

Notice 88-116

Low-Income Housing Tax Credit--Carryover of 1989 Credits for Certain Projects in Progress, Description of Construction, Reconstruction or Rehabilitation, Placed in Service

Section 42(n)(1) of the Internal Revenue Code (the “Code”) provides, generally, that the State housing credit ceiling under section 42(h) shall be zero for any calendar year after 1989. Thus, in general, all buildings eligible for the low-income housing credit must be placed in service before January 1, 1990. Under section 42(n)(2), however, 1989 credit amounts that are not allocated in 1989 may be applied to a building placed in service in 1990 if such building is constructed, reconstructed, or rehabilitated by the taxpayer and more than 10 percent of the reasonably anticipated cost of such construction, reconstruction, or rehabilitation has been incurred as of January 1, 1989. The purpose of this Notice is to provide guidance to taxpayers under section 42(n) of the Code regarding (1) what costs will be considered construction, reconstruction, or rehabilitation costs; and (2) when such costs will be considered to be incurred. In addition, this Notice provides guidance regarding when a building will be considered to be placed in service for purposes of section 42.

CONSTRUCTION, RECONSTRUCTION OR REHABILITATION COSTS

For purposes of section 42(n), the term construction, reconstruction, or rehabilitation costs means any amount that is (1) properly chargeable to a capital account and (2) incurred before or on January 1, 1989. Amounts are chargeable to a capital account if they are properly includible in computing eligible basis under section 42(d). Amounts treated as an expense and deducted in the year they are paid or incurred or amounts that are otherwise not added to eligible basis do not qualify. For example, the cost of acquisition of an existing building is a qualifying cost. Amounts incurred for taxes and architectural and engineering fees, site survey fees, legal expenses, insurance premiums, development fees, and other construction related costs satisfy the definition of construction, reconstruction, or rehabilitation costs if they are included in the eligible basis of the building. Production period interest (within the meaning of section 263A(f)) allocable to the construction, reconstruction, or rehabilitation of a building is a qualifying cost. The cost of land is not a qualifying cost. For purposes of section 42(n), the total anticipated costs of construction, reconstruction, or rehabilitation shall be determined by reference to a reasonable estimate, on or before January 1, 1989, of such amount.

COSTS INCURRED AS OF JANUARY 1, 1989

Construction, reconstruction, or rehabilitation costs are incurred for purposes <Page 450> of this section on the date such expenditures would be considered incurred under an accrual method of accounting, regardless of the method of accounting used by the taxpayer incurring the costs with respect to other items of income and expense.

PLACED IN SERVICE

For purposes of section 42, the term “placed in service” has two definitions--one for buildings and one for rehabilitation expenditures that are treated as a separate new

building (section 42(e)(4)(A)). The placed-in-service date for a new or existing building used as residential rental property is the date on which the building is ready and available for its specifically assigned function, i.e., the date on which the first unit in the building is certified as being suitable for occupancy in accordance with state or local law. In general, a transfer of the building results in a new placed-in-service date if, on the date of the transfer, the building is occupied or ready for occupancy.

Under section 42(e)(4)(A) of the Code, rehabilitation expenditures that are treated as a separate new building are placed in service at the close of any 24-month period, over which such expenditures are aggregated. The placed-in-service date of section 42(e)(4)(A) applies even if the building is occupied during the rehabilitation period.

A building may be placed in service even if the rental units in the building are not currently occupied by low-income tenants.

This document serves as an “administrative pronouncement” as that term is described in 1.661-3(b)(2) of the Income Tax Regulations and may be relied upon to the same extent as a revenue ruling or revenue procedure.