Private Letter Ruling 8941035, IRC Section 42

July 14, 1989

This letter responds to your letter dated March 27, 1989, submitted on behalf of the Partnership as its authorized representative, requesting a ruling regarding the application of section 42(h)(1)(C) of the Internal Revenue Code to a reservation of low-income housing credit dollars made by the Authority to the buildings in the Project in a. The represented facts as they pertain to the request for a ruling are set forth blow.

BACKGROUND

The Partnership, a State A limited partnership, was formed on b, for the purpose of constructing the Project, a low-income housing project located in City. The Partnership anticipated that the Project would qualify for FmHA financing from the Farmers Home Administration under the Section 515 program and also for federal tax credits under section 42 of the Code. In order to be eligible to claim credits under section 42, an owner of a building must first receive a housing credit dollar allocation from the appropriate housing credit agency of the state in which the building is located.

ORGANIZATION OF THE PARTNERSHIP

The original general partners of the Partnership were C, who owned a bb percent interest, and his wife D, who owned a cc percent interest. The remaining dd percent interest was held by the sole limited partner, Corp E, a State A corporation.

A first Amended and Restated Agreement of limited Partnership was entered into effective as of c, which modified the interest of all of the partners. C and D remained as general partners and acquired a collective d percent interest in profits from the sale of the Project, a e percent interest in operative profits, and a e percent interest in losses. Corp F, a State B corporation, also became a general partner and acquired a f percent interest in profits from the sale of the Project, a f percent interest in operating profits, and a f percent interest in losses. Partnership G, a State B Limited partnership, became the sole limited partner and acquired a g percent interest in profits from the sale of the Project, a h percent interest in operating profits, and a h percent interest in losses. Corp E withdrew and ceased to hold any equity interest in the Partnership.

CONSTRUCTION OF THE PROJECT

The Partnership began construction of the Project on i. On j, Corp E, on behalf of the Partnership, sent to the Authority the Partnership's application for an allocation of housing credit dollars. The cover letter that accompanied this application stated that because construction of the Project was not expected to be completed until k, the Partnership did not intend the allocation to be effective until 1.

On m, the Authority notified Corp E by letter that a housing credit dollar amount of $ n had been reserved for the Project. The letter stated that "

{i} in the event that tax credits are not allocated this calendar year, these credit funds will be reserved from the Authority's 1 allocation." The letter also stated " {p} lease notify us when the project is placed in service and you wish to have our Authority allocate the tax credit."

On o, Corp E notified the Authority that the Partnership had miscalculated its basis in the Project and it requested that the reservation be increased to $ p. The authority responded on q, by approving the new reservation amount.

Construction of the Project was completed on r, and at least a portion of the units were occupied by s. Consistent with its j, letter, the Partnership did not request the Authority to make an allocation for u. By letter dated t, Corp E, on the Partnership's behalf, requested the Authority to make the allocation for 1 pursuant to this reservation made in u. Following this request, the Authority allocated 1 housing credit dollars to the Project buildings by issuing Form 8609's under cover of a letter dated v.

Upon receiving this letter and the enclosed Form 8609's, the Partnership discovered that the letter and the forms erroneously specified the maximum applicable percentage as the applicable percentage for w, instead of the applicable percentage for x, the month in which the buildings were placed in service. By letter dated y, Corp E, on the Partnership's behalf, requested that the error be corrected. In response, the Authority on z, issued revised Form 8609's for the Project's buildings specifying the applicable percentage for x, as the maximum applicable percentage for the 1 allocation of housing credit dollars (the "Revised Form 8609's").

In a letter to the Partnership dated aa, the Authority stated that it had adopted the procedure of issuing a reservation letter as its method of issuing a binding commitment pursuant to section 42(h)(1)(C) of the Code. More specifically, the Authority stated that the reservation letter to Corp E dated m, as supplemented by the letter dated q, constituted a binding commitment by the Authority to allocate in 1 $ p in housing credit dollars to the buildings in the Project.

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, 1986-3 (Vol. 1) C.B. 106, as amended by the Technical and Miscellaneous Revenue Act of 1988 (Pub. L. 100-647), 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(c)(2)(A) of the Code defines the term "qualified low- income building" as any building that is part of a qualified low- income housing project at all times during the period beginning on the 1st day in the compliance period on which such building is part of such a project, and ending on the last day of the compliance period with respect to such building.

Section 42(g)(1) of the Code defines the term "qualified low- income housing project" as any project for residential rental property if the project meets the requirements of subparagraph (A) or (B), whichever the taxpayer elects. The election is irrevocable. Section 42(g)(1)(A) states that the project meets the requirements of subparagraph (A) if 20 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 50 percent or less of area median gross income, as adjusted for family size. Section 42(g)(1)(B) states that the project meets the requirements of subparagraph (B) if 40 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 60 percent or less of area median gross income, as adjusted for family size.

Section 42(g)(2)(A) of the Code provides that a residential unit is rent-restricted if the gross rent (defined in section 42(g)(2)(B)) that is paid for the unit does not exceed d percent of the income limitation that section 42(g)(1) imposes upon the occupants of such unit.

Section 42(h) of the Code mandates a local/state allocation procedure by which a state housing credit agency may allocate low- income housing credit dollar amounts to qualified low-income housing buildings within the agency's jurisdiction. Section 1.42-1T(c)(1) of the Temporary Regulations, that were published on June 22, 1987, define a "State housing credit agency" as any State agency specifically authorized by gubernatorial act or State statute to make housing credit allocations on behalf of the State and to carry out the provisions of section 42(h).

Section 42(h)(1)(B) of the Code provides the general rule that an allocation of a housing credit dollar amount shall be taken into account only if it is made not later than the close of the calendar year in which the building is placed in service. The only exceptions to this general rule are contained in subsections (C),(D), or (E) of section 42(h)(1). Under section 42(h)(1)(C), an allocation may be made in a year succeeding the calendar year in which a building is placed in service if, there is a binding commitment (not later than the close of the calendar year in which the building is placed in service) in which the housing credit agency agrees to allocate a specified housing credit dollar amount to such building beginning in a specified later taxable year. Under section 42(h)(1)(D), an allocation may be made in a year succeeding the calendar year in which a building is placed in service if, during such later year, there is an increase in the building's qualified basis from the qualified basis of the building during the previous year. Finally, under section 42(h)(1)(E), an allocation may be made in a year preceding the calendar year in which a building is placed in service if, (i) the building is placed in service not later than the close of the second calendar year following the calendar year in which the allocation is made,

and (ii) the taxpayer's basis in the low-income housing project (as of the close of the calendar year in which the allocation is made) is more than 10 percent of the taxpayer's reasonably expected basis in such project (as of the close of the second calendar year referred to in clause (i)).

State housing credit agencies may allocate a credit by one of two methods. The first method is outlined in section 1.42- 1T(d)(8)(ii) of the temporary regulations and states that housing credit allocations are deemed made when Part I of IRS Form 8609, Low-Income Housing Credit Allocation Certification, is completed and signed by an authorized official of the housing credit agency and mailed to the owner of the qualified low-income building. The second method is limited to the section 42(h)(1)(E) exception to the general rule in section 42(h)(1)(B) that allocations by state housing credit agencies must be made not later than the close of the calendar year in which a building is placed in service. An allocation pursuant to section 42(h)(1)(E) is made by an allocation document that satisfies the procedural and informational requirements for such allocations as required in Notice 89-1, 1989-2, I.R.B. 10.

Section 1.42-1T(d)(8) of the temporary regulations provides that a State housing credit agency may provide a procedure for making, in advance of a building's being placed in service, a binding commitment (e.g., by contract, inducement, resolution, or other means) to make a housing credit allocation in the calendar year in which a qualified low-income building is placed in service or in a subsequent calendar year. The regulation also provides that any advance commitment shall not constitute a housing credit allocation for purposes of this section. However, the retroactive application of the amendments to section 42(h)(1) of the Code made by the Technical and Miscellaneous Revenue Act of 1988 supersede this provision and provides that a binding commitment under section 42(h)(1)(C) is an allocation that meets the requirements of section 42(h). Accordingly, a procedure adopted by a State housing credit agency for making, in advance of a building's being placed in service, a binding commitment of housing credit dollar amounts, will satisfy the requirements of section 42(h)(1)(C). Such a procedure had been adopted by the Authority by the issuance of reservation letters. Specifically, the Authority stated that the reservation letter to Corp E on behalf of the Partnership dated m, as supplemented by the letter dated q, constituted a binding commitment by the Authority to allocate in 1 $ p in housing credit dollars to the buildings in the Project.

Therefore, based upon the above facts and representations, we rule that the m, and q, letters from the Authority to Corp E reserving housing credit dollar amounts to the Project buildings constituted a "binding commitment" on the part of the Authority in u under Section 42(h)(1)(C) to allocate a specified housing credit dollar amount to the buildings in the Project in 1, and that the Authority's allocation in 1 of $ p in housing credit dollars to the Project buildings under the revised Form 8609's qualifies under section 42(h)(1)(C).

No opinion 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.

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.

In accordance with the power of attorney on file, the original of this letter is being sent to you as the taxpayer's authorized representative.

A copy of this letter should be attached to the federal income tax return of Partnership for the taxable year in which the transaction contained in this letter ruling was consummated.

Sincerely yours,

James F. Ranson

Chief, Branch 5

Office of the Assistant Chief Counsel

(Passthroughs and Special Industries)