Private Letter Ruling 8902039, IRC Section 42

Oct. 19, 1988

This letter is in response to your letter dated May 2, 1988, submitted on behalf of Partnership, in which you request a private letter ruling pertaining to the low-income housing credit under section 42 of the Internal Revenue Code.

The following relevant representations have been submitted for consideration:

Partnership is a limited partnership formed under the laws of State M for the purpose of acquiring, rehabilitating, and operating The Apartments, which is a low-income housing project. Corporation, of which you are Treasurer, is the general partner of Partnership.

Partnership acquired The Apartments from Seller on a for the total consideration of $b, comprised of the assumption of a $c mortgage insured by the United States Department of Housing and Urban Development and the execution of a $d purchase money note to Seller. The Apartments were placed in service by Partnership on the date of acquisition.

Your letter makes application for a waiver with respect to The Apartments of the 10-year holding period requirement prescribed in section 42(d)(2)(B)(ii) of the Code, which may be granted under the provisions of section 42(d)(6)(A). However, because the credit for acquiring a building is allowable only for buildings placed in service after 1986 and before 1991, no credit would be allowable with respect to the acquisition cost of buildings placed in service by Partnership in 1985 regardless of whether or not they had been held for 10 years by the prior owner. We have discussed this by telephone, you have advised that Partnership is aware of it, and you have stated that Partnership asks us to rule only on whether or not its proposed rehabilitation of the buildings can qualify for the "separate new building" treatment (and tax credits) under section 42(e) even though no credit is allowable on the buildings' acquisition cost.

With respect to certain buildings placed in service after 1986, sections 42(a) and 42(b) of the Code provide in general for the low-income housing credit. Section 42(b)(1) prescribes the credit rate or "applicable percentage" that is to be used in computing the credit for qualified low-income buildings placed in service in 1987 that are (1) new and federally subsidized for the taxable year, (2) new but not so subsidized, and (3) existing buildings. Similarly, section 42(b)(2) prescribes the applicable percentage for the same three categories of buildings placed in service after 1987. The credit rate that is applicable to a new building that is not federally subsidized for the taxable year placed in service is different (greater) than the credit rate applicable to the other two categories of buildings.

Section 42(d)(2) of the Code provides rules for determining the eligible basis of an existing building, which is a factor in the determination of its qualified basis. In general, the eligible basis of an existing building that meets certain requirements is the cost of its acquisition plus certain rehabilitation expenditures incurred by the taxpayer within a limited period of time. One of the requirements in section 42(d)(2)(B)(ii) is that, as of the date of its acquisition by the taxpayer, 10 years must have elapsed since the date the building was last placed in service. Section

42(d)(6)(A) provides rules under which in certain circumstances the 10-year holding period requirement may be waived.

Section 42(e)(1) of the Code provides that certain rehabilitation expenditures paid or incurred by the taxpayer with respect to any building shall be treated for purposes of that section as a separate new building. In general, rehabilitation expenditures may qualify for this new building treatment if the qualified basis attributable to such expenditures incurred during any 24-month period, when divided by the low-income units in the building, is $2,000 or more. The cost of the building's acquisition is not includable in such rehabilitation expenditures.

Section 42(e)(5) of the Code provides that rehabilitation expenditures may be treated either as a separate new building under section 42(e) or as an addition to the building's acquisition cost under section 42(d)(2), but may not be taken into account under both subsections. Section 42(e)(4) provides that nothing in section 42(d)(2) shall prevent a credit from being allowed by reason of section 42(e).

Under section 42(e)(4) of the Code, rehabilitation expenditures on an existing building that fail the 10-year holding period test of section 42(d)(2)(B)(ii) may qualify for the separate new building treatment of section 42(e) regardless of that failure.

Based on the representations in your letter of May 2, 1988, we rule as follows:

If rehabilitation expenditures are paid or incurred by Partnership with respect to The apartments in a sufficient amount as required by section 42(e) of the Code and those expenditures are treated as placed in service under the rules of section 42(e) before January 1, 1990, such expenditures will be treated as a separate new building within the meaning of section 42(e), regardless of whether The Apartments in the hands of Partnership meet the requirements of section 42(d)(2)(B)(ii).

No opinion is expressed or implied regarding whether Partnership's proposed rehabilitation expenditures will qualify otherwise for the low-income housing credit under section 42 of the Code.

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 one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling will be modified or revoked by adoption of temporary or final regulations, to the extent the regulations are inconsistent with any conclusions in the ruling. See section 16.04 of Rev. Proc. 88-1, 1988-1 I.R.B. 7, 19. However, when the criteria in section 16.05 of Rev. Proc. 88-1 are satisfied, a ruling is not revoked or modified retroactively, except in rare or unusual circumstances.

A copy of this letter should be filed with the income tax return of each partner in Partnership for the taxable year in which the transaction covered by this ruling is consummated.