

Private Letter Ruling 8844062, IRC Section 42

Aug. 11, 1988

This letter is in response to the letters dated March 4, 1988, April 18, 1988, and May 16, 1988, from Partnership's authorized representative, requesting rulings under the low-income housing credit provisions of section 42 of the Internal Revenue Code. The facts and representations as submitted are substantially set forth below.

Partnership, a State M limited partnership, is made up of N, a State M general partnership which is the general partner, and the individuals O, P, Q, and R, each of whom is a limited partner. The general partnership, N, has two partners, individual S and Corporation T.

Partnership was organized to purchase, invest in, renovate, lease, operate, manage, and sell The Project, a residential apartment complex. In furtherance of this purpose, Partnership purchased The Project prior to its having been placed in service. In addition to receiving housing assistance payments from the U.S. Department of Housing and Urban Development (HUD) pursuant to Section 8, Part 880, of the U.S. Housing Act of 1937, the low-income housing credit under section 42 of the Code provides Partnership with a tax incentive to offer low-income housing to eligible low-income elderly and handicapped persons.

Pursuant to a Contract for Deed, and its First Amendment, Partnership purchased for original use the partially-constructed Project from N on a. The purchase of The Project included the land, building, and attached personal property.

As consideration for the purchase of The Project, Partnership agreed to pay a principal sum of \$b, the payment terms for which are summarized as follows: (1) \$c upon execution of the Contract for Deed; (2) \$d, plus interest thereon from the date of the Agreement at the rate of e percent per annum, payable on or before f; and (3) Partnership's assumption on a nonrecourse basis of the existing nonrecourse mortgage in the approximate amount of \$g, which is secured by The Project. For purposes of determining basis, the purchase price is allocated \$h to the building and \$i to the land.

Partnership agreed to assume, on a nonrecourse basis the above-mentioned Mortgage which was executed between U, as mortgagee, and N, as mortgagor, to finance completion of The Project. The Mortgage Note and Mortgage were originally executed on j. The Mortgage was co-insured by HUD. The sale of N's interest in The Project to Partnership and the terms therein were consented to by U on k.

The Project is new construction. N started construction of The Project in 1987 and will finally complete it in 1988 pursuant to the terms of the Contract for Deed. One of the units will be a rent-free 2-bedroom manager's unit which will be occupied by the resident manager(s) responsible for managing the entire building. All of the other units will be 1-bedroom, 1-bath units, each individually equipped with a range, refrigerator, drapes,

carpet and individual gas heat. An asphalt parking lot is adjacent to the building for resident and visitor parking. Also included in The Project is a laundry facility, furnished community room, and a maintenance shop.

As of l, m of the s units were complete and ready for occupation, with the remaining units scheduled for final completion by n. As of o, City V issued a Temporary Certificate of Occupancy with respect to the building. The Certificate of Occupancy was stamped "Temporary" as there were several miscellaneous minor items requiring correction, but the temporary nature of the certificate did not prevent occupancy.

During the last quarter of 1987, Partnership placed advertisements in several newspapers and other periodicals published in State M, advising that it was accepting applications for housing in the subsidized rental project. As of l, p of the units were occupied by tenants and rental applications were approved (and apartment numbers assigned) with respect to q other units.

Partnership applied to W for a section 42 low-income housing credit allocation. On December 29, 1987, W made the following allocations on Form 8609: (1) the housing credit dollar amount allocated was \$r; (2) the maximum applicable credit percentage allocated was 9 percent; (3) maximum qualified basis was \$h, reflecting total purchase price less the price paid for the land; and (4) the percentage of aggregate basis financed by tax-exempt bonds was 0 percent.

In obtaining the 1987 allocation, Partnership relied in part on a document entitled the "Summary of the Low-Income Housing Tax Credit Program," prepared by W, regarding the proper determination date for when a building is placed in service for purposes of obtaining an allocation under section 42 of the Code. The Summary provides that " {a} building is generally placed in service by an owner when any portion of the building is first ready to be rented to tenants."

As a result of uncertainty regarding the actual placed-in-service determination date and State M's allocation, Partnership attempted to receive a protective 1988 low-income housing credit allocation. As of January 18 and 29, 1988, W refused to commit to an allocation for 1988.

In a letter dated May 16, 1988, your representative advises that Partnership now proposes to sell The Project to X. The proposed sale adds to to the list of taxpayers interested in the requested rulings X, its sole shareholder Y, and Z (the common parent of the affiliated group filing consolidated returns of which X and Y are members). The consummation of the sale of The Project is conditioned on the receipt by Partnership and X of the requested rulings.

Section 42(a) of the Code provides that for purposes of section 38, the amount of the low-income housing credit determined under this section for any taxable year in the credit period shall be an amount equal to--(1) the applicable percentage of (2) the qualified basis of each qualified low-income building.

Section 42(f)(1) of the Code provides that for purposes of this section, the term "credit period" means, with respect to any building, the period of 10 taxable years beginning with the taxable year in which the building is placed in service or, at the election of the taxpayer, the succeeding taxable year.

Section 42(c)(1)(A) of the Code provides that the qualified basis of any qualified low-income building for any taxable year is an amount equal to--(i) the applicable fraction (determined as of the close of such taxable year) of (ii) the eligible basis of such building (determined under subsection (d)(5)). Section 42(d)(1) provides that for purposes of this section the eligible basis of a new building is its adjusted basis; and section 42(i)(4) defines the term "new building" as a building the original use of which begins with the taxpayer.

Section 42(h)(1) of the Code provides that no credit shall be allowed by reason of this section for any taxable year with respect to any building in excess of the housing credit dollar amount allocated to the building under that subsection. An allocation shall be taken into account under the preceding sentence only if it occurs not later than the earlier of-- (A) the 60th day after the close of the taxable year, or (B) the close of the calendar year in which such taxable year ends.

Section 42(h)(6)(B)(ii) of the Code provides that a housing credit agency may allocate its housing credit dollar amount for any calendar year only to buildings placed in service before the close of such calendar year.

Section 1.17(a)-11(e)(1)(i) of the Income Tax Regulations provides that property is first placed in service on the date that it is first placed in a condition or state of readiness and availability for a specifically assigned function, whether in a trade or business, in the production of income, in a tax-exempt activity, or in a personal activity.

Section 42(d)(5)(A) of the Code provides, in general, that the eligible basis of any building for the entire compliance period for such building shall be its eligible basis on the date such building is placed in service.

Section 42(d)(2)(A)(i)(11) of the Code provides that the eligible basis of an existing building includes amounts chargeable to capital account and incurred by the taxpayer (before the close of the 1st taxable year of the credit period for such building) for property (or additions or improvements to property) of a character subject to the allowance for depreciation.

Section 42(m)(1)(B) of the Code provides the Secretary with authority to promulgate regulations dealing with buildings that are placed in service in portions.

We believe that the definition of the term "placed in service" under section 1.167(a)(11)(e)(1)(i) of the regulations is applicable in the instance case. Based on Partnership's representations regarding the Temporary Certificates of Occupancy and the

extent to which The Project was advertised as available for occupancy, we conclude that The Project was placed in service in calendar year 1987.

Under section 42(d)(2) of the Code, a taxpayer can buy an existing building, place it in service as low-income housing in 1987, defer the commencement of the 10-year credit period until the following taxable year (the 42(f)(1) election), and include in the building's eligible basis its cost of acquisition plus all rehabilitation expenditures (properly chargeable to capital account) that are paid or incurred with respect to the building through the close of that following year. If the building is placed in service late in 1987 but the rehabilitation is not complete at the time, the owner will have until the close of the first taxable year of the credit period within which to incur routine "build-out" or finishing-up expenditures, and all such expenditures that otherwise qualify will be includable in eligible basis.

Section 42(d)(5) of the Code provides that eligible basis of a building is determined on the date such building is placed in service. Pursuant to our authority in section 42(m)(1)(B) of the Code, in cases where a building is placed in service in portions, the Service will determine eligible basis on the last day of the year in which the building is placed in service or, if the taxpayer makes a section 42(f)(1) election the last day of the year succeeding the year in which the building was placed in service.

This conclusion is supported by the requirements of section 42(i)(1)(B) of the Code that requires the taxpayer to certify to the Secretary the adjusted basis and eligible basis (of any qualified low-income building) as of the close of the first year of the credit period.

Therefore, based on the facts and representations in the letters from Partnership's representative we rule as follows:

1. The Project was placed in service in calendar year 1987.
2. In that The Project has been placed in service in portions and Partnership has elected to defer the start of the 10-year credit period pursuant to section 42(f)(1) of the Code, the eligible basis of The Project shall include all expenditures properly chargeable to the capital account on The Project that are incurred during the first taxable year of the credit period.

No opinion is expressed or implied regarding the application of any other provisions of the Code or regulations. This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.

Temporary or final regulations pertaining to the issues addressed in this ruling have not been adopted. This ruling is issued under the authority of Rev. Proc. 87-7, 1987-2 I.R.B. 15, that enables the Service to issue rulings that previously would have been precluded by the provisions of section 5.07(2) of Rev. Proc. 88-1, 1988-1 I.R.B. 11. Therefore, this ruling may be modified or revoked by the Service. However, when the criteria in section

16.05 of Rev. Proc. 88-1 are satisfied, a ruling is not modified or revoked retroactively, except in rare or unusual circumstances.

Copies of this letter are being sent to the persons you have designated to receive it in accordance with the Powers of Attorney on file in this office.

A copy of this letter should be filed with the income tax return of each partner in Partnership for the first taxable year in the 10-year credit period, which is 1988 because of the election under section 42(f)(1) to defer the start of the credit period from 1987 to 1988.