Private Letter Ruling 8910014, IRC Section 42

December 7, 1988

This letter is in response to your letter dated June 22, 1988, submitted on behalf of Partnership and M, the general partner 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 organized under the laws of State L. The individuals currently holding a partnership interest in Partnership are M, N, and O. N and O are limited partners of Partnership. Partnership is currently doing business under the name P. Partnership will file its federal partnership return, Form 1065, with the Internal Revenue Service Center in City S. Partnership is under the audit jurisdiction of the District Director in City T.

Seller is a limited partnership organized under the laws of State L. Q is the general partner of Seller, and R is a limited partner. Q and R own 100 percent of the partnership interest in Seller.

On a, Partnership acquired the buildings, land, and improvements thereon that comprise the Project for the purpose of owning and operating the Project as an investment. Partnership purchased the Project from Seller for a sales contract price of $ b. Significantly, Partnership and Seller are not related parties as defined under (i) section 179(d)(2) of the Code, as applicable under section 42(d)(2)(D)(iii)(1) of the Code, or (ii) section 42(d)(2)(D)(iii)(11). As part of the consideration for sale, Partnership assumed Seller's outstanding mortgage indebtedness on the Project in the amount of approximately $ c.

The mortgage indebtedness assumed by Partnership represents the remaining outstanding principal and accrued interest payable to the United States of America, acting through the Farmers Home Administration (FmHA) of the Department of Agriculture under the terms of two promissory notes executed by Seller on d. The two promissory notes evidence the $ e section 515 Rural Rental Housing (RRH) loan extended by the FmHA to Seller, which was used by Seller to finance the acquisition of the Project in ***. One promissory note has a face amount of $ f with interest payable at a rate of g percent per annum, while a second promissory note has a face amount of $ h, with interest payable at a rate of g percent per annum.

The i buildings (which contain j apartment units) in the Project continue to be federally-assisted under section 515 of the Housing Act of 1949 in Partnership's hands as a result of its assumption of Seller's FmHA RRH mortgage indebtedness. Thus, Partnership is the new mortgagor of the Project and the FmHA remains the mortgagee.

Upon its acquisition of the Project, Partnership placed the Project buildings in service as low-income housing, and is currently in the process of rehabilitating the buildings. The Project buildings were last placed in service by Seller in ***. There have been no nonqualified substantial improvements (as defined in section 42(d)(2)(D)(i) of the Code) made to the Project since it was originally placed in service by Seller and Seller was not allowed a low-income housing credit under section 42 for the buildings in the Project.

On k, the FmHA accelerated Seller's RRH loan obligation and declared the entire unpaid loan balance immediately due and payable as a result of Seller's default on certain terms and conditions contained in the two promissory notes and the FmHA real estate mortgage agreement it executed in *** .

On l, the U.S. Attorney's office for U, on behalf of the United States, filed a suit in the U.S. District Court for U to foreclose Seller's FmHA mortgage, as a result of Seller's noncompliance with certain terms and conditions of its promissory notes and FmHA real estate mortgage agreement. On m, Seller filed an answer with the U.S. District Court for U, in response to the complaint filed by the U.S. Attorney's office.

By letter dated n, FmHA's local office advised Partnership that it should take title to the Project immediately in order to protect the reserve funds required by the original FmHA Loan Agreement executed between the FmHA and Seller. The Project was acquired on a, and Partnership currently believes that certain acquisition costs and rehabilitation expenditures relating to the Project will qualify for the low-income housing credit under section 42 of the Code. Partnership has received approval for such credit from the housing credit authority of State L, pending a favorable response to Partnership's ruling request.

In connection with the proposed claim for the credit under section 42 of the Code, Partnership represents that all terms and conditions of section 42 and related sections will be met except for the requirement in section 42(d)(2)(8)(ii); and Partnership asks that such requirement be waived under the authority given the Secretary of Treasury by section 42(d)(6)(A)(i).

Section 42(d) of the Code provides rules for determining the eligible basis of a new or existing building, a factor used in computing the amount of credit earned. In the case of an existing building that meets certain requirements the eligible basis consists of the building's acquisition cost plus rehabilitation expenditures incurred within a limited period of time. Section 42(d)(2)(B)(ii), however, requires that as of the date the building is acquired by the taxpayer at least 10 years must have elapsed since the later of the date the building was last placed in service or the date of the most recent nonqualified substantial improvement of the building.

Section 42(d)(6)(A)(i) of the Code provides that on application by the taxpayer, the Secretary may waive the 10-year requirement of section 42(d)(2)(B)(ii) with respect to any federally-assisted building if the Secretary (after consultation with the appropriate federal official) determines that such waiver is necessary to avert an assignment of the

mortgage secured by property in the project (of which such building is a part) to the Department of Housing and Urban Development or FmHA.

Section 42(d)(6)(B)(iii) of the Code defines the term "federally-assisted building" as including any building that is substantially assisted, financed, or operated under section 515 of the Housing Act of 1949.

Section 1.42-2T of the Temporary Income Tax Regulations contains requirements that must be satisfied to permit the waiver referred to in section 42(d)(6)(A)(i) of the Code.

We have examined Partnership's representations and have determined that the buildings in the Project are federally-assisted buildings within the meaning of section 42(d)(6)(B)(iii) of the Code, and that the Project's transfer to Partnership was approved by FmHA to avert foreclosure due to delinquencies and shortages in project accounts or to Seller's noncompliance with the terms and conditions of the real estate mortgages, and that the requirements of section 1.42-2T of the temporary regulations have been satisfied.

Based on the representations in your letter dated August 10, 1988, we rule as follows:

The requirement under section 42(d)(2)(B)(ii) of the Code is waived with respect to Partnership's acquisition of the Project.

No opinion is expressed or implied regarding whether Partnership's costs of acquisition and rehabilitation of the buildings in the Project 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.

In accordance with the power of attorney on file, this letter is being sent to you as the authorized representative of Partnership. A copy of this letter should be filed with each partner's income tax return for the tax year in which the transaction covered by this ruling is consummated.

We are sending a copy of this letter to FmHA in accordance with that agency's request.