County	Rio Arriba County	San Miguel County	Taos County.
NV	Douglas County	Mineral County	Pershing County.	
NY	Clinton County	Columbia County	Cortland County	Essex County.
	Greene County	Hamilton County	Jefferson County	Otsego County.
	Schuyler County	Sullivan County	Tompkins County	Ulster County.
OR	Clatsop County	Coos County	Curry County	Deschutes County.
	Hood River County	Jefferson County	Josephine County	Klamath County.
	Lincoln County.			
PA	Monroe County	Northumberland County	Schuylkill County	Wayne County.
PR	All.			
RI	Newport County (part)	Washington County (part)		
SC	Beaufort County	Fairfield County.		
SD	Faulk County	Spink County.		
TN	Haywood County	Trousdale County.		
TX	Aransas County	Burleson County	Camp County	Gillespie County.
	Hopkins County	Hudspeth County	Jasper County	Kerr County.
	Kimble County	Kleberg County	Llano County	Nacogdoches County.
	Polk County	Rains County	Red River County	Robertson County.
	Tyler County	Val Verde County	Van Zandt County	Walker County.
	Washington County.			
UT	Daggett County	Iron County	Washington County	
VA	Caroline County	Cumberland County	Frederick County	King And Queen County.

IRS SECTION 42(D)(5)(C) DIFFICULT DEVELOPMENT AREAS—NONMETROPOLITAN AREAS—Continued

State	County	County	County	County
	Madison County	Orange County	Shenandoah County	Westmoreland County.
VI	Virgin Islands.			
VT	Addison County	Bennington County	Lamoille County	Orange County.
	Rutland County	Washington County	Windham County	Windsor County.
WA	Clallam County	Douglas County	Grays Harbor County	Jefferson County.
	San Juan County	Skagit County.		
WV	Greenbrier County	Harrison County	Taylor County	Upshur County.
WY	Teton County.			

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