

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.

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Building Identification Numbers

A Building Identification Number (BIN) is assigned to every building receiving an allocation of IRC §42 credit, or, as described in IRC §42(h)(4), is financed with tax-exempt bonds subject to the volume cap under IRC §146. The rules for assigning BINs are outlined in Notice 1988-91.

Purpose

BINs are needed to identify low-income buildings when state agencies and owners report IRC §42-related events to the IRS: The BIN is comparable to an individual's Social Security Number (SSN) or an entity's EIN (Employer Identification Number), which are sometimes collectively referred to as Taxpayer Identification Numbers (TIN). BINs are identified on the following forms:

- Form 8609, Low-Income Housing Credit Allocation and Certification.
- Form 8610-A, Carry-Over Allocation of Low-Income Housing Credit.
- Form 8823, Low-Income Housing Credit Agencies Report of Noncompliance or Building Disposition
- Form 8609-A, Annual Statement for Low-Income Housing Credit
- Form 8586, Low-Income Housing Credit, if there has been a decrease in Qualified Basis.
- Form 8877, Recapture of Low-Income Housing Credit, if there is a recapture event under IRC §42(j).

Format

The BIN consists of a two character state designation (the postal state abbreviation) followed by a two digit designation identifying the year the credit is allocated, and a five digit numbering designation.

For example, the identification number for one of 25 buildings allocated a credit in 1987 by the Connecticut Housing Finance Authority (the only housing credit allocating agency in the state) might read CT-87-00023.

Unique BIN

The BIN must be unique to the building and must be used for all allocations of credit. Three examples:

- A building may receive separate allocations of credit for the acquisition of the building and the rehabilitation of the building.
- A newly constructed building may receive credit allocations in different calendar years. A separate Form 8609 will be used for each allocation, but the BIN assigned for the first allocation will be used for the subsequent allocation. See Treas. Reg. 1.42-6(d)(2)(x).
- An owner receives an allocation of credit to construct a new low-income building. The building is timely placed in service and completes the 15-year compliance period. The building is then sold to a new owner who applies for and receives an allocation of credit for acquiring and rehabilitating the existing building. The BIN assigned at the time the building was constructed will be used again, even though the allocation of credit is for a new owner and the 15-year compliance period has expired for the first allocation.

Assignment by Authorized Housing Credit Agency

The BIN will be assigned by the housing credit agency that is authorized to make the credit allocation. If there is more than one allocating agency in the state, the agencies should coordinate the assignment of BINs to ensure that BINs are not duplicated.

Reporting Noncompliance with Utility Allowance Requirements: Specifics and General Guidelines

In the last newsletter, the lead article was an announcement that the “Guide for Completing Form 8823” is now available on www.irs.gov. The article also included a summary of revisions to Chapter 18, which addresses the utility allowance requirements and had been significantly updated. Based on feedback from the state housing agencies, which use the Guide as a reference, this article provides additional explanations for reporting noncompliance to the IRS.

Specific Instructions in Chapter 18

The reporting of noncompliance with the Utility Allowance requirements is now expressly limited to those instances where the noncompliance causes the rent paid by the tenant to exceed the gross rent limit. It is a two-pronged test:

1. Did the taxpayer make an error when computing the utility allowance?
2. Did the error cause the rent paid by the tenant to exceed the gross rent limit for one or more months?

Only when the answer to both questions is “yes,” would a state agency report noncompliance with the utility allowance requirements on Form 8823, line 11m. It follows, then, to ask whether a state agency should also report noncompliance on line 11g, Gross Rent(s) Exceed Tax Credit Limits. Chapter 18 is silent, but Chapter 11 of the Guide, which addresses Gross Rent Limits, on page 11-9, reads:

If the noncompliance is the result of noncompliance with the utility allowance requirements, the error should be noted under category 11m, Owner did not properly calculate utility allowance.

Does this mean that 11m should be noted *instead* of 11g, or *in addition to* 11g?

To answer this question, reference can be made to the general rules provided in Chapter 2, Instructions for Completing Form 8823. On page 2-2, there’s a list of “General Guidelines.” The first guideline on the list reads:

1. Select all applicable categories of noncompliance.

Example 1: The state agency determined that 1 out of 10 low-income units in a building had been rented to a household with incomes that did not meet the income eligibility restrictions. Category 11a, Household income above income limit upon initial occupancy, should be selected.

Example 2: The state agency determined that 7 out of 10 low-income units in a one-building project were rented to households with incomes that did not meet the income eligibility restrictions. As a result, the owner did not meet the 40/60 minimum set-aside for that year. Category 11a, Household income above income limit upon initial occupancy, should be selected, and category

11f, Project failed to meet minimum set-aside requirement, should be selected.

Applying the general principle demonstrated in Example 2, noncompliance with the utility allowance requirements will result in the reporting of noncompliance with the gross rent limits on line 11g *in addition to* reporting noncompliance with the utility allowance requirements on line 11m.

Corrective Action

Admittedly, the cross-referencing between Chapter 18 and Chapter 11 could have been better and should be updated to reflect the relationship between utility allowances and maximum gross rent. So, in your copy of the Guide:

1. Keep a copy of this newsletter with Chapter 18, and
2. On page 11-9, change #1 to read:

“If the noncompliance is the result of noncompliance with the utility allowance requirements, the error should *also* be noted under category 11m, Owner did not properly calculate utility allowance.”

The text will be updated the next time the Guide is revised.

Amending Forms 8823

What if a state agency reported noncompliance with the utility allowance requirement when the noncompliance resulted in the rents exceeding the gross rent limit, but did *not* identify noncompliance on line 11g?

Amended Forms 8823 are not necessary. Forms 8823 are accepted by the IRS as accurate when filed, but failure to identify a cascade of non-compliance issues resulting from a single error is not a fatal flaw. When evaluating Forms 8823, the IRS will independently conclude that the single error caused multiple violations of IRC §42 requirements. After all, regardless of whether the state agency reports the noncompliance with the gross rent limits, the taxpayer has *actually* violated the requirements and the residential rental units are no longer qualified low-income units.

General Guidelines for Reporting Noncompliance

The revisions to Chapter 18, addressing utility allowances, surfaced underlying issues that should also be addressed in more general terms.

Scope

The scope of the Guide for Completing Form 8823 is limited to providing guidelines for state agencies when evaluating an owner’s compliance with IRC §42 requirements and reporting any observed noncompliance, or noncompliance of which the state agency becomes aware, to the IRS.

Our purpose was to help the state agencies more consistently identify and report noncompliance issues. No attempt was made to identify the tax consequence of noncompliance for the owner.

Owner (Taxpayer) Responsibility

Owners are responsible for determining the tax effect of any noncompliance.

1. Will the noncompliance affect the Applicable Fraction reported on Form 8609-A, Line 2?
2. Will the noncompliance affect the Eligible Basis reported on Form 8609-A, Line 1?
3. Will the noncompliance affect the Applicable Percentage reported on Form 8609-A, Line 5?

If noncompliance affects either the Applicable Fraction or Eligible Basis, the owner will also need to determine whether the credit recapture provisions under IRC §42(j) are applicable.

“Out of Compliance” and “Back in Compliance” Dates

State agencies identify the date the building ceased to comply with the IRC §42 provisions (line 8); i.e., the *earliest* date of noncompliance for all the noncompliance issues being reported. And then, when all the noncompliance issues are corrected, the state agency reports the date the *last* issue was resolved (line 9). The reporting of these dates identifies the time span of the noncompliance.

In the Guide, when defining the “back in compliance date,” the IRS looks to the date the noncompliance behavior ceases. The date the noncompliance with a specific requirement ceases, however, is not necessarily the date the building again qualifies for the credit. When there is a cascade of inter-related noncompliance issues, the whole fact pattern must be considered.

Specific to correcting noncompliance with the utility allowance requirement, the Guide provides the following explanation on page 18-11.

“A unit is considered back in compliance when the rent charged is reduced and correctly reflects the utility allowance. The date of correction is [the] date that the rents correctly reflect the utility allowance.”

Specific to the Gross Rent issue, the Guide provides the following instructions on page 11-10:

“Once a unit is determined to be out of compliance with the rent limits, the unit ceases to be a low-income unit for the remainder of the owner’s tax year. A unit is back in compliance on the first day of the owner’s next tax year if the rent charged on a monthly basis does not exceed the limit.”

Therefore, when noncompliance with the gross rent limit occurs because of noncompliance with the utility allowance requirements, the date noncompliance is corrected is always the first day of the owner’s next tax year, even though the noncompliance with the utility allowance requirements presumably ceased at an earlier date. In other words, a building is not back in compliance until all of the noncompliance issues are corrected.

“Close of the Taxable Year” Determination

Owners may question whether the credit should be lost for the entire year when the Guide instructs state agencies to report noncompliance with the gross rent limit under 11m rather than 11g when the noncompliance is associated with the utility allowance requirements. This question speaks to the continuous nature of compliance with the gross rent limit requirements.

Under IRC §42(c)(1)(A)(i), the Applicable Fraction is determined at the “close of such taxable year,” and is, generally considered a “snap shot” determination. However, each IRC §42 requirement’s “snap shot” has its own unique characteristics.

Specific to determining whether an owner is complying with the gross rent limit requirement, the question is not whether the rent was correctly limited at the end of the year, or even if the cumulative rent paid during the year is correctly limited on an annual basis. As explained in Chapter 11 of the Guide, to be considered compliant at the end of the taxable year, the owner must comply with the gross rent limit requirement each month of the taxable year. Further, the Guide also explains that an owner cannot reverse noncompliance with the gross rent limit by refunding excess rent, and then claim the credit as if the noncompliance never occurred.

The gross rent limit requirement is not the only IRC §42 rule requiring consideration of continuous compliance during the taxable year. If a taxpayer received a credit allocation from the IRC §42(h)(5) nonprofit set-aside, the nonprofit organization must materially participate (within the meaning of IRC §469(h)) in the development and operation of the project throughout the compliance period. As explained in Chapter 22 of the Guide, a nonprofit is considered to materially participate when it is regularly, continuously, and substantially involved in providing services integral to the operations of a project. The project is out of compliance for any taxable year where the nonprofit entity does not participate (in both management decisions and day-to-day activities) on a basis that is regular, continuous, and substantial. In other words, the determination at the end of the year is based on what happened during the year.

Noncompliance Categories

Line 11a-p identify 16 specific IRC §42 requirements for which noncompliance (and subsequent correction thereof) are reported. Line 11q is a catch-all “other” category. Line 13 is used to report the disposition of a low-income building, which is not necessarily a noncompliance issue, but does have tax consequences.

So, how did the IRS decide which IRC §42 requirements to specifically identify and which would be reported using Line 11(q)? That’s not an easy question to answer since the form reflects the views of many groups and individuals over a long period of time. But there are no hidden agendas. Decisions were made based on what information the IRS needed to administrate the IRC §42 program, given the practicalities of data collection and the limits of form design.

Why are the noncompliance categories important? Grouping the reports of noncompliance by category facilitates IRS analysis of taxpayer compliance and improves internal efficiencies. Consistent reporting by state agencies further enhances those efficiencies. Did you know that the first versions of Form 8823 (1992, 1994) did not include noncompliance categories? The state agencies were asked to “describe” the noncompliance.

Isn't it redundant to include a specific line for reporting noncompliance with the utility allowance requirements when the noncompliance will always be reported as noncompliance with the gross rent limit?

Not exactly. Two immediate conclusions can be made based on the identified noncompliance categories.

1. If only 11g is identified, then the noncompliance involves something other than a problem with the utility allowance.
2. If both 11g and 11m are identified, then the problem with the gross rent limit involves the utility allowance and may include additional rent-related issues.

To take it a step further, if 11g and 11m are identified and 11f is checked to note that the project failed the minimum set-aside requirement, then we can also conclude that the problem with the utility allowance is probably systemic.

But the decision to specifically identify certain compliance issues and how individual noncompliance issues are reported is a matter of convention intended to promote consistent reporting of noncompliance and facilitate IRS analysis of the reports.

We could have decided differently. For example, if 11g and 11m are identified, it really isn't clear whether the noncompliance with the utility allowance requirements is the *only* reason the gross rent limit has been violated. We could have asked the state agencies to report problem with utility allowances under 11m *without* identifying 11g. Since noncompliance under 11m *always* results in noncompliance with the gross rent limit, it really isn't necessary to mark both categories. At the same time, identifying 11g without 11m would mean that the noncompliance was not related to the utility allowance requirements. The two types of noncompliance would be distinguishable.

In fact, I (Grace Robertson) am reasonably certain that at a NCSHA conference before the June 2011 conference, I probably advised the state agencies just as described above.

Keep in mind that there is no absolute right or wrong way to report noncompliance. Noncompliance needs to be reported in a manner that best reflects the noncompliance issues and best helps the IRS administer the IRC §42 program. At this point, we have determined that the reporting of a “cascade” of noncompliance issues is more beneficial for the IRS than sorting out the reasons for the noncompliance.

So, from now on, the state agencies are asked to report the noncompliance following the general rules set out in the Guide and report the cascade of noncompliance issues.

Lessons Learned

1. One little word can make a big difference. Please update Chapter 11, page 9, #1 to read: If the noncompliance is the result of noncompliance with the utility allowance requirements, the error should *also* be noted under category 11m, Owner did not properly calculate utility allowance.
2. The scope of the Guide for Completing Form 8823 is limited to the evaluation of an owner's compliance and the reporting of noncompliance.
3. Owners (taxpayers) are responsible for determining the tax consequences of noncompliance regardless of how the state agency reported the noncompliance on Form 8823.
4. The IRS accepts the Forms 8823 as filed, but independently evaluates taxpayer compliance and any possible tax consequences associated with noncompliance.
5. Don't forget the general rules when applying the specific rules.

Quiz

A taxpayer received an allocation of credit in 2007 and builds 50 single-family homes. The buildings are placed in service in 2009. The taxpayer elects to begin the credit period in 2010 and the 40-60 minimum set-aside. The taxpayer does not elect to treat any of the buildings as a multi-building project. In July of 2011, the state housing agency inspects the buildings and conducts a tenant file review. The agency determines that the current tenant in one of the homes, who moved in on August 1, 2009, is not income-qualified.

Should the agency file a Form 8823? If so, which noncompliance category should be identified? The answer is at the end of the newsletter, just before the Administrative Reminders.

Claiming IRC §42 Credit for the 11th Year of the 15-Year Compliance Period

Under IRC §42(f)(2), the allowable credit is limited based on when the low-income buildings are placed in service and when the residential units are first occupied by income-qualified households. Any reduction in the allowable credit that would be allowable if the rule was not applied is allowable in the 11th year of the compliance period. The 11th year credit is reported on Form 8609-A, Annual Statement for Low-Income Credit, line 17, which is filed with the tax return for the entity owning the IRC §42 building(s). Basically, if all goes well:

$$\text{First Year Credit} + 11^{\text{th}} \text{ Year Credit} = \text{Allocated Credit}$$

However, if any of the units were first occupied by qualified tenants after the end of the first year of the credit period, then the taxpayer can claim the 2/3 credit under IRC §42(f)(3) for each remaining year of the 15-year compliance period that the unit is a low-income unit. There's a special rule to limit the credit for the year the unit first qualifies, but no rule com-

parable to the rule under IRC §42(f)(2) allowing the taxpayer to claim credit deferred from the first year in the 11th year of the compliance period.

Completing Form 8609-A

- Even though no credit is allowable for the 11th year, taxpayers should complete the computation of the credit in Part II of Form 8609. Particularly, do not skip lines 1 through 14.
- The amount on line 15, allowable credit for the year, should be zero or the allowable 2/3 credit.
- Line 16 is rarely applicable since low-income buildings are owned by single entities. Read the instructions for consideration of special rules related to dispositions.
- The credit deferred from the first year is entered on line 17.
- The total allowable credit is entered on line 18.

Documentation

If a taxpayer claims deferred credit in the 11th year, then the taxpayer must be able to document how much credit was claimed in the first year and how it was computed.

Miscellaneous

And don't forget to complete Part I, which satisfies the annual reporting requirement under IRC §42(1)(2).

Subscribing to the LIHC Newsletter

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Pop Quiz Answers

- (1) 11a, Household income above income limit upon initial occupancy, because the tenant was not income-qualified at move-in.
- (2) 11f, Project Failed the Minimum Set-Aside, because each building is a separate project and the percentage of qualified low-income units in the building is less than 40% (in fact, it is zero).
- (3) 11p, Building is no longer in compliance or participating in the section 42 program, because the project failed the minimum set-aside requirement for the first year of the credit period.

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, requires entries if you are reducing the

amount of credit to be carried forward to a tax year you are not going to audit. Enter the amount of credit carryforward to be disallowed for Item 46. Code "L" should be entered for Item 47. See IRM 4.4.12.4.58 for an example.

Surveying LIHC Tax Returns: If you believe it is appropriate to survey an LIHC return, please fax Form 1900 to Grace Robertson, at 202-283-2485, for signature approval.

TEFRA Requirements: As LIHC property owners are almost always partnerships, and are likely to be subject to TEFRA procedural requirements. More information is available on the TEFRA website, along with a list of TEFRA Coordinators.

♪ Grace Notes ♪

Last week I found myself driving on a "connector" road between two subdivisions of housing. Because of the terrain and foliage, the area has a feeling of isolation, except for the sidewalk along one side of the road. It is very unusual to see anyone walking there, so I was rather surprised when I saw a teenager walking her dog, a beautiful little collie. As I drove towards her, I could see that the little collie was having trouble walking slowly enough to keep pace with the girl, who was just shuffling along. I was a little concerned, but as I drove by her, I could see that she was working with a small hand-held device...probably texting or maybe playing a game.

My first thought was "wow," in a million years I couldn't put one foot in front of the other, walk a dog, *and* either type a message coherently or focus on a computer game well enough to win, *all* at the same time! But as I looked back in my rear view mirror, I felt a little sad. She hadn't noticed that it was a beautiful morning or that she was walking through a really nice area. She hadn't even noticed the beautiful little collie looking up at her, trying to get her attention...maybe to play a little or just walk a little faster.

So, wouldn't you know, a few days later I leave work just late enough to be caught in afternoon traffic and find myself first in line at a red light. It's the intersection of two small streets, but traffic is moving so slowly and it so congested that.....well, traffic is at a dead stop. Quite unexpectedly, I see a young woman weaving her way quickly through the cars, approximately in the cross walk. She's tall and her long hair is pulled back tightly to the crown of her head, a long pony tail swinging in rhythm to her long strides. She's wearing a beautiful silk dress with a brown and blue paisley print (I'm partial to paisley prints) and she's moving so quickly that she's almost running on her toes (the really high heels help). She's holding her right arm out to her side and as she moves closer to me, I can tell she's holding a leash. When she's right in front of me, I can see an itsy-bitsy little Pomeranian prancing right along side her, looking up at its mistress, excited and fully trusting her to lead the way. If I dared to interpret their body language, I'd say they both felt absolutely beautiful. But then they were gone, the light changed, and I rolled along.

I promised myself I'm going to play more with Hannah and Olivia (the cats) and wholehearted give them my full, undivided attention. Hmm...would Hannah walk on a leash?

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