Private Letter Ruling 8921035, IRC Section 42

February 23, 1989

This letter is in response to your letter dated February 29, 1988, and subsequent correspondence, submitted on behalf of Taxpayer, in which you request a letter ruling regarding the low-income housing credit under section 42 of the Internal Revenue Code. The represented facts are set forth below.

Taxpayer plans to purchase real estate and improvements containing approximately *** square feet located in Location X, which formerly comprised the Z (the "Real Estate"). Taxpayer will purchase the Real Estate from an individual. ("Seller") who purchased it in . . . from County Y. Seller did not rehabilitate or renovate the Real Estate and did not use it for housing. Seller leased a portion of the first floor of the Real Estate to County Y to be utilized as an office.

Taxpayer plans to purchase and renovate the Real Estate so that it can be used as a low-income housing project (the "Project") that would qualify for low-income housing credit under section 42 of the Code. Due to the nature of the facilities available in the Real Estate, Taxpayer further desires to offer meals to residents of the Project. The meals would be offered in a shared dining facility available to all residents of the Project. Taxpayer would require MANDATORY payment for one meal per day from each resident of the Project, as a condition of occupancy, in addition to the gross rent to be paid by the residents. All other meals and any other amenities and services offered by Taxpayer would be optional.

Taxpayer has requested a ruling that in the event it requires mandatory payment for one meal a day by each occupant of the Project as a condition of occupancy, the Project would be a "qualified low- income housing project" under section 42(g)(1)(A) of the Code.

Section 38(a) of the Code provides for a general business credit against tax that includes the amount of the current year business credit. Section 38(b)(5) provides that the amount of the current year business credit includes the low-income housing credit determined under section 42(a).

Section 42(a) of the Code, added by section 252 of the Tax Reform Act of 1986 (the "1986 Act"), 1986-3 (Vol. 1) C.B. 106, provides that, for purposes of section 38, the amount of the low-income housing credit determined under section 42 for any tax year in the credit period shall be an amount equal to the "applicable percentage" of the qualified basis of each qualified low-income building.

Section 42(g)(1) of the Code defines the term "qualified low- income housing project" to mean any project for residential rental property if the project meets the rent restriction requirements of section 42(g)(1)(A) or (B), whichever the taxpayer elects. The election is irrevocable. Section 42(g)(2)(A) provides that a unit is rent-restricted if the gross rent

(defined in section 42(g)(2)(B)) that is paid for the unit does not exceed 30 percent of the income limits that section 42(g)(1) imposes upon the occupants.

Notice 89-6, 1989-2 I.R.B. 16, states that regulations under section 42 of the Code will provide that the furnishing to tenants of services other than housing (whether or not such services are significant) will not prevent property from qualifying as residential rental property. However, any charges for services that are not optional to low-income tenants must be included in gross rent for purposes of section 42(g)(2)(A) of the Code. A service is optional if payment for the service is not required as a condition of occupancy. Thus, in certain circumstances, a retirement-type facility may qualify under section 42 as a residential rental facility, notwithstanding that significant services other than housing are furnished to tenants. However, if continual nursing, medical, or psychiatric care is provided, it will be presumed that such services are mandatory. This is generally the case with hospitals, nursing homes, sanitariums, and lifecare facilities.

Notice 89-6 provides an example where meals and other services are provided to low-income tenants in a retirement home. Under the example, the cost of these services, when combined with rent and utility allowances, exceeds the 30 percent gross rent limitation. If any low-income tenants are required to pay for these services as a condition of occupancy, then the units occupied by these tenants are not rent-restricted units and are not included in qualified basis. However, if payment for these services is OPTIONAL, then these units are rent-restricted units and are includible in qualified basis assuming that the gross rent limitation is otherwise satisfied. Where multiple services are provided, a building owner must decide which services are mandatory and included in the 30 percent gross rent limitation. All other services must be provided on an optional basis.

Based upon the above facts and representations, the residents of the Project will be required to pay for at least one meal per day and such payment is required as a condition of occupancy. Thus, the cost of the meals must be included in determining whether the 30 percent gross rent limitation of section 42(g)(2)(A) of the Code is exceeded.

Further, in order to determine the eligible basis of an existing building under section 42(d)(2)(A) of the Code, section 42(d)(2)(B)(ii) requires that there must be a period of at least 10 years between the date of the building's acquisition by the taxpayer and the later of either the date the building was last placed in service, or the date of the most recent nonqualified substantial improvement of the building. Section 42(i)(5) defines "existing building" as any building which is not a new building. Because Taxpayer represents that the Real Estate was originally purchased from County Y in *** section 42(d)(2)(B)(ii) prohibits the Real Estate from qualifying for the low-income housing credit under section 42.

Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Because this ruling is issued under the authority of Rev. Proc. 88-18, 1988- 20 I.R.B. 32, and section 5.07(3) of Rev. Proc. 89-1, 1989-1 I.R.B. 8, this ruling may be modified or revoked by the Service. However, when the criteria in

section 16.05 of Rev. Proc. 89-1 are satisfied, a ruling is not revoked or modified retroactively, except in rare or unusual circumstances.

A copy of this letter should be attached to the appropriate federal income tax return for the taxable year in which the transaction covered by this ruling is consummated.

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 Taxpayer.