

# PERFORMANCE AUDIT



Office of the  
Washington  
State Auditor  
Pat McCarthy

## Housing Finance Commission: Tenant purchase options under the Low- Income Housing Tax Credit program

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# Executive Summary

## State Auditor's Conclusions (page 28)

At the highest level, the findings of this performance audit are disappointing. An option for tenants in affordable housing projects to buy their homes has not yet been used, despite applying to 135 housing units in 2023.

This failure to deliver on the possibility of homeownership is not the result of state management, however. The state Housing Finance Commission has followed the rules for the tenant purchase option in the federal Low-Income Housing Tax Credit Program.

We found the tenant ownership option is little-known and largely misunderstood. It is not, as it has sometimes been called, a “rent-to-own” program. Though a property must be available to rent for 15 years to become eligible for the purchase option, tenants are not obliged to buy their homes, nor are they automatically transferred from rental agreements to purchase contracts. Indeed, the legal path from renting to purchasing these homes appears quite complex.

I'm particularly proud of our auditors' work to gain a ground-level understanding of the program by meeting with groups of property renters in tribal housing projects. We found that tenants had limited information about the purchase option and wanted to know more. Similarly, we found project developers would like more information about the option and its goals.

In my view, it is telling that auditors could find little information on the federal intent behind including a relatively small incentive for the ownership option in housing projects that otherwise focus on rental units. As our recommendations show, this tenant ownership option needs greater clarity – in communicating how it works, what tenants' options are, and the goals of policy makers in offering it.

## A Primer on Tenant Purchase Options (page 6)

The federal Low-Income Housing Tax Credit (LIHTC) program encourages development of affordable rental housing. A few LIHTC projects offer options for tenants to buy their homes, referred to as tenant purchase options. Properties developed under this arrangement usually offer tenants the option to buy after the home has been available to rent for 15 years. Tenants are not obliged to buy, nor are they automatically transferred from a rental agreement to a purchase contract. Tenant purchase options are thus different from lease-purchase (sometimes called “rent-to-own”) programs.

Project owners are responsible for completing multiple steps before interested tenants can buy their homes. This includes removing the financial partner from the project, preparing tenants for homeownership, and resolving legal complexities for homes located on tribal lands, when applicable. This process can be complex, and so it may take significantly longer than the initial 15 years before tenants actually take ownership of their homes if they are interested in doing so.

## Background (page 10)

The Housing Finance Commission manages the LIHTC program in Washington. LIHTC affordable housing projects offering tenant purchase options are rare. Only 18 of the state's nearly 1,300 LIHTC projects offer tenant purchase options; all but one are managed by tribal governments. Of the 18 projects, just six — with a combined total of 135 homes — had properties old enough to qualify for tenant purchase as of 2023.

Evictions at housing projects managed by the Nooksack Indian Tribe raised concerns about tenant purchase options and, more widely, the LIHTC program managed by the commission. This audit examined the commission's oversight of housing projects that offer tenant purchase options. It did not evaluate the Nooksack Housing Department's decision to evict disenrolled tribal members living in LIHTC housing.

## The Housing Finance Commission met legal requirements, but improved oversight could better support homeownership (page 15)

The commission met legal requirements related to tenant purchase options. It awarded points for tenant purchase in project applications for most of the audit period in accordance with its policies. Although the commission temporarily suspended application points for tenant purchase options during the 2023-24 application cycle, no projects expressed interest in using the option during that time.

Although the commission met legal requirements, its monitoring activities were ineffective for ensuring project owners' progress toward tenant purchases. For example, the commission did not follow its own plan for monitoring project owners' progress in that area. However, commission staff said they have few options to respond to project noncompliance beyond reporting it to the IRS.

Finally, the commission did not develop sufficient guidance for project owners to implement tenant purchase options. Project owners said they would appreciate additional guidance that clarifies the commission's expectations.

## Although the LIHTC program has not yet produced any homeowners, tenants have received other meaningful benefits (page 21)

Project owners have yet to sell and transfer the 135 eligible homes for sale to tenants. This appears inconsistent with formal agreements between the project owners and the commission, although the complex process to prepare for home sales means some delay before tenants can take ownership of their homes could be expected. Commission officials also pointed to limitations in their ability to compel project owners' actions. Project owners we spoke with described a variety of challenges they faced in preparing for tenant home purchases, including unclear requirements and limited guidance. Tenants we interviewed saw benefits to homeownership but also possible challenges. Their understanding of purchase options varied, and most wanted more information about how the program worked. Tenants who want to purchase their homes may face systemic financial barriers. Despite these barriers to homeownership, LIHTC projects provide affordable rental housing to disadvantaged communities, even if tenants do not buy eligible homes. These income-restricted housing options directly benefit communities through increased housing supply and below-market rents.

## Recommendations (page 29)

We made recommendations to the commission to improve its monitoring of projects with tenant purchase options and to provide project owners clearer guidance. These recommendations seek to provide greater assurance that projects will fulfill the tenant purchase options they agreed to, and to improve communication about purchase options between the commission, project owners and tenants.

### Next steps

Our performance audits of state programs and services are reviewed by the Joint Legislative Audit and Review Committee (JLARC) and/or by other legislative committees whose members wish to consider findings and recommendations on specific topics. Representatives of the Office of the State Auditor will review this audit with JLARC's Initiative 900 Subcommittee in Olympia. The public will have the opportunity to comment at this hearing. Please check the JLARC website for the exact date, time, and location ([www.leg.wa.gov/JLARC](http://www.leg.wa.gov/JLARC)). The Office conducts periodic follow-up evaluations to assess the status of recommendations and may conduct follow-up audits at its discretion. See **Appendix A**, which addresses the I-900 areas covered in the audit. **Appendix B** contains information about our methodology.

# A Primer on Tenant Purchase Options

## The federal Low-Income Housing Tax Credit program encourages development of affordable rental housing

Almost 40 years ago, the U.S. Congress recognized the country's fast-growing need for affordable housing was outpaced by the increasing costs of building it. Legislators saw that it was economically unfeasible to build homes that would rent for less than market rates without somehow making up the difference between the costs of constructing the property and the rental income it could generate to pay off construction costs. This gap would be present even if rental profit was not a consideration. As part of the Tax Reform Act of 1986, Congress hit upon a solution: to encourage development by leveraging private funding through the Low-Income Housing Tax Credit (LIHTC) program.

Under this program, federal tax credits are awarded to a **project owner** (typically a government housing authority or a nonprofit organization) to offset the cost of constructing or rehabilitating rental housing. In exchange, the owner agrees to reserve a portion of rent-restricted homes for low-income households. To obtain upfront construction financing, project owners sell the tax credits to a **financial partner** (typically a private investment firm or other financial institution) in exchange for financing. Once the property is open for tenants, the financial partners may claim the tax credits to reduce their federal taxes for 10 years. The LIHTC program is estimated to cost the federal government an average of \$13.5 billion annually in forgone tax revenue. Since its inception, the program has paid for 90% of the federally funded affordable housing in America, financing nearly 3.5 million homes, including thousands in Washington. Projects are typically apartments or other multifamily homes but can also include individual houses.

The federal government gives states authority to allocate tax credits, typically through a housing finance agency or similar state agency, which then allocate the tax credits to qualifying housing projects. These agencies must develop plans for how they will allocate the tax credits and have considerable flexibility to create plans based on the state's housing needs. State agencies typically develop an application process through which project owners may apply for tax credits to construct the housing development. States may use a process through which applications are scored using a points system to ensure the credits are awarded consistently and correctly according to program rules. Once a project has been selected, project owners agree to follow LIHTC program rules.

The IRS oversees the LIHTC program. This includes determining whether projects are following program rules to claim the tax credits during the 10-year time frame.

## A few LIHTC projects offer options for tenants to buy their homes

Although primarily concerned with promoting and sustaining affordable rental accommodation, LIHTC rules allow states to allocate tax credits to projects that will allow tenants to buy their home after it has been available to rent for 15 years. Although the IRS refers to this practice as “eventual tenant ownership,” for the purposes of this report we use the term **tenant purchase option**. In Washington, applications for LIHTC tax credits that incorporate tenant purchase options must include a high-level plan of how the project owner will implement the purchases. The plan must describe how the project owner will determine the sale price and eligibility requirements for tenants to buy the homes.

Properties developed under this arrangement usually offer tenants the option to buy after the home has been available to rent for 15 years. (Unsold homes remain rental housing under tax credit program rules.) Tenants are not obliged to buy, nor are they automatically transferred from a rental agreement to a purchase contract. Tenant purchase options are thus different from lease-purchase (sometimes called “rent-to-own”) programs. In lease-purchase, a portion of the tenant’s rent payments is applied to the sale price, and the tenant is required to purchase the home after a specified period of time.

Homes with tenant purchase options are often single-family houses, townhouses or duplexes. Their clearer property lines – compared to condominiums or other multifamily housing – typically do not require a homeowners’ association or cooperative to manage common areas.

Project owners determine the sale price, as they do in conventional home sales. However, the price is typically lower than homes sold in the rest of the housing market because the program is intended to preserve affordable housing and can only be sold to people who meet LIHTC income eligibility rules. They may structure the purchase in multiple ways. For example, they can award tenants incentive points for meeting certain conditions, such as making timely rent payments, or apply a discount based on how long the tenant has lived there. In some cases, a project owner may decide to apply a portion of the tenant’s rent toward the sale price, similar to a rent-to-own program. **Exhibit 1** (on the following page) shows some of the most common differences between these two types of home purchases and the traditional home-buying process.

## Exhibit 1 – The LIHTC tenant purchase process in Washington differs from both traditional homebuying and “lease-purchase” processes

Traditional homebuying process	Private lease-purchase option (also called rent-to-own)	Tenant purchase option
No rental period required before purchase	Rental period required before purchase	Home is a rental for 15 years before purchase option becomes available
Not typical for tenants to live in home before buying	Tenants have typically lived in the home for at least one year	Tenants have typically lived in the home for several years
Purchase price negotiated between buyer and seller	Purchase price set in lease-purchase contract	Purchase price set by project owner
Purchase price not based on income	Purchase price not based on income	Purchase price must be affordable to low-income households
Typically a competitive process with multiple potential buyers	Noncompetitive process once contract signed	Noncompetitive process
Buyers must obtain financing (down payment, mortgage pre-approval)	Buyers must obtain financing (down payment, mortgage pre-approval)	Buyers must obtain financing (down payment, mortgage preapproval)
Homeownership classes not required	Homeownership classes not required	Project owner may require buyers attend homeownership classes
Purchase typically includes both the home and land	Purchase typically includes both the home and land	Purchase of home may exclude the land in tribal developments
Typically no other parties beyond buyer and seller	Typically no other parties beyond buyer and seller	Other involved parties: development’s financial partner, Bureau of Indian Affairs

Source: Auditor prepared based on general information and Housing Finance Commission documents.

### Project owners are responsible for completing multiple steps before interested tenants can buy their homes

Even after homes have been available to rent for 15 years, multiple steps remain before tenants can purchase them. This process to sell and transfer the homes must be initiated by the project owner. First, the project owner must remove the financial partner from the project so that the project owner – typically a nonprofit or similar tax-sheltered organization – is the only legal owner of the home. This step allows the project owner to transfer ownership to tenants without the additional taxes incurred by private home sales. This must happen before project owners can offer homes for sale to tenants.

Project owners must then provide tenants the option to purchase their homes, which includes preparing tenants for the financial obligations of homeownership. Project owners may have their own requirements for determining if tenants are eligible to buy their homes, which they must complete before offering homes for sale. Project owners may offer homeowner education classes, either optionally



or as a condition for purchase, covering topics that include home maintenance, budgeting and financing. Budgeting and finance information can help tenants understand how to save for a down payment and obtain a mortgage, either through a traditional bank or other lender.

Finally, homes located on tribal lands have legal complexities that must be resolved before the project owner can sell them. Because tribal developments are built on land held in trust for the tribe by the federal government, the land must be legally separated from the building before the house can be made available for sale. This step typically calls for the involvement of the Bureau of Indian Affairs – a layer of bureaucracy few other property sales incur.

In summary, the process to sell and transfer homes to tenants can be complex, and only starts when a project has been available to rent for 15 years. As a result, it may take significantly longer before tenants are able to actually take ownership of their homes if they are interested.

# Background

## The Housing Finance Commission manages the LIHTC program in Washington

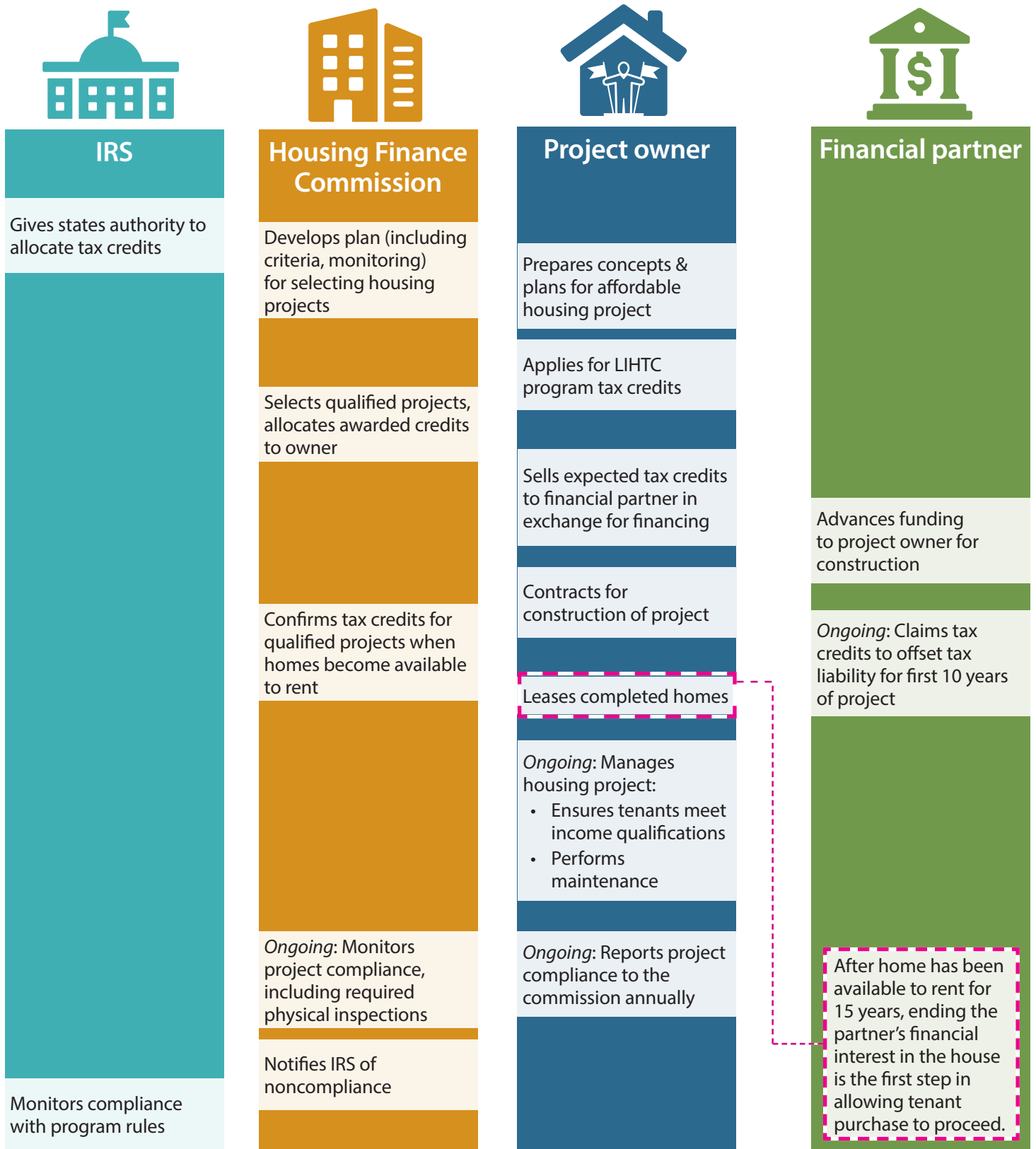
The Washington State Housing Finance Commission administers the state's LIHTC program. The agency is responsible for determining how to allocate tax credits to housing projects and ensuring that approved projects follow federal requirements.

**Allocating tax credits.** The commission uses an annual, competitive application process to allocate tax credits to proposed housing projects. Applicants self-score their applications and commission employees review them based on the state's priorities for housing development. For example, the commission gives preference to projects that serve the lowest income tenants, serve low-income tenants for the longest periods, and are located in certain census tracts. They also consider whether the development has set aside homes for people who are elderly, disabled or recently homeless. The commission allocated an average of \$21.1 million annually to about 12 new projects with 950 homes each year for the last four application cycles (2021-2024).

**Ensuring compliance with federal rules.** After awarding tax credits, the commission must ensure that project owners follow program rules that include verifying tenants remain eligible for low-income housing, charging the correct amounts for rent, and conducting home inspections. Commission staff verify tenants' eligibility and that rent payments are within LIHTC program limits annually; building inspections must take place at least once every three years.

**Exhibit 2** (on the following page) illustrates the commission's role in overseeing the LIHTC program. See the primer on tenant purchase for more information on the roles of project owners, financial partners and the IRS.

**Exhibit 2 – Low-Income Housing Tax Credit (LIHTC) program roles and relationships**



Source: Auditor prepared based on information from the Housing Finance Commission and the Congressional Research Service

## LIHTC affordable housing projects offering tenant purchase options are rare

Projects with tenant purchase options represent a very small share of all LIHTC projects in Washington. Only 18 of the state's nearly 1,300 LIHTC projects offer tenant purchase options; all but one are managed by tribal governments. Using tenant purchase options can help the tribes preserve affordable housing and increase the overall wealth of tribal members. These developments are usually single-family homes, which can increase homeownership among tribal members where there are otherwise limited opportunities to do so.

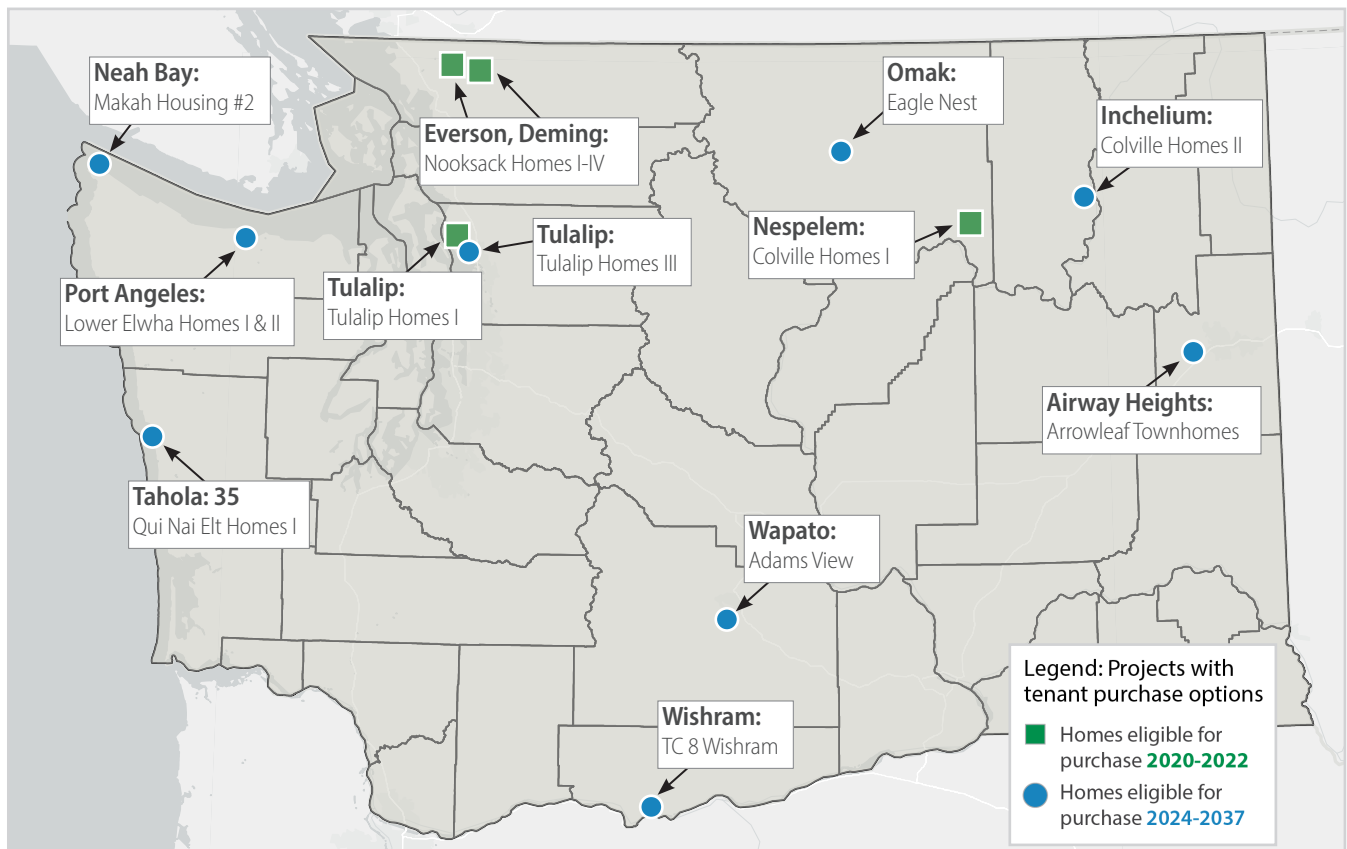
Of the 18 projects, just six — across three counties, with a combined total of 135 homes — had properties old enough to qualify for tenant purchase as of 2023. (See the sidebar for a note about project numbers.) The oldest buildings qualified for tenant purchase in 2020. By 2030, around 250 homes, from an additional seven housing projects in six counties, will become eligible for tenant purchase. The map in Exhibit 3 shows the locations of housing projects with tenant purchase options.

### A note about total project numbers

Two of the 18 projects did not include tenant purchase options in their LIHTC applications, but asked the commission to incorporate their intentions several years after winning the tax credits. We included these two projects here to calculate the total number of homes available, but not in our review of the high-level plans developed by project owners.

### Exhibit 3 – Map of projects with tenant purchase options

Homes eligible for purchase in ■ 2020-2022 and ● 2024-2037



Source: Housing Finance Commission data.

## Evictions at the Nooksack Indian Tribe drew attention and concerns from lawmakers and others

Evictions at housing projects managed by the Nooksack Indian Tribe raised concerns about tenant purchase options and, more widely, the LIHTC program managed by the commission. Starting in 2013, the Nooksack Indian Tribe began the process of disenrolling a group of about 300 tribal members. In 2018, the tribe completed the disenrollment process, which meant these people were no longer eligible for tribally operated programs, including housing managed by the Nooksack Housing Department. Following the disenrollment, the tribe moved to evict some of the former members from homes built with LIHTC funding and that incorporated tenant purchase options.

Lawmakers and others expressed concern that disenrollment meant that tenants lost the option to buy homes that had reached the end of the required 15-year rental period between 2020 and 2022. Several lawsuits were filed to stop the evictions, but the Washington State Supreme Court and federal courts have declined to hear those cases, citing the sovereignty of tribal governments to determine who is eligible for tribal membership and programs, including housing.

This audit did not evaluate the decision to evict tenants who lived in housing managed by the Nooksack Housing Department for two reasons. First, tribal governments are sovereign entities, and their finances and programs (with limited exceptions around tribal schools) are outside the audit authority of the State Auditor's Office. Second, the evictions are the subject of ongoing lawsuits. Rather, we focused our audit on the Housing Finance Commission because it is the state agency that oversees housing projects with tenant purchase options.

## This audit examined the Housing Finance Commission's oversight of housing projects that offer tenant purchase options

Legislators asked the State Auditor to look into whether projects with a tenant purchase option did actually deliver on the promise of giving tenants the opportunity to buy eligible homes. They have also raised questions about the commission's compliance with federal and state laws and regulations, and whether it provides sufficient oversight of housing projects that include tenant purchase options.

The audit answered the following questions:

1. Has the Housing Finance Commission followed applicable federal and state laws related to financing and overseeing housing projects that offer tenant purchase options?
2. What benefits have tenants in projects with a tenant purchase option received related to affordable housing and homeownership?
3. How could the Housing Finance Commission improve tenant outcomes for projects with tenant purchase options?

# Audit Results

## The Housing Finance Commission met legal requirements, but improved oversight could better support homeownership

### Results in brief

The commission met legal requirements related to tenant purchase options. It awarded points for tenant purchase in project applications for most of the audit period in accordance with its policies. Although the commission temporarily suspended application points for tenant purchase options during the 2023-24 application cycle, no projects expressed interest in using the option during that time.

Although the commission met legal requirements, its monitoring activities were ineffective for ensuring project owners' progress toward tenant purchases. For example, the commission did not follow its own plan for monitoring project owners' progress in that area. However, commission staff said they have few options to respond to project noncompliance beyond reporting it to the IRS.

Finally, the commission did not develop sufficient guidance for project owners to implement tenant purchase options. Project owners said they would appreciate additional guidance that clarifies the commission's expectations.

## The Housing Finance Commission met legal requirements related to tenant purchase options

Federal and state laws place few requirements on the commission's oversight of housing projects with tenant purchase options. **Exhibit 4** (on the following page) lists the criteria under federal law that state housing finance agencies are expected to follow; they must include tenant purchase options as part of their application criteria.

### Exhibit 4 – Tenant purchase options are just one element federal law requires state agencies to consider

- Project location
- Housing needs characteristics
- Project characteristics, including whether the project uses existing housing as part of a community revitalization plan
- Tenant populations with special housing needs
- Sponsor characteristics
- Public housing waiting lists
- Tenant populations of individuals with children
- Projects intended for eventual tenant ownership
- Energy efficiency of the project
- Historic nature of the project

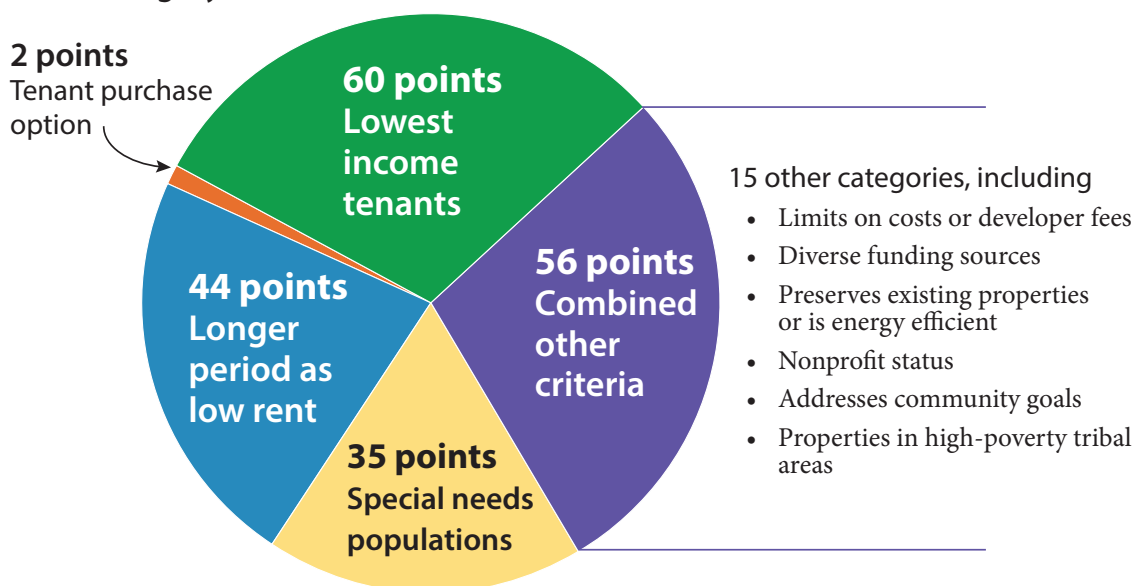
Source: 26 USC 1.42 (Internal Revenue Code, “low-income housing credit” section).

State regulation uses similar language. These laws do not specify how the commission should implement and oversee such options beyond what is required for all Low-Income Housing Tax Credit (LIHTC) projects, which include annual income verifications and building inspections every three years.

### The commission awarded points for tenant purchase in project applications in accordance with its policies

The commission included the tenant purchase option as part of its application process and awarded points for such projects. Federal and state laws do not specify how states should prioritize or weight the criteria; commission policies use application points to incentivize projects that meet these criteria. Exhibit 5 shows a breakdown of how Washington allocates about 200 total points; the exact amount of points depends upon the location of the project.

### Exhibit 5 – Maximum application points the Housing Finance Commission awards for each category



Source: Housing Finance Commission policies.



About half of the total points are allocated for serving the lowest income tenants (60 points) and serving low-income tenants for the longest periods (44 points). Most of the remaining points are awarded based on how the project addresses other community needs, such as serving those who are disabled, or government priorities such as limiting developer fees. The commission allocates two points for tenant purchase options.

Commission staff said they have received 24 applications that proposed tenant purchase options. We reviewed five of those applications: all received two points, consistent with state regulation and the commission's policies.

***Although the commission temporarily suspended application points for tenant purchase options, no projects expressed interest in using the option***

The commission decided to suspend points for tenant purchase options for the 2023-24 application cycle. Applicants could still include a tenant purchase option if they chose. However, commission staff said that no one proposed new housing projects with the option, either formally through an application or informally through discussions. Commission employees said they paused the application points while they finished developing new processes and guidelines for applicants. The commission developed new policies and procedures for new projects and reinstated application points for tenant purchase options for the 2024-25 application period.

**Although the commission met legal requirements, its monitoring activities were ineffective**

IRS oversight of the LIHTC program offers state agencies only minimal guidance for managing the program generally or tenant purchase options specifically. Federal audits conducted by the Government Accountability Office and the Treasury Inspector General of Tax Administration identified lack of oversight to states as an ongoing issue. Commission staff also said they lack federal guidance or best practices for projects with tenant purchase options. Nevertheless, the commission is responsible for providing effective program oversight in Washington.

We reviewed leading practices from the federal government, such as the Government Accountability Office and the U.S. Department of Housing and Urban Development to identify how the commission could improve its project monitoring.

**The commission did not follow its own plan for monitoring project owners' progress toward tenant purchases**

Although the commission included a monitoring schedule in its formal agreements with project owners, it did not take steps to execute it. The agreements required project owners to submit an update on their progress toward fulfilling tenant

purchase options no less than once every five years, and at the commission's request. However, our review showed that none did so, and the commission did not request updates until 2022, which meant the commission was unaware of project owners' progress throughout the required 15-year rental period.

The commission did not ensure it received project updates for four main reasons:

- **No policies or procedures.** The commission lacked policies and procedures related to monitoring tenant purchase options. Employees did not have clear expectations about what project owners should include in their progress updates, how to request updates or what their review of these updates should examine.
- **Timing issues.** The timing of the proposed monitoring schedule (every five years) did not align with the commission's other existing monitoring processes for verifying tenant eligibility and conducting building inspections. This off-cycle schedule was difficult for employees to administer, especially without clear procedures to follow.
- **Other program priorities.** Although one employee raised the lack of progress updates as an issue in 2016, commission managers said their focus during the first 15 years is on compliance with tax program rules that take priority, such as ensuring tenants meet income eligibility requirements and that project owners comply with health and safety standards.
- **COVID-19 pandemic.** The first properties to reach eligibility for tenant purchases did so during the public health emergency, which disrupted business across all LIHTC properties. Commission managers said that during this time, federal agencies issued several compliance waivers to prioritize the health and safety of residents and staff, which added complexity to administering the program.

Housing commission officials said they took a hands-off approach for the first 15 years that tenant purchase options were part of the LIHTC application. The commission focused on compliance requirements that applied to all LIHTC projects and not specifically on tenant purchase outcomes, which affect relatively few projects. For example, managers said they prioritized making sure all homes were being rented and that all tenants met the program's income requirements. They reasoned that even if tenants could not or did not buy a home, tenants would remain in affordable rental housing. They saw this as a positive outcome consistent with the program's main purpose. We discuss the topic of other positive outcomes in Chapter 2.

The commission revised its policies and procedures to better incorporate tenant purchase options into its existing monitoring process during the audit. It has incorporated new requirements concerning project updates and monitoring into its policies and project application, and created a guide for project owners and tenants. Project owners will be required to provide regular updates on their progress toward achieving their tenant purchase plans. They must submit an annual certification

confirming compliance during the project's first 12 years, a more detailed update in year 13 (such as how many tenants intend to buy their homes) and home inspections in year 14 and complete any needed home repairs before sales can proceed. Project owners will also be required to include information about tenant purchase options in its lease agreements. The commission is implementing these changes for the 2024-25 application cycle. The commission had already implemented some of these changes with existing projects in 2022.

### ***Commission staff said they have few options to respond to project noncompliance***

The LIHTC program has few enforcement options for state housing finance agencies when project owners are not following program rules, according to commission staff. The primary tool available is to report noncompliance to the IRS. Commission staff said the IRS is more likely to act during the first 15 years, before the financial partner exits the project, because it can require the financial partner to pay back the tax credits. Staff also said that after the first 15 years, the IRS can no longer apply this penalty and is therefore less likely to follow up.

Commission staff reported two projects to the IRS during the audit period because the owners did not provide updated information as requested. According to commission staff, one project did provide updated information, but the other had not. The commission did not receive any direct response from the IRS and is unaware of any actions the IRS may have taken.

## **The commission did not develop sufficient guidance for project owners to implement tenant purchase options**

In their project applications, project owners were required to include a high-level plan of how they will fulfill tenant purchase options. The 16 projects that included the option in their initial applications complied with this basic requirement. Most incorporated general information about their timelines and processes for tenant purchase, including tenant eligibility requirements and legal steps that the project owner and tenant must take. However, the plans lacked specific information in part because the commission's applications did not require them to do so. None set out how tenants would indicate their interest in buying a home, when the process begins or how long it was likely to take. Lacking such information, tenants could find it difficult to decide whether they should exercise the purchase option or how to start the process. By ensuring applicants make their plans specific and clear at the outset, and explaining clearly how they will communicate the plans to their tenants one day, the entire process would become more transparent for tenants.

The commission's application policy set out only general requirements for the information tenant purchase plans should include but did not specify details; neither did the guidance made available to project owners. Project owners were encouraged to contact the commission during the application process if they wanted to include tenant purchase options.

***Project owners would appreciate additional guidance that clarifies the commission's expectations***

Only three of the nine project owners with tenant purchase options had homes that had been available to rent for 15 years during the audit period, making them eligible for sale. We spoke with three project owners to learn what information they shared with tenants, and their views on guidance or instructions they received from the commission. Two said they had given tenants some general information about the option but not specific details. The third owner had not given tenants any information because the homes had only recently been available to rent, and the COVID-19 public health emergency had affected their normal move-in processes. In addition, two of them said they would appreciate more guidance from the commission, such as training or a sample tenant transfer plan, because tenant purchase was a relatively new process for them. Even though some project owners have managed other federally funded homeownership programs, none had completed the process as part of the LIHTC program.

During the audit, commission staff updated project owner guidance materials to provide clearer expectations around tenant purchases while also giving them flexibility in developing their plans. Staff also said they were working with project owners with existing projects to fully develop their tenant purchase plans.

## Although the LIHTC program has not yet produced any homeowners, tenants have received other meaningful benefits

### Results in brief

Project owners have yet to sell and transfer the 135 eligible homes to tenants. This appears inconsistent with formal agreements between the project owners and the commission, although the complex process to prepare for home sales means some delay before tenants can take ownership of their homes could be expected. Commission officials also pointed to limitations in their ability to compel project owners' actions.

Project owners we spoke with described a variety of challenges they faced in preparing for tenant home purchases, including unclear requirements and limited guidance.

Tenants we interviewed saw benefits to homeownership but also possible challenges. Their understanding of purchase options varied, and most wanted more information about how the program worked. Tenants who want to purchase their homes may face systemic financial barriers. Despite these barriers to homeownership, LIHTC projects provide affordable rental housing to disadvantaged communities, even if tenants do not buy eligible homes. These income-restricted housing options directly benefit communities through increased housing supply and below-market rents.

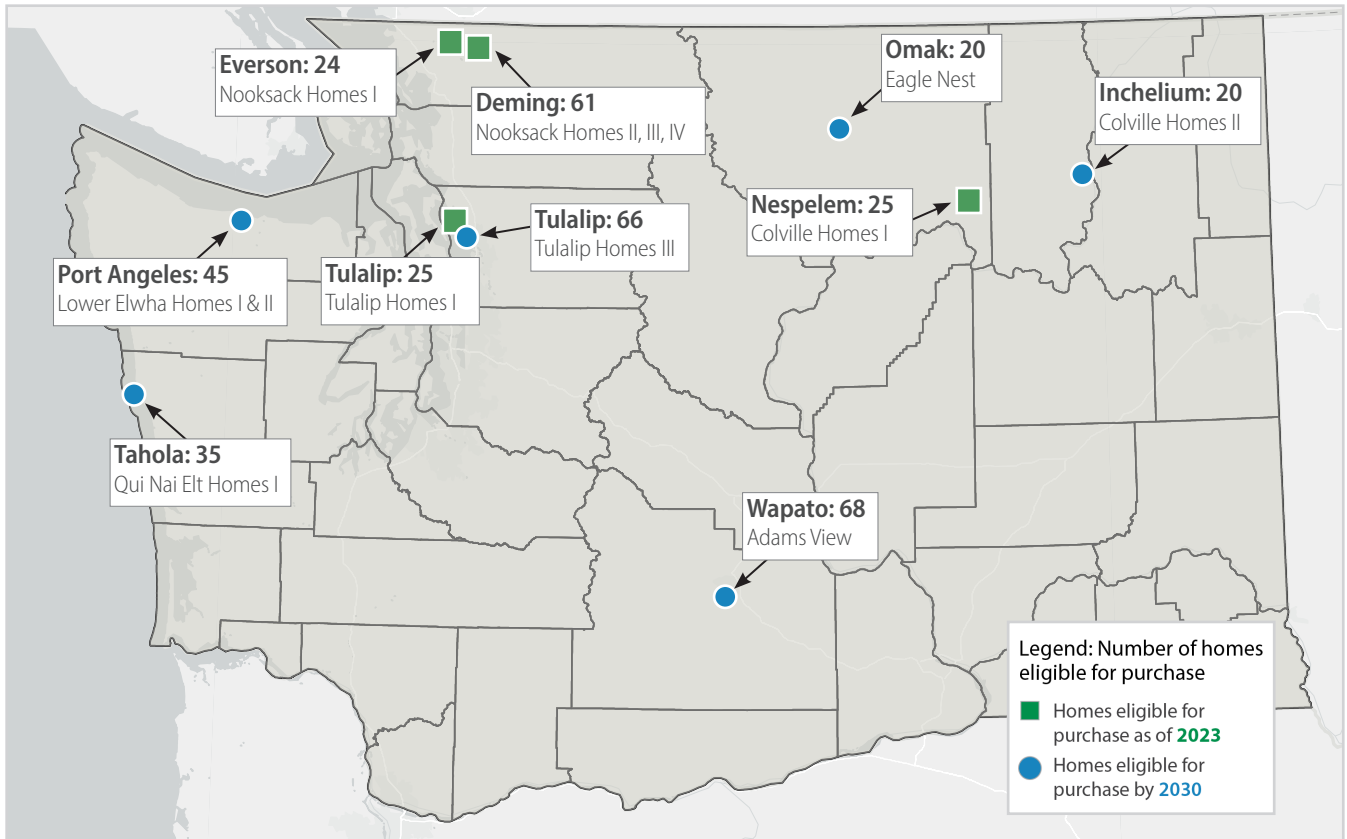
## Project owners have yet to sell and transfer the 135 eligible homes to tenants

As of 2023, 135 homes – across six developments in three counties (Okanogan, Snohomish, Whatcom) – qualified for sale, meaning they had been available to rent for 15 years under the LIHTC program. However, commission staff confirmed that no project owners had sold and transferred eligible homes to their tenants yet.

An additional 254 homes will become eligible by 2030. Between those already eligible and those entering availability by 2030, 389 homes will be eligible for tenant purchase in 2030. The map in **Exhibit 6** (on the following page) shows their locations and the number of eligible homes.

**Exhibit 6 – Number of homes eligible for tenant purchase options**

Homes eligible for purchase ■ as of 2023 and ● by 2030



Source: Housing Finance Commission data.

Although the lack of home sales so far has not violated any laws or regulations, it appears inconsistent with the formal agreements between the commission and project owners. The agreements stated that project owners would transfer all homes to “tenant ownership” after they had been available to rent for 15 years.

There are some extenuating circumstances that help explain this apparent inconsistency. First, as described in the Primer, the process of tenant ownership itself is complex, and can only commence after the first 15 years of a project has been completed. Some delay before tenants can take ownership of their homes could therefore be expected. Second, commission officials said they have limited ability to compel the project owners’ actions beyond reporting them to the IRS. However, as discussed earlier in the report, the commission did not monitor project owners’ progress toward preparing the homes for sale, which could also have contributed to this delay.

### ***Project owners described challenges in preparing their projects for tenant purchases***

In interviews, two project owners described a variety of challenges they faced in preparing for tenant home purchases including unclear requirements and limited guidance. One did not start preparing for tenant purchases until homes they managed became eligible for sale, because other aspects of the project took attention away from the tenant purchase option. A second, whose homes were not yet eligible for sale, was taking time to prepare tenants thoroughly, due to past problems experienced with a different homeownership program. Although we reached out to another project owner that had reached the purchase eligibility date, we did not receive a response.

More generally, commission officials said that processing individual home sales to tenants created a meaningful administrative burden for project owners. They also said that although few other states had achieved any tenant purchases, two important factors that could improve the likelihood of success were clear communication about the option from project inception and ongoing coaching support for owners.

## **Tenants we interviewed saw benefits to homeownership but also possible challenges**

We held two small focus groups with nine or fewer tenants to gain their perspectives on the tenant purchase option. One group met in eastern Washington, with people living in homes managed by the Yakama Nation Housing Authority, the other in western Washington with people living in two projects managed by the Lower Elwha Housing Authority. We discussed topics including their awareness of the tenant purchase option, how realistic buying their home felt, and what additional information or support they would want to help them make decisions around homeownership. We offered participants reasonable compensation for their time and contributions to the conversation. See Appendix B for more information about the focus groups.

### **Interested in homeownership, but with some concerns about feasibility**

Several tenants in both groups said they were interested in owning their home, with some more committed to the idea than others. Some were explicit about their intent to buy a home, and even shared plans for future renovations. Others seemed cautiously interested, saying they needed more information about the purchase process and price.



Quotes appearing in *italics* in this section of the report are drawn from conversations held during the two focus group sessions.



However, the two groups had significantly different opinions about the feasibility of owning their own homes. Most in the western Washington group felt that ownership was a realistic goal; those in eastern Washington were more doubtful for a variety of reasons. People in the former group were five or less years away from home purchase eligibility and had already experienced some homeowner preparation training, which helped them feel more confident that homeownership was within reach. People in eastern Washington lived in homes only a few years old, and had not received any homeowner training. Participants at both locations expressed frustration about the long timeline to ownership: up to 15 years of rental payments to make until the home became eligible, plus taking on a mortgage. They were also uncertain about their future circumstances.

*“Half of us here are over 50. This is our first opportunity to even rent-to-own. We don’t see us living that long.”*

### **Their understanding of purchase options varied, and most wanted more information about how the program worked**

The two focus groups displayed very different understandings of the tenant purchase option. Most people in the western Washington group said they had received information about the option to buy a home, but many of those in eastern Washington were much less clear about the option to buy their homes and how to participate. For example, two believed their homes were rentals only, saying nothing had been said to them about buying a home. Three other people knew that ownership was possible but had limited and varied understandings of how the process worked.

*“I thought it was Section 8 and we would just be renters.”*

*“I thought I’d just be renting. I never heard anything about rent to own, or eventually have the option to own.”*

### **Information tenants felt would make them more confident as potential buyers**

Aside from the general information they may have received from their project’s owner, tenants wanted answers to specific issues to better determine if they wanted to purchase their homes. And most tenants wanted the answers in a written format they could review and consider without pressure. The following are examples of the types of questions they raised:

- **Financing.** How are house prices determined? How much will my house cost? How much would I need for a downpayment, if any? How would I obtain a mortgage, and would changes in my income affect mortgage payments? Would property insurance be included in my mortgage?



- **Title for the home.** How does being located on tribal land affect homeownership? How are property lines set and adjusted? Could my family members or relatives inherit the house after my death?
- **Actual purchase process.** When and how will I be notified that homes are eligible to buy? What steps would be involved in purchasing, and how long would it likely take?
- **Homeownership education.** Where can we learn more about budgeting to help save for buying our home? What should we know about ongoing maintenance activities and costs currently handled by the project owner?

*“Financials is a big piece for me. I’m a single income parent of two. Making sure cost is affordable, not needing to work multiple jobs to pay for the mortgage.”*

*“I have a daughter, grandson and granddaughter that would like to own my house if I die, but I’m not sure who will get it.”*

Project owners are responsible for providing the information and support tenants need to understand their purchase option. But our interviews with project owners showed that they would welcome additional guidance because tenant purchase was a relatively new process for them. The previous chapter suggests ways the commission can help by providing guidance for more detailed and transparent tenant transfer plans.

## Even tenants who want to purchase their homes may face systemic financial barriers

Even if they were eager to buy a LIHTC home, low-income tenants served by these housing projects are likely to face barriers to homeownership. Additional costs paired with the long timeline to purchasing, as listed below, could reduce the incentive for tenants to buy their home.

- **Higher monthly costs.** Most project owners in Washington plan to offer homes for sale so that mortgage payments are no more than 20% higher than tenants’ monthly rent. Tenants on fixed incomes may not be able to afford home maintenance costs, previously covered by the project owner, on top of the higher cost of a mortgage.
- **Modest incentives to buy.** There may be less incentive for tenants to purchase depending on how project owners determine the purchase price. For example, 10 of the 12 tenant purchase plans we reviewed offered incentives based on the number of years a person has rented – a limited benefit for newer renters moving into a home that is just a few years away from eligibility. A 30-year mortgage after a lengthy rental period may also limit the incentive to purchase, especially for older tenants.

- **Difficulty saving for a down payment.** Tenant households generally earn less than half of the median income for households in their area, limiting their disposable income. These households may therefore have difficulty saving up for even a small down payment.
- **Lack of financial experience.** Tenants may have limited experience with homeownership and financial processes. For example, one focus group participant said they did not have a credit history because they had only recently obtained a credit card. Another said they had good credit but did not know where to start the process of securing a home loan. Lack of financial experience may make it difficult for tenants to obtain mortgages or affordable mortgage rates.

Finally, some tenants may simply not want to become homeowners. In fact, the project owners we interviewed said they expected as much. Even though homeownership for tenants is a goal of these projects, project owners do not necessarily screen for tenants who will want to become homeowners. It is therefore reasonable to expect that some homes that are eligible for purchase would remain as rentals.

## LIHTC projects provide affordable rental housing to disadvantaged communities, even if tenants do not buy eligible homes

### Income-restricted housing options directly benefit communities through increased housing supply and below-market rents

As of 2023, about 500 tenants lived in the six housing developments mentioned at the start of this chapter. We estimated another 1,000 people live in the additional 250 homes that will become eligible by 2030. These 1,500 people may or may not be able to take advantage of the tenant purchase option when it arises, but Washington LIHTC projects approved through the commission provide other benefits to their tenants.

Disadvantaged communities benefit when project owners build quality, income-restricted homes in their neighborhoods. Households in these projects earned less than half the area median income, on average, so income-restricted housing may be the only feasible option for them. In addition, people who are disabled or were recently homeless occupy about 40% of the homes in these projects: the commission encourages project owners to designate housing that serves these populations. Finally, these projects can provide safe, quality housing in areas with few alternatives. For example, one project owner said the project was adding housing to a location where most other homes were aging and dilapidated.

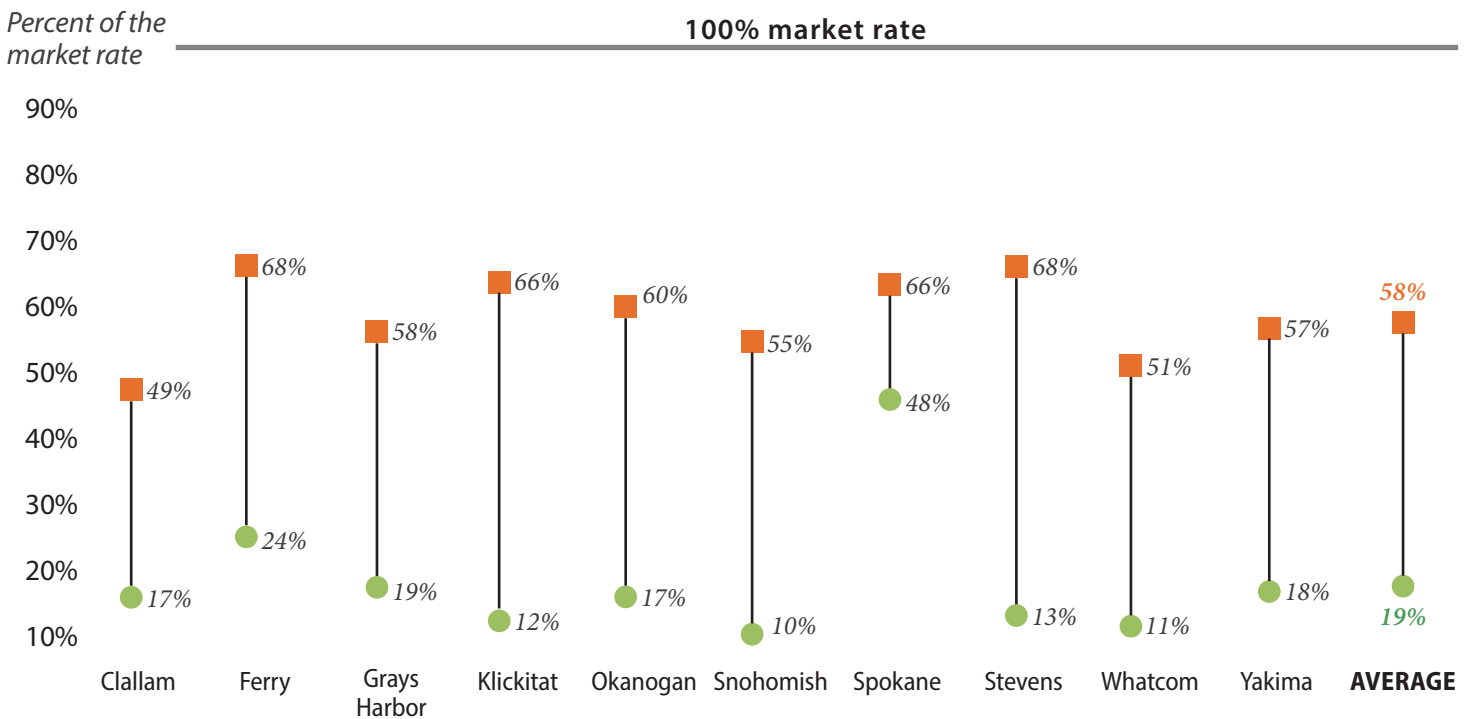
*“I will say the roofing on these is very high quality on these houses. I was amazed. They’re great houses to get into. It doesn’t look like anyone skimped on materials when they built. There’s just typical new house stuff. There’s no way we could afford to get out in the world on the incomes we have.”*

### Tenants paid significantly less rent than they would for private housing

Even if tenants do not buy homes in the projects we looked at, they have nonetheless benefited from below-market rent. Not only do LIHTC regulations cap rents based on area median incomes, tribal tenants may also receive housing subsidies from other programs that reduce their out-of-pocket rent payments. Through a combination of these sources, tenants paid on average less than 20% of market-rate, with Snohomish County tenants paying only 10%. Even tenants living in the only non-tribal project with a tenant purchase option, in Spokane County, paid just under half the market-rate rent. Exhibit 7 illustrates the difference between what tenants paid out of pocket and the maximum project owners could theoretically charge for rent. Although we could not determine how much each factor – rent regulations and outside subsidies – individually contributed to reducing rent due to data limitations, both helped tenants pay less than market rates.

#### Exhibit 7 – Tenant rent as a percentage of local market-rate rents

Range shows ■ maximum allowable rent charged compared to ● typical rent paid out of pocket by tenants



Source: Auditor prepared using data from the Housing Finance Commission.

# State Auditor's Conclusions

At the highest level, the findings of this performance audit are disappointing. An option for tenants in affordable housing projects to buy their homes has not yet been used, despite applying to 135 housing units in 2023.

This failure to deliver on the possibility of homeownership is not the result of state management, however. The state Housing Finance Commission has followed the rules for the tenant purchase option in the federal Low-Income Housing Tax Credit Program.

We found the tenant ownership option is little-known and largely misunderstood. It is not, as it has sometimes been called, a “rent-to-own” program. Though a property must be available to rent for 15 years to become eligible for the purchase option, tenants are not obliged to buy their homes, nor are they automatically transferred from rental agreements to purchase contracts. Indeed, the legal path from renting to purchasing these homes appears quite complex.

I'm particularly proud of our auditors' work to gain a ground-level understanding of the program by meeting with groups of property renters in tribal housing projects. We found that tenants had limited information about the purchase option and wanted to know more. Similarly, we found project developers would like more information about the option and its goals.

In my view, it is telling that auditors could find little information on the federal intent behind including a relatively small incentive for the ownership option in housing projects that otherwise focus on rental units. As our recommendations show, this tenant ownership option needs greater clarity – in communicating how it works, what tenants' options are, and the goals of policy makers in offering it.

# Recommendations

## For the Housing Finance Commission

To help ensure that project owners make progress toward fulfilling the tenant purchase options they agreed to in their applications, as described on pages 17-19, we recommend the Housing Finance Commission:

1. Continue to improve the current process for monitoring project owners' progress toward fulfilling their tenant purchase plans. The process should include:
  - a. Establishing a process for project owners to provide progress reports on their plan implementation
  - b. Setting a reporting frequency for progress reports that ensures changes are reported in a timely manner and that aligns with other existing monitoring processes
  - c. Documenting the reporting process and frequency in written policies and procedures

To address the need for clearer guidance around project plans for tenant purchase options so project owners can more effectively meet program goals, as described on pages 19-20:

2. Develop guidance to provide clearer expectations to project owners on how to develop and implement their tenant purchase plans. Guidance materials can include printed documents and templates as well as training. This guidance should identify information to incorporate into the tenant purchase plans. Elements that could be included:
  - A timeline for when the project owner will provide tenant education and when homes will be available to buy
  - The method for calculating the selling price of eligible units
  - Expected tenant communication, including:
    - The timeline and necessary steps for the homebuying process
    - Information about the purchase price and any other financial obligations tenants should anticipate
    - The content and timing of homeownership education classes provided by the project owner
    - Other terms and conditions of homeownership, such as whether the buyer could transfer their homes to family members and details about land ownership on tribal trust lands

# Agency Response



*Opening doors to a better life*

Nicole Bascomb-Green  
*Chair*

Steve Walker  
*Executive Director*

November 12, 2024

Honorable Pat McCarthy  
Washington State Auditor  
P.O. Box 40021  
Olympia, WA 98504-0021

Dear Auditor McCarthy:

Thank you for the opportunity to review and respond to the State Auditor's Office (SAO) performance audit on tenant purchase options under the Low-Income Housing Tax Credit (LIHTC) program.

We agree that it is unfortunate that no units have yet been sold and that improvements to our process and compliance oversight were needed to better prepare owners to offer units for sale to tenants after year 15. Over the past two years, since realizing this need, we have worked as closely as possible with the owners of LIHTC properties with the eventual tenant ownership option (referred to as tenant purchase option in the report) to support owners' progress towards fulfilling this commitment.

As the result of a two-year effort, we have also implemented a comprehensive new framework to support implementation, with policies and procedures that align with the auditors' recommendations.

In January 2023, our staff embarked on a process to research and analyze the LIHTC eventual tenant ownership option, soliciting guidance from other states and project consultants as well as feedback from project owners. An internal report completed in November 2023 outlined recommendations to improve implementation, and a staff work group was formed to turn those recommendations into policies and procedures for LIHTC applicants, project owners, and our own compliance staff.

This ongoing work was completed in 2024, while the performance audit was being conducted, and the new policies and procedures were fully implemented this fall. We expect to update them further in the coming year, as eligible projects begin to sell and convert rental units to homeownership.

We greatly appreciate your team's work on this audit. We are committed to ongoing evaluation and continuous improvement to achieve affordable housing outcomes for residents.

If you have any questions or concerns, please contact Jackie Moynahan at [Jackie.moynahan@wshfc.org](mailto:Jackie.moynahan@wshfc.org).

Sincerely,

A handwritten signature in blue ink that reads "S Walker".

Steve Walker  
Executive Director  
Washington State Housing Finance Commission

## **Official Response to Performance Audit Housing Finance Commission: Tenant purchase options under the Low-Income Housing Tax Credit Program – November 12, 2024**

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The Washington State Housing Finance Commission provides this management response to the State Auditor’s Office (SAO) performance audit report received on October 14, 2024.

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### SAO Performance Audit Objectives

The SAO’s performance audit addressed three questions:

1. Has the Housing Finance Commission followed applicable federal and state laws related to financing and overseeing housing projects that offer tenant purchase options?
  2. What benefits have tenants in projects with a tenant purchase option received related to affordable housing and homeownership?
  3. How could the Housing Finance Commission improve tenant outcomes for projects with tenant purchase options?
- 

Recommendations to the Commission in brief:

**SAO Recommendation 1:** Continue to improve the current process for monitoring project owners’ progress toward fulfilling their tenant purchase plans. The process should include:

- a. Establishing a process for project owners to provide progress reports on their plan implementation
- b. Setting a reporting frequency for progress reports that ensures changes are reported in a timely manner and that aligns with other existing monitoring processes
- c. Documenting the reporting process and frequency in written policies and procedures

### **STAFF RESPONSE:**

We appreciate and agree with the recommendation to improve our monitoring processes to support project owners’ progress towards fulfilling their commitments to make units available for sale to residents beginning at the end of the 15-year compliance period. Our 2024 policy updates include a defined process and procedure for owners to submit progress reports throughout the compliance period. This process is aligned with existing monitoring processes to streamline the additional reporting requirements. Included below are the specific actions we have already taken that address Recommendation 1 a-c.

### Action Steps and Time Frame

We have completed improvements to our monitoring and reporting requirements for projects that elect the tenant purchase option (referred to below as eventual tenant ownership) in the following ways:

- **Recommendation 1 a & b:** As part of the owner’s annual report submission each January 31, the owner is now required to confirm in the Owner Annual Certification their compliance with the project’s Eventual Tenant Ownership Conversion Plan. Starting when the project reaches year 13, the owner must submit a report describing progress towards implementing the Conversion Plan, including, but not limited to, the number of eligible tenants who have received homebuyer, budget, and financial education and counseling. *Completed*

- **Recommendations 1c:** These updated requirements are documented in several places:
- Section 6.20 of the 2025 9% Tax Credit Program policies, and posted on our website here [9% Competitive Housing tax credit policies \(wshfc.org\)](https://wshfc.org). *Completed. Effective August 2024*
  - Section 4.24 of the regulatory agreement for any new projects. *Completed. Effective August 2024*
  - In a new 9% Housing Credit Program Eventual Tenant Ownership Guide which is publicly available on our website here: [3\\_ETO Guide v1.0.pdf \(wshfc.org\)](#). *Completed. Effective August 2024*
  - A new section in the Tax Credit Compliance Procedures Manual has been completed and will be posted on the Commission's website by November 30, 2024.
  - An updated LIHTC Owner's Annual Certification form has been completed and will be posted on the Commission's website by December 2024. Owners will start using this immediately.
  - An updated Lease Rider Form is completed and will be on the Commission website by November 30, 2024. It will be effective on 1/1/25 for new residents and at recertification for existing residents.

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**SAO Recommendation 2:** Develop guidance to provide clearer expectations to project owners on how to develop and implement their tenant purchase plans. Guidance materials can include printed documents and templates as well as training. This guidance should identify information to incorporate into the tenant purchase plans. Elements that could be included:

- A timeline for when the project owner will provide tenant education and when homes will be available to buy
- The method for calculating the selling price of eligible units
- Expected tenant communication, including:
  - The timeline and necessary steps for the homebuying process
  - Information about the purchase price and any other financial obligations tenants should anticipate
  - The content and timing of homeownership education classes provided by the project owner
  - Other terms and conditions of homeownership, such as whether the buyer could transfer their homes to family members and details about land ownership on tribal trust lands

**STAFF RESPONSE:**

We also appreciate and agree with this recommendation that both guidance and clear expectations are needed to support both project owners and residents. As part of our policy updates, we created a suite of new materials, including a new guide (also referenced in Recommendation 1), an application template, and updated requirements for the Lease Rider and Lease Addendum. The specific actions we have taken that collectively address Recommendation 2 are outlined below, with key components highlighted in bold.



### Action Steps and Time Frame

The suite of materials that are completed and now available include:

- A new 9% Housing Credit Program Eventual Tenant Ownership Guide which is publicly available on our website here: [3\\_ETO Guide v1.0.pdf \(wshfc.org\)](#). *Effective August 2024.*
  - The Developer/Property Owner Guidance Section, Conversion Plan Requirements beginning on page 5 outlines the requirements and provides guidance on: Resident Eligibility, **Purchase Price, Homebuyer Education Courses, Budgeting and Financial Counseling**, Maintenance and Inspections and Investor Exit Strategy and Encumbrances.
  - The Pre-Conversion Requirements Years 1- 15: Required Resident Forms section on page 8 includes a newly required ETO Lease Addendum **to provide clear written communication to residents about the tenant purchase option, including but not limited to the property's specific resident eligibility and purchase requirements, the purchase price and/or purchase price methodology, and any other terms and conditions.**
  - The Resident/Potential Homeowner Guide section, starting on page 11, informs residents of **required documentation regarding the tenant purchase option when a lease is signed and provides information on homeowner education, budgeting and financial counseling resources.**
  
- Developers interested in electing the eventual tenant ownership option (tenant purchase option) for any new project are also now **required to attend a Pre-Application Meeting to discuss their project and plans with Commission staff.** In addition, **we created a new application template to support project owners in submitting their conversion plan.** A copy of the application template can be found on page 14 of the 9% Housing Credit Program Eventual Tenant Ownership Guide. *Effective August 2024 for projects applying this year.*
  
- In addition, we have **outlined the process for converting units from rental to homeownership.** This is included in the Conversion Requirements section of the 9% Housing Credit Program Eventual Tenant Ownership Guide starting on page 9, and will also be reflected in the Tax Credit Compliance Procedures Manual. The outline includes **the timeline for readying units for sale, the process the property owner must take to sell and convey the units, and the requirement to gain approval from the Bureau of Indian Affairs for projects located on tribal trust land.** *Effective August 2024.*

# Appendix A: Initiative 900 and Auditing Standards

## Initiative 900 requirements

Initiative 900, approved by Washington voters in 2005 and enacted into state law in 2006, authorized the State Auditor’s Office to conduct independent, comprehensive performance audits of state and local governments.

Specifically, the law directs the Auditor’s Office to “review and analyze the economy, efficiency, and effectiveness of the policies, management, fiscal affairs, and operations of state and local governments, agencies, programs, and accounts.” Performance audits are to be conducted according to U.S. Government Accountability Office government auditing standards.

In addition, the law identifies nine elements that are to be considered within the scope of each performance audit. The State Auditor’s Office evaluates the relevance of all nine elements to each audit. The table below indicates which elements are addressed in the audit. Specific issues are discussed in the Results and Recommendations sections of this report.

I-900 element	Addressed in the audit
1. Identify cost savings	<b>No.</b>
2. Identify services that can be reduced or eliminated	<b>No.</b>
3. Identify programs or services that can be transferred to the private sector	<b>No.</b>
4. Analyze gaps or overlaps in programs or services and provide recommendations to correct them	<b>No.</b>
5. Assess feasibility of pooling information technology systems within the department	<b>No.</b>

I-900 element	Addressed in the audit
6. Analyze departmental roles and functions, and provide recommendations to change or eliminate them	<b>No.</b>
7. Provide recommendations for statutory or regulatory changes that may be necessary for the department to properly carry out its functions	<b>No.</b>
8. Analyze departmental performance data, performance measures and self-assessment systems	<b>No.</b>
9. Identify relevant best practices	<b>Yes.</b> The audit identified leading practices for the Washington State Housing Finance Commission to strengthen its monitoring and guidance for housing projects with tenant purchase options.

## Compliance with generally accepted government auditing standards

We conducted this performance audit under the authority of state law (RCW 43.09.470), approved as Initiative 900 by Washington voters in 2005, and in accordance with generally accepted government auditing standards as published in *Government Auditing Standards* (July 2018 revision) issued by the U.S. Government Accountability Office. 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.

## The mission of the Office of the Washington State Auditor

To provide citizens with independent and transparent examinations of how state and local governments use public funds, and develop strategies that make government more efficient and effective. The results of our work are widely distributed through a variety of reports, which are available on our website and through our free, electronic [subscription service](#). We take our role as partners in accountability seriously. We provide training and technical assistance to governments and have an extensive quality assurance program. For more information about the State Auditor's Office, visit [www.sao.wa.gov](http://www.sao.wa.gov).

# Appendix B: Objectives, Scope and Methodology

## Objectives

The purpose of this performance audit was to examine the Washington State Housing Finance Commission's oversight of Low-Income Housing Tax Credit (LIHTC) housing projects that offer tenant purchase options. The audit addressed the following objectives:

1. Has the Housing Finance Commission followed applicable federal and state laws related to financing and overseeing housing projects that offer tenant purchase options?
2. What benefits have tenants in projects with a tenant purchase option received related to affordable housing and homeownership?
3. How could the Housing Finance Commission improve tenant outcomes for projects with tenant purchase options?

For reporting purposes, the audit results have been organized into key findings. The messages relate to the original objectives as follows:

- The Housing Finance Commission met legal requirements but could do more to oversee housing projects that include tenant purchase options (pages 15-20) – This finding addresses Objectives 1 and 3.
- No tenants have become homeowners through the program, but they have received other meaningful benefits (pages 21-27) – This finding addresses Objectives 2 and 3.

## Scope

This audit examined the commission's policies and practices, reviewed information for projects that included a tenant purchase option, and assessed benefits to tenants for LIHTC projects that offer tenant purchase options. It also evaluated the commission's compliance with relevant laws and regulations and identified ways to improve the agency's oversight of these projects to help achieve positive tenant outcomes. Our primary audit period was January 2019 through December 2023. However, because the homes included in this audit are available to rent for at least 15 years before they can be purchased, some information from before this period was also included in our reviews.

The audit did not examine the lease agreements between tenants and the project owners, including tribal housing authorities. We also did not evaluate the decision by the Nooksack Indian Tribe Housing Department to evict tenants who lived in housing the Housing Department managed.

## Methodology

We obtained the evidence used to support the findings, conclusions and recommendations in this audit report during our fieldwork period (March 2024 to June 2024), with some additional follow-up work afterward. We have summarized the work we performed to address each of the audit objectives in the following sections.

### **Objective 1: Has the Housing Finance Commission followed applicable federal and state laws related to financing and overseeing housing projects that offer tenant purchase options?**

#### *Reviewed laws and regulations*

We reviewed federal and state laws and regulations for the LIHTC program, identifying which requirements were relevant to tenant ownership.

#### *Interviewed commission managers and staff*

We interviewed managers and staff to understand the commission's processes to oversee the state's LIHTC projects to ensure compliance with relevant legal requirements.

#### *Reviewed LIHTC applications*

We reviewed a judgmental selection of five LIHTC project applications that included tenant purchase options, including four current projects and one waitlisted project. Commission staff said that they had received 24 applications that proposed tenant purchase options, but we did not review all applications to confirm this. We reviewed each project's application and scoring materials to ensure the application indicated election of the tenant purchase option, included a tenant purchase plan and was awarded points appropriately. Because we did not use a statistically representative sample of project applications, the results cannot be extrapolated to all projects overseen by the commission.

### **Objective 2: What benefits have tenants in projects with a tenant purchase option received related to affordable housing and homeownership?**

#### *Data reliability testing*

The commission provided data from two separate systems. One is an internal database used by the commission to track various aspects of LIHTC housing projects at the project level, such as compliance monitoring, billing, and project details and history. The other is a public-facing system that project owners and their management agents use to enter compliance and financial information at the individual tenant level, including tenant income, household size and special needs designations. This public-facing system is jointly owned by the commission and the Department of Commerce.

We obtained project details for all LIHTC projects from the internal system for 2023. We also received five years (2019-2023) of data from the public-facing system containing tenant-level information for LIHTC projects with tenant ownership options. We determined the data from both systems was reliable for our audit purposes. Data reliability work included tests for inappropriate duplicates, blank fields and

illogical values, and comparing key fields between our datasets for the two systems. We could not trace data from the public-facing system to supporting documentation submitted by project owners because the commission does not retain copies due to tenant privacy concerns. However, the commission's annual review process helped provide assurance over the reliability of this data.

### ***Data analysis: Timeline and count of homes available for tenant purchase***

We calculated the number of homes that qualified for tenant purchase as of 2023, and by 2030, using each project's first credit year. (See sidebar.) We also identified the number of tenants living in homes eligible for purchase. The actual number of tenants in homes currently eligible for purchase in 2023 was available in our dataset.

"First credit year" is the year the project owner made a project's homes available to rent.

We used two methods to estimate the number of future tenants. First, we used the actual number of tenants in these projects as of 2023. Second, we used the average number of tenants by home size from 2019 through 2023. These two methods gave us an estimated range of tenants who would be living in homes eligible for purchase between 2024 and 2030. We used the midpoint of this range to estimate the number of tenants who might be living in homes reaching eligibility for purchase by 2030.

We found that homes within a single project may become eligible for tenant purchase in different years. We used the project's first credit year as the starting point for calculating eligibility for all homes under a specific project. However, project owners may postpone the first credit year by one year for some or all of the homes in their project. Thus, it is possible the actual number of eligible homes in a given year could differ since we calculated eligibility for all homes based on the project's first credit year. Because we analyzed this data based on date ranges rather than individual years, the effect on our analysis should be minimal.

Two projects managed by the Spokane Indian Housing Authority added tenant purchase options in 2023, several years after the projects were started. Since these projects only recently added the tenant purchase option, we excluded Spokane figures from this analysis.

### ***Data analysis: Analyzing tenant income, special needs and rent***

**Income:** We compared average tenant incomes from 2023 to average incomes in their area. We calculated average income for tenants in all projects with purchase options, stratified by the number of bedrooms in each home. We also calculated the overall average household income as a percentage of area median income for all homes with tenant purchase options using the commission's calculations at the individual household level.

**Special needs populations:** We calculated the number of households with disabled or previously homeless people using tenant data from 2023 for all LIHTC projects with tenant purchase options.

**Rent charged:** We compared the amount project owners charged tenants for rent in 2023 to market-rate rents for similar sized homes in their area. We calculated average rent charged, stratified by location and the number of bedrooms in each home. However, we could not determine the actual rent charged by project owners due to incomplete housing subsidy data necessary to calculate rent charged. Subsidy data was incomplete because tenants residing on tribal land may receive housing subsidies from other grant programs their tribes manage, and project owners are not required to include these subsidies in their annual reports to the commission. We instead used the maximum allowable rent housing authorities could charge under the LIHTC program, compared to market-rate rent figures from the

U.S. Department of Housing and Urban Development (HUD). We used HUD data for one-to-four-bedroom homes and estimated rent for five-bedroom homes using a simple linear regression model.

**Rent paid:** We compared the amount tenants paid out of pocket for rent in 2023 to market rates for similar sized homes in their area. Actual tenant rent payment data was available in our dataset. Like the rent charged methodology above, we compared the average rent payment by home size to market-rate rents figures.

### **Objective 3: How could the Housing Finance Commission improve tenant outcomes for projects with tenant purchase options?**

#### ***Researched practices in other states***

We reviewed qualified allocation plans or related documentation about tenant purchase options for the following states with federally recognized tribes: Arizona, California, Idaho, Minnesota, Montana, New Mexico and Oklahoma. We also identified other relevant criteria from other rent-to-own programs, including in the private sector.

#### ***Reviewed project's tenant purchase plans***

We reviewed each project's tenant purchase plan to better understand the options proposed by the project owners. This included the mechanisms for purchasing homes, the timeline and process, and any homeownership education classes offered. We then compared these plans to practices in other states.

#### ***Interviewed project owners***

We interviewed employees from three project owners that manage six housing projects with tenant purchase options to understand their plans to implement tenant purchase and identify recommendations for the commission.

#### ***Tenant focus groups***

We conducted focus groups with tenants at two housing projects with tenant purchase options to understand what information had been shared with them about homeownership and identify recommendations for the commission. In eastern Washington, the group was composed of nine people living in projects managed by the Yakama Nation Housing Authority; in western Washington, of eight people living in projects managed by the Lower Elwha Housing Authority. We reached out to several project owners across the state to arrange focus groups with their tenants when selecting housing projects for our focus groups. Only two project owners were available to do so. We discussed topics including tenants' awareness of the tenant purchase option, how realistic buying their home felt, and what additional information and support they wanted to help make decisions around homeownership. To compensate focus group members for their time and input, we gave each participant a \$50 gift card to a major retail store.

#### ***Reviewed practices for project monitoring and oversight***

We researched practices related to project monitoring, accountability and compliance. Research also focused on communication and collaboration. We compared these practices to the commission's processes for overseeing tenant purchase options.

### *Interviewed commission employees*

We interviewed managers and staff to understand the commission's processes for overseeing the LIHTC program generally and tenant purchase options specifically, as well as its planned changes to its monitoring structure.

### **Work on internal controls**

**Objective 1** – We assessed internal controls relevant to legal requirements for tenant purchase options. This work included reviewing the qualified allocation plan and related policies, along with a selection of LIHTC project applications.

The design of internal controls appeared to be generally effective for the qualified allocation plan and selection criteria for housing projects. We determined the commission met legal requirements for project selection criteria and that related internal controls were operating effectively.

The design of controls for compliance monitoring did not appear to be effective as it relates to this objective because there are no requirements specific to tenant purchase.

**Objective 3** – We assessed internal controls relevant to monitoring tenant purchase options. This included reviewing the agreements between the commission and project owners, as well as the tenant purchase plans submitted by project owners as part of their LIHTC project applications.

We identified opportunities for the commission to improve its controls for monitoring tenant purchase plans through strengthening the design of internal controls in this area and communicated this through our recommendations. We did not evaluate the implementation of controls or assess their effectiveness.





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– Pat McCarthy, State Auditor

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