Examination Specialization and Technical Guidance's

Low Income Housing Credit Newsletter

Internal Revenue Service Issue #24, April 2007

The LIHC newsletter provides a forum for networking and sharing information about IRC §42, the Low-Income Housing Credit and communicating technical knowledge and skills, guidance and assistance for developing LIHC issues. We are committed to the development of technical expertise among field personnel. Articles and ideas for future articles are welcome!! The contents of this newsletter should not be used or cited as authority for setting or sustaining a technical position.

Guide for Completing Form 8823: an IRS Revenue Agent's Viewpoint

The new Guide for Completing Form 8823 was unveiled at the National Council of State Housing Agencies' January 2007 conference. The guide was written at the request of the state agencies and with their assistance, to promote the consistent application of IRC §42 requirements and reporting of noncompliance to the IRS via Form 8823.

While the guide was written specifically for state agencies and its scope is limited to the reporting of noncompliance and building dispositions, the guide is also a very useful audit tool for revenue agents.

Taxpayers are selected for audit based on the reported noncompliance. All the Forms 8823 and attached explanation are included in the case file. Reviewing the chapters for the categories of noncompliance reported by the state agency will help agents understand the issue and prepare for the audit.

The guide is the only comprehensive source of information for topics not detailed in the Code. Here are a few examples:

> Households need to be income-qualified in order for a rental unit to qualify for the credit. How is the income limit determined? How do you define a household? Income isn't taxable income, how is it determined and verified? What kind of documentation should be in the tenant file? See chapter 4.
>
> Under the Code, the low-income units must be suitable for occupancy. How is "suitable for occupancy" defined? If the property looks okay to you when you tour the property as part of your audit, is that good enough? See chapter 6.
>
> The rent charged for low-income rental units must be restricted. What if the taxpayer charges the tenant fees? Which fees are allowable? How do the fees affect the rent limit? Does it matter? See chapter 11.

The guide is well-documented within the text, in footnotes, and at the end of each chapter. These references will be helpful when citing the authority to sustain technical positions.

In total, there are 16 categories identifying specific noncompliance issues, plus an "other" category and the reporting of building dispositions, which trigger the application of the recapture rules (see Exhibit 24-1). Happy reading!

Editor's Note: The guide is available sending an e-mail to **Grace.F.Robertson@irs.gov**. The guide will not be available on the IRS web for a while due to technical problems.

IRC §42 Filing Requirements

It's *that* time of year…time to file federal tax returns. For owners of LIHC properties, this will include computing the credit amount on Form 8609-A, Annual Statement for Low-Income Housing Credit. A few reminders:

For Part 1: Compliance Information. The building identification number should be identified on Line A and answer all the questions. If the taxpayer answered "no" to item C, the credit is subject to disallowance.

For Part II, which is the actual computation of the credit, there are several common errors:

Eligible Basis

Eligible Basis is determined as of the close of the first taxable year of the credit period and is generally the same every year. See IRC §42(d) for all the requirements. Decreases in Eligible Basis will result in a decrease in Qualified Basis which will trigger the recapture provisions under IRC §42(j).

Applicable Fraction- First Year Computation

The Applicable Fraction is determined as of the last day of each tax year. For the first year of the credit period, the Applicable Fraction is the average fraction over the 12-month period. See IRC §42(f)(2).

Intuitively, the allowable credit for the first year should be proportionate to the maximum housing credit dollar amount on Form 8609, line 1b, and the proportion should be the "averaged" Applicable Fraction.

For example, a low-income building is 100% occupied by income-qualified households on the last day of the first taxable year of the credit period, but the "averaged" Applicable Fraction is 58.04%. The Eligible Basis is $2,000,000 and the Applicable Percentage is 8.1%.

For the first year of the credit period, the allowable credit is computed as:

Eligible Basis	$2,000,0000
x Applicable Fraction:	.5804
x Applicable %:	.081
Credit Amount:	$94,025

For years after the first year, the allowable credit is computed as:

Eligible Basis:	$2,000,0000
x Applicable Fraction:	1.0
x Applicable %:	.081
Credit Amount:	$162,000

$94,025/$162,000 is 58.04%. This is a good check on the math, but unfortunately is not a true statement if the state agency allocated less credit than the full amount of credit supported by the eligible basis. In our example, suppose the state agency limited the maximum annual credit amount allowable to $110,000 under IRC 42(m)(2)? The credit for years after the first year would be limited to the $110,000, but what about the first year?

The credit is computed just as before. Since $94,025 is less than the $110,000 maximum allowable credit, the full $94,025 can be claimed for the first year of the credit period.

Eligible Basis:	$2,000,0000
x Applicable Fraction:	.5804
x Applicable %:	.081
Credit Amount:	$94,025

For the 11th year of the credit period, the allowable credit is the portion of the credit not allowed in the first year. So, in our example, $110,000 - $94,025 = $15,975 for year 11. The taxpayer should keep documentation of the credit amount claimed for the first year of the credit period.

Applicable Percentage

If, as a result of renting additional low-income units after the end of the first year of the credit period, there is an increase in Qualified Basis, then the Applicable Percentage for the additional Qualified Basis is 2/3 of the Applicable Percentage identified on Form 8609, line 2.

Disposition of Building

If a low-income building or interest therein is sold or otherwise disposed, the Qualified Basis at the end of the taxable year is zero and no credit is allowable. The taxpayer is also subject to the recapture rules and must file Form 8611 with their tax return. If, however, the building continues to operate as a qualified low-income building, the taxpayer can avoid the recapture requirement by placing a bond with the IRS. The bond is filed with the Philadelphia Campus using Form 8693 within 60 days of the disposition. Form 8693 is not filed with the taxpayer's tax return.

Form 8609, Low-Income Housing Credit Allocation and Certification

Taxpayers are no longer required to file Form 8609 with their tax returns. Instead, taxpayers complete the IRC §42(l) certification by submitting the completed Form 8609 to the IRS just *one time.*

> The certification must be made using the Form 8609 received from the state agency, with Part I completed, signed and dated.

Taxpayers must make the one time submission even if they filed Form 8609 with their tax return in a prior year (if the allocation was made using the November 2003 revision of the form, refer to the instructions for the December 2005 revision for additional information).

Taxpayers must complete the one time submission with Part II completed for qualified low-income buildings financed with tax-exempt bonds.

Taxpayers make elections by checking the "yes" or "no" boxes for lines 8b, 9a, 9b, 10a, and 10b. The four elections 10(a)-(d) are irrevocable.

If the taxpayer elects to treat the building as part of a multiple building project (line 8b), each building to be included in the project must be identified in an attachment to the Form 8609. Refer to the instructions for the December 2006 revision of Form 8609 for additional information.

LIHC and ESTG: Office of Examination Specialization and Technical Guidance (ESTG)

The LIHC program is managed by ESTG, a group within SBSE Exam Policy. There are 13 program analysts and technical advisors who are experts on a variety of technical issues, industries, and specific Code sections like IRC §42. The group is committed to the development of technical expertise through training and mentoring, and maintains a website that includes a page for the LIHC program. Reference material and technical information is available at: **http://sbse.web.irs.gov/TG/TGIndustryIssues.htm#LowIncome**.

Note: The webpage is part of the IRS' internal network and is not available to the general public.

IRS Guidance

1. Rev. Proc. 2007-20 – Transactions in which the refundable or contingent fee is related to the low-income housing credit under IRC §42(a) are not reportable transactions for purposes of the disclosure rules under Treas. Reg. 1.6011-4(b)(4). However, the transactions may be reportable under (b)(2), (b)(3), (b)(5), (b)(6) or (b)(7) of the same regulation.

2. Chief Counsel Notice CC-2007-010 – the IRS has provided limited relief for satisfying the requirement for making a carryover allocation of LIHC dollar amount under IRC §42(h)(1)(E) and (F) in the Gulf Opportunity Zone by the close of the 2006 calendar year. Given the unique nature of the problems in the GO ZONE and the administrative complexities associated with the initial allocation of credits from the Credit Cap, the Service will consider carryover allocations intended to be made from the 2006 Credit Cap that satisfy Treas. Reg. 1.42-6(d)(2)(i) through (x), but signed and dated by January 31, 2007, as having been made by the close of the 2006 calendar year.

LIHC Administrative Reminders

All LIHC cases should include Project Code 0670 and ERCS Tracking Code 9812. If you expand an audit to include additional years or related taxpayers, please make sure the additional returns also carry the LIHC project code and tracking code designation.

TEFRA Reminders

As LIHC property owners are almost always partnerships, and are likely to be subject to TEFRA procedural requirements, please remember that examiners are required to document actions taken and decisions made. Examiners must complete Form 12813, TEFRA Procedures Checksheet for every examination of a partnership or limited liability company (LLC) filing as a partnership. If the partnership or LLC is subject to the TEFRA procedures, three additional checksheets are required:

Form 13814, TEFRA Linkage Package Checksheet

Form 13828, Tax Matters Partner (TMP) Qualification Checksheet

Form 13827, Tax Matters Partner (TMP) Designation Checksheet

Surveying LIHC Tax Returns

If you believe it is appropriate to survey an LIHC return, please fax Form 1900 to Grace Robertson, at 202-283-2240, for signature approval.

Subscribing to the LIHC Newsletter

The LIHC Newsletter is distributed through e-mail, free of charge. If you would like to subscribe, just contact Grace Robertson at **Grace.F.Robertson@irs.gov**.

♫*Grace Notes*♫

You might have noticed that the format of the newsletter changed ever so slightly this month. It's not that I rearrange the furniture on a whim, but with the release of the Guide for Completing Form 8823, it did seem appropriate to hit the "reset" button.

First of all, a really, really big thanks to everyone that assisted with the Form 8823 Guide – ideas and discussions, writing, providing references, feedback on drafts, editing….and well, everything else. It has been quite a journey.

My second thought is that we have been issuing the LIHC newsletter since October of 2000 and if you look back at those old newsletters…well, we've come a long way. If you find a conflict between the newsletter and the guide – the information in the guide is the most current and should be followed.

Change is a pain, but progress is excellent!

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