

Internal Revenue Service

Department of the Treasury
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Date:
April 06, 2012

In Re:

LEGEND:

Taxpayer 1 =

Taxpayer 2 =

LLC =

State 1 =

County =

City =

Building 1 =

Building 2 =

Building 3 =

District =

Site =

Corp1 =

Corp 2 =

Corp 3 =

Corp 4 =

Corp 5 =

date 1 =

date 2 =

date 3 =

date 4 =

date 5 =

date 6 =

date 7 =

date 8 =

date 9 =

year 1 =

b =

Dear :

This is in response to your ruling request dated on October 10, 2011, and subsequent correspondence requesting a ruling under sections 47(c)(2)(B)(v)(I) and 168(h)(1)(B) of the Internal Revenue Code on behalf of Taxpayer regarding the rehabilitation of historic buildings.

FACTS

Taxpayer 1, Taxpayer 2, and LLC are multi-member State 1 limited liability companies, which have not elected under §301.7701-3 to be taxed as corporations and, therefore, will be taxed as partnerships for federal income tax purposes. Taxpayer 2 was formed for the purpose of acquiring, rehabilitating, constructing, developing, leasing and selling Building 1. Taxpayer 2 intends to rehabilitate Building 1 in a manner that

would qualify its expenditures for the Federal historic tax credit. Taxpayer 1 was formed for the purpose of acquiring, rehabilitating, constructing, developing, leasing and selling Building 2. Taxpayer 1 intends to rehabilitate Building 2 in a manner that would qualify its expenditures for the Federal historic tax credit. LLC was formed for the purpose of acquiring, rehabilitating, constructing, developing, leasing and selling Building 3. LLC will rehabilitate Building 3 in a manner that would qualify its expenditures for the Federal historic tax credit.

Each of Building 1, Building 2, and Building 3 (collectively, the Buildings) has been determined by the National Park Service (NPS) to be a “contributing building” and, therefore, a “certified historic structure” within the District, which is a historic district listed on the National Register of Historic Places. The Buildings together with other related land are collectively referred to as the Site. According to the submission, the Site is part of a larger real estate development controlled by Corp 1. Beginning in year 1, representatives of Corp 2 (related to Taxpayer 2) met with representatives of Corp 1 to discuss rehabilitation of the Buildings. The Buildings were to be developed in an integrated manner and be used for research. Corp 2 wanted to develop the Buildings because of their proximity to each other, their common history and architectural or physical design, and the common marketing plan of using those structures.

Corp 1 and Corp 2 anticipated that the Buildings would be developed simultaneously. However, the recession made it impractical to finance such a large developmental project all at once. Instead, Corp 2 began developing Building 3 first, with plans to develop Buildings 1 and 2 as soon as practicable. The design phases of Building 3 began in date 1, and rehabilitation began in date 2. It is projected that the rehabilitation of Building 3 will be substantially completed around date 3, and tenants will begin moving in on or about date 4.

The design of Building 1 began in date 5, and the design of Building 2 began in date 6, prior to completing the construction of Building 3. It is anticipated that the rehabilitation of Buildings 2 and 3 will be performed along the same time line, with demolition for each building beginning in date 7, and new construction beginning in date 8. Corp 3 will be the architect for each of the Buildings. Corp 4 will be the general contractor for each of the Buildings.

The Buildings are separated by public streets, but there are a number of architectural features which physically tie the Buildings together. On the side of Buildings 1 and 2 is a . The will be retained, which will create an outdoor concourse connecting the two buildings. There is a ground level walk way physically connecting Buildings 1 and 2. A one-story bridge between both buildings will be reactivated and refurbished. There is a two-story bridge between Buildings 1 and 2, which tenants in those buildings can use to go from one building to the other without the necessity of exiting in the open air. Once the Buildings have been rehabilitated, they will be interconnected by the refurbished pedestrian

bridges for the benefit of tenants. In addition, a new connection stair will be built to allow easy external access between Buildings 2 and 3.

Building 3 will contain retail stores and restaurants accessible to tenants in the Buildings. Building 2 will have a fitness center, retail and services that will be open to tenants in all of the Buildings. In addition, Building 3 will have a conference center which may be used by certain tenants in all of the Buildings. Tenants of the Buildings also will share usage of surface parking lots and the park adjacent to Building 1.

County and City entered into an Agreement dated date 9, with Corp 5 and LLC 3 to fund up to \$b for costs incurred in connection with the infrastructure improvements and/or site preparations for rehabilitating the Site in order to create an interconnected and integrated project.

Taxpayer 2 requests a ruling that for purposes of the rehabilitation tax credit and applications of §§ 47(c)(2)(B)(v)(I) and 168 (h)(1)(B) to Taxpayer 2's rehabilitation and leasing of Building 1, the "property" will include all of the net rentable floor space in the Buildings.

LAW AND ANALYSIS

Section 47(c)(2)(B)(v)(I), as amended by section 3025(a) of the Housing Assistance Tax Act of 2008, provides that the term "qualified rehabilitation expenditure" does not include any expenditure in connection with the rehabilitation of a building which is allocable to the portion of the property which is (or may reasonably be expected to be) tax-exempt use property (within the meaning of § 168(h)), except that "50 percent" shall be substituted for "35 percent" in § 168(h)(1)(B)(iii). Section 3025(b) of the Act provides that the amendment made by section 3025 shall apply to expenditures properly taken into account for periods after December 31, 2007.

Section 168(h)(1)(B)(i) states that, in the case of non-residential real property, the term "tax-exempt use property" means that portion of the property leased to a "tax-exempt entity" in a "disqualified lease." Under section 168(h)(1)(B)(ii), the term "disqualified lease" means any lease of the property to a tax-exempt entity, but only if: (I) part or all of the property was financed (directly or indirectly) by an obligation the interest on which is exempt from tax under section 103(a) and such entity (or a related entity) participated in such financing, (II) under such lease there is a fixed or determinable price purchase or sale option which involves such entity (or a related entity) or there is the equivalent of such an option, (III) such lease has a lease term in excess of 20 years, or (IV) such lease occurs after a sale (or other transfer) of the property by, or lease of the property from, such entity (or a related entity) and such property has been used by such entity (or a related entity) before such sale (or other transfer) or lease.

Under section 168(h)(1)(B)(iii), property will be considered “tax-exempt use property” only if the portion of the property leased to tax-exempt entities in disqualified leases is more than 35 percent of the property (the “35-percent exception”). Section 168(h)(1)(B)(iv) provides that improvements to a property (other than land) will not be treated as a separate property.

Section 1.168(j)-1T, Q&A-6, of the temporary Income Tax Regulations provides that the phrase “more than 35 percent of the property” means more than 35 percent of the net rentable floor space of the property. The net rentable floor space in a building does not include the common areas of the building, regardless of the terms of the lease. For purposes of the “more than 35 percent of the property” rule, two or more buildings will be treated as separate properties unless they are part of the same project, in which case they will be treated as one property. Two or more buildings will be treated as part of the same project if the buildings are constructed under a common plan, within a reasonable time of each other, on the same site and will be used in an integrated manner.

Section 168(h)(1)(B)(iii) provides that property will not be treated as “tax-exempt use property” if the portion of the property leased to tax-exempt entities in disqualified leases is no more than 35 percent of the property. Under § 47(c)(2)(B)(v)(I), the test is no more than 50 percent for purposes of the rehabilitation credit. Taxpayer 2 posits that, even if Building 1 is leased to tax-exempt entities in disqualified lease, the determination of whether the 50-percent threshold is crossed should be made by reference to the total net rentable floor space in the Buildings combined because the Buildings are part of the same “project” under Q&A-6 of the temporary regulations and thus the Buildings together constitute the “property” for purposes of § 168(h). Therefore, according to the submission, if this 50-percent threshold is not crossed with respect to the total net rentable floor space in the Buildings, no portion of the “property” will be “tax-exempt use property” within the meaning of § 168(h)(1)(B) as modified for purposes of the rehabilitation credit by § 47(c)(2)(B)(v)(I).

For purposes of determining if the Buildings in this case should be considered part of a single project for purposes of Q&A-6 of the temporary regulations and § 168(h)(1)(B)(iii), Taxpayer 2 represents that the Buildings are constructed under a common plan, within a reasonable time of each other, located on the same site, and will be used in an integrated manner.

Taxpayer 2 represents that there is a common plan for the construction/rehabilitation of the Buildings. First, County and City entered into an Agreement with Corp 5 and LLC, pursuant to which County and City agreed to fund up to \$b for costs incurred in connection with the infrastructure improvements and/or site preparations for the rehabilitation of the Site where the Buildings are located. The purpose of Agreement is to create an interconnected and integrated center. Second, Corp 3 will contract to design the rehabilitation of each of the Buildings in a manner consistent

with their historic nature. Thus, there will be a consistent architectural theme and landscape design throughout this area. In addition, the NPS letter notes that NPS views the rehabilitation work as “a single overall project,” and rehabilitation certification will be issued “on the merits of the overall project rather than for each structure.”

Moreover, it has been represented that the Buildings have been designed and are being constructed under a common plan that calls for shared facilities and amenities, including restaurants and shops that are intended to allow the tenants of the Buildings easy access to dining and retail establishments. Corp 4 will perform the rehabilitation of all of the Buildings.

We have no facts or reason to doubt or challenge these representations. The design of the buildings/improvements are to be constructed on the Site, the use of a single architect (Corp 3), the use of a single general contractor (Corp 4), the County-City financing, the NPS letter, and the existence of shared elements all support the conclusion that the renovation of the Buildings is part of a single common plan for the improvement of the Site.

The submission also indicates that the construction and renovation of the Buildings will all be completed within a reasonable time of each other. According to the submission, Corp 2 began developing Building 3 first, with plans to develop Buildings 1 and 2 as soon as practicable. The design phases of Building 3 began in date 1 and rehabilitation began in date 2. It is projected that the rehabilitation of Building 3 will be substantially completed around date 3, and tenants will begin moving in on or about date 4. Design work on Building 1 began in date 5 and the design work on Building 2 began in date 6, prior to completion of construction on Building 3. It is anticipated that the rehabilitation of Buildings 1 and 2 will be performed along the same time line, with demolition for each building beginning in date 7 and new construction beginning in date 8. In our view, the construction and renovation of the Buildings will be performed and completed within a reasonable time of each other.

The facts show that the Buildings will be constructed on the same site (i.e., the Site) separated only by public streets. However, the Buildings will be interconnected through skywalks. Several parking lots will be shared among the tenants of the Buildings. Buildings 1 and 2 will be connected by an outdoor concourse. Building 2 and 3 will be connected by newly constructed steps. Accordingly, there is little doubt that based on the descriptions and exhibits in the submission, the Buildings are located on the same site.

Lastly, the facts in the submission indicate that the Buildings will operate in an integrated manner. For instance, the Buildings will be marketed to tenants which will do research consistent with the

Agreement entered into between County, City, Corp 5 and LLC, which funded up to \$b for costs incurred in connection with the infrastructure improvements and/or site preparations for the rehabilitation of the Site in order to create an interconnected

and integrated center. In addition, an employee has been hired to market the Buildings to prospective tenants. Corp 2 will market and manage the Site as a single project, seeking economies of scale and the benefits of a significant amount of diverse space available for lease. Corp 2 will utilize a single maintenance operation to work on the Site. Corp 2 should also benefit from the economic synergies associated with development of a core of high quality commercial properties on one site. The Buildings will share, and their tenants will use, many amenities/facilities, including a fitness center, a central conference center, convenient retail and restaurant options, parking and a park for recreation. The Buildings are adjacent to each other. Finally, a single Corp 2 employee will be responsible for arranging events and lecture programs for the common benefit of the tenants in the Buildings. Consequently, the Buildings will be operated in an integrated manner.

CONCLUSION

Based on the facts submitted and representations made, the Buildings constitute one project for purposes of §1.168(j)-1T, Q&A-6, of the temporary regulations. Accordingly, we conclude that for purposes of the rehabilitation tax credit and the application of §§ 47(c)(2)(B)(v)(I) and 168 (h)(1)(B) to Taxpayer 2s rehabilitation and leasing of Building 1, the “property” will include all of the net rentable floor space in the Buildings.

No opinion is expressed or implied regarding the application of any other provision in the Code or regulations. Specifically, no opinion is expressed or implied regarding whether the rehabilitation of Historic Building is a “substantial rehabilitation” or “certified rehabilitation,” or whether expenditures incurred to rehabilitate Historic Building are “qualified rehabilitation expenditures” under section 47(c).

This ruling is directed only to the taxpayer that requested it. Under section 6110(k)(3) it may not be used or cited as precedent. In accordance with a power of attorney filed with the request, a copy of this letter is being sent to your authorized representatives. We are sending a copy of this letter to the appropriate SBSE office.

Sincerely,

William A. Jackson
Chief, Branch 5
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosures (2)

Copy of this letter
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