

Low Income Housing Credit Newsletter

Internal Revenue Service

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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.

LIHC Audit Expectations

The LIHC program may be only a small portion of the IRS' effort to encourage compliance with the tax law, but it does contribute to SBSE Examination's success when quality audits are conducted. In this article, nine expectations or strategies for completing quality audits of LIHC tax returns in a timely manner are discussed.

Issue Identification and Case Building

Case files for LIHC audits will include information and documents needed to develop the LIHC issues, including:

Classification check sheets identifying the specific issues and the potential adjustment to the credit,

The reason for the audit will be identified. The audit may result from information submitted by a state agency on Form 8823, industry sources, public information, or IRS analyses.

Memoranda and technical guidance for specific issues, and

When appropriate, copies of prior year returns.

Most LIHC properties are owned by partnerships. Yk1 research will be provided as needed to help examiners understand the partnership structure.

Technical Assistance

When an audit is initiated (Status 12), the examiner will be contacted by the Headquarters analyst. The analyst will provide assistance as needed throughout the examination.

Customer Satisfaction

Examinations should be conducted expeditiously and the actions should be timely.

Keep taxpayers and their representatives informed of the case's status from the start of the examination through its resolution.

Provide taxpayers and their representatives with clear, complete and accurate explanations of the report, adjustments, and available options for resolving issues.

Minimum LIHC Audit Requirements

Determining the scope of an examination is the process through which examiners select issues warranting examination, so that (with reasonable certainty) all items necessary for a substantially correct determination of the tax liability have been considered. At a minimum, the following LIHC issues must be addressed:

Eligible Basis: Review the taxpayer's records to confirm that only allowable costs for depreciable residential rental property and amenities have been included in the computation.

Habitation Standards: Tour the property to ensure that the property is well maintained and suitable for occupancy.

Tenant Eligibility: Review the taxpayer's tenant files to ensure that tenants are income-qualified.

Rent Limits: Ensure that the restricted rent is correctly computed and allowances under IRC §42(g)(2), which reduce the gross rent amount, are properly applied.

In cases where the state agency has reported that the taxpayer is no longer participating in the program, the audit can be limited to consideration of the recapture provisions under IRC §42(j).

Investor returns are also identified for audit when the taxpayer has failed to correctly recapture the LIHC under IRC §42(j) and/or did not correctly and timely secure a surety bond or securities under IRC §42(j)(6).

Examination of Income

The examination of income is a required issue for all tax returns selected for audit and while LIHC partnerships are usually audited for specific IRC §42 issues, examiners must still complete the minimum income probes as outlined in IRM 4.10.4.3.4. In addition, the following two audit techniques should also be used

The financial status analysis described in IRM 4.10.4.3.3.1 is not required for partnership returns, but a quick review of the cash flows based on the rental schedule included with the return to estimate whether the taxpayer has sufficient funds to cover the operational expenses can be insightful. If the loss represents a true imbalance of cash flows, i.e., more expenses paid than income reported, then the source of funds used to pay operational costs and service debt should be identified.

Examiners should also review the taxpayer's website as part of the tour of the business. See IRM 4.10.4.3.6.2. While the taxpayer is probably not involved in e-commerce, the taxpayer may use the Internet to advertise available housing. The site may disclose rents, renting practices, and the availability of amenities.

Issue Development and Taxpayer Privacy

Examiners should complete the audit at the taxpayer's premises, conduct interviews and tour the business site whenever possible to ensure proper factual development.

The obligation to protect taxpayers' privacy and safeguard taxpayer information is a fundamental part of the IRS' mission to apply the tax law with integrity and fairness. Taxpayers have the right to expect that information they provide

with be safeguarded and used only in accordance with the law.

No information will be collected or used with respect to taxpayers that is not necessary and relevant for tax administration and other legally mandated or authorized purposes.

Information will be collected, to the greatest extent practicable, directly from the taxpayer to whom it relates. (See IRM 4.10.1.6.12 for procedures to be used when making third party contacts.)

Information about taxpayers collected from third parties will be verified to the extent practicable, with the taxpayers themselves, before a determination is made using the information.

Required Filing Checks

Examiners are encouraged to expand an audit to include multiple years or related taxpayers in all cases when appropriate. See IRM 4.10.5.

Penalties

Transactions designed to defeat the tax system must be addressed. Consideration should be given to fraud (IRM 20.1.5.12), aiding and abetting penalties (IRM 20.1.6.6) and preparer penalties (IRM 20.1.6.3).

Case Monitoring and Quality Improvement

To ensure proper monitoring of LIHC cases, Project Code 0670 and Tracking Code 9812 are used to identify audits in process. Examiners will be asked to provide information about the case, issue development, and results. On occasion, closed cases will be reviewed. The information will be used to improve the quality of case work and administration of the program. The information will be not be used to evaluate employee performance.

Administrative Reminders

Expanding Audits, Project/Tracking Code:

All LIHC cases should include Project Code 0670 and ERCS Tracking Code 9812. If the audit is expanded to include additional years or related taxpayers, the additional returns should

also carry the LIHC project code and tracking code designation.

Form 5344, Revenue Protection: The Examination Closing Record, Form 5344, contains four blocks of information to account for adjustments that reduce a credit carryforward. Blocks 44 through 47 identify the type of credit and the extent of any adjustment made. See IRM 104.3.12.4.55 through 58 for details.

Surveying LIHC Tax Returns: If you believe it is appropriate to survey an LIHC return, please fax Form 1900 to Grace Robertson, at 202-283-7008, for signature approval.

TEFRA Requirements: As LIHC property owners are almost always partnerships, and are likely to be subject to TEFRA procedural requirements, please remember document actions taken and decisions made by completing:

- Form 12813, TEFRA Procedures
- Form 13814, TEFRA Linkage Package Checksheet
- Form 13828, Tax Matters Partner (TMP) Qualification Checksheet
- Form 13827, Tax Matters Partner (TMP) Designation Checksheet

More information is available on the TEFRA website, along with a list of TEFRA Coordinators who can help walk you through the procedures.

http://tefra.web.irs.gov/m1/1a_home.asp

Subscribing to the LIHC Newsletter

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

♪ Grace Notes ♪

It's time to set goals for FY2008. I was once asked how I managed to get so much done, and other than being a bit too focused and intense at times, here's what I answered:

First, you need to decide what it is you want to accomplish; i.e., the *goal*. The IRS is responsible for administering the tax code with integrity and fairness for all. Part of the strategy for administering the tax code is conducting audits. So, for SBSE Examination, the goal is to efficiently conduct quality audits..

Second, you need to determine what must be done to accomplish the goal; i.e., *quality* audits *efficiently* completed. In this newsletter, I have outlined nine tasks or expectations that will contribute to the completion of efficiently conducted quality audits of taxpayers owning LIHC properties. The tasks and expectations I've identified are not new, nor are they particularly unique to the LIHC program. But they are the "tried and proved" methodology for completing quality audits in a timely manner.

Third, and this may seem obvious, but you need to actually complete the tasks identified in step two. What is not so obvious is that you must do *only* those tasks that actually move you closer to your goal. Distractions -all those fun things you *want* to do- can be your downfall!

And that brings us to the heart of the matter: how do you achieve your goals and have fun, too? After all, being focused and intense can give you a royal headache. And that reminds me of two of my favorite quips from my respected elders:

"Work isn't work if its fun."

"You have to do it til you like it."

Grace Robertson
Phone: 202-283-2516
Grace.F.Robertson@irs.gov