

Private Letter Ruling 9537007, IRC Section 42

Date: June 15, 1995

Dear \*\*\*

This letter responds to the letter dated April 13, 1995, and subsequent correspondence submitted on behalf of Partnership, requesting a private letter ruling that will waive, for the Project, the 10-year holding period requirement in section 42(d)(2)(B)(ii) of the Internal Revenue Code under the authority of the exception provided in section 42(d)(6)(A)(ii).

Partnership has made the following representations:

Partnership was formed for the purpose of acquiring, rehabilitating, owning, developing, and managing as an investment and a business, certain residential real estate located in City A, State B, and known as the Project. Corp M, the general partner of Partnership, is a wholly owned subsidiary of Corp O, which is itself a wholly owned subsidiary of Corp P, a State C charitable corporation exempt from federal income taxes under section 501(c)(3). Partnership's initial limited partner is Corp N, which is also a State C charitable corporation. Corp M, owns a b percent partnership interest and Corp N owns the remaining c percent partnership interest in Partnership.

Seller, a State B limited partnership, placed the Project in service in t1, and financed the property through a mortgage loan held by the United States Department of Housing and Urban Development (HUD). However, Seller developed substantial arrearages on this HUD-held mortgage causing the assignment of the loan to HUD on t2. The Project was subject to the possibility of foreclosure.

The Project consists of d buildings housing e residential apartment units. On t3, Partnership acquired the Project from Seller for a total consideration of \$f. The terms of the acquisition include payment of \$g plus Seller's closing costs and the assumption by Partnership of the existing first mortgage. HUD approved the purchase transaction, including the assumption of the mortgage and the assignment the section 8 housing assistance payments. Also, on t3, HUD acting as an authorized agent of the Federal Housing Commissioner agreed with Partnership to the terms of a mortgage modification. Under this agreement the terms of the Original Note between HUD and Seller were substituted with three separate notes. Note A in the principal amount of \$h reflected a portion of the outstanding principal balance on the Original Note as of t4. Note B in the principal amount of \$i reflected the remaining portion of the outstanding principal balance on the Original Note as of t4, and Note C in the principal amount of \$j reflected the arrearage due on the Original Note as of t4.

On t5, Partnership received from Authority a t6 carryover allocation of low income housing credits dollar amount of \$k. The cost of capital improvements to the buildings in the Project, as well as deposits to reserves and transactions costs will be met by equity

raised through the sale of limited partnership interests in Partnership. Partnership anticipates that this process will assure a useful life for the Project which exceeds the investment period and protects the mortgage principal which will be remaining.

Partnership currently estimates that rehabilitation expenses for the Project will be \$1, or approximately \$m per low-income unit which is in excess of the minimum requirements of section 42(e)(3).

The Partnership certifies that the Project is substantially assisted under section 8 of the United States Housing Act of 1937, and therefore consists of federally-assisted buildings under section 42(d)(6)(B)(i) and section 1.42-2(c)(1) of the Income Tax Regulations. Partnership has also provided evidence that it has taken assignment of the Project's section 8 housing assistance payments and has attached to this ruling request the required documentation.

In a letter dated t7, the National Office of the Internal Revenue Service was informed that the Project is a "troubled project" by the National Office of HUD. A copy of the letter is attached to the request for this letter ruling.

Partnership has made the following representations and certifications with respect to the Project: (1) The acquisition of the buildings in the Project is by purchase (as defined under section 179(d)(2) and as further restricted by section 42(d)(2)(D)(iii)(I)); (2) Partnership acquired the buildings in the Project for the purpose of providing affordable housing to qualified low-income households; (3) The buildings in the Project were not previously placed in service by Partnership, or by a person who was a related person (as defined in section 42(d)(2)(D)(iii)(II)) with respect to Partnership at the time the buildings were last placed in service; (4) As of t7, the buildings in the Project were "federally-assisted buildings" as defined in section 42(d)(6)(B)(i), and section 1.42-2(c)(1) of the Income Tax Regulations; (5) As of t7, federal mortgage funds with respect to the Project were at risk within the meaning of section 1.42-2(c)(2); (6) There have been no nonqualified substantial improvements to the buildings in the Project since there were last placed in service; (7) To the best of knowledge of Partnership and its representatives, no prior owner of the Project was allowed a low-income housing credit under section 42 for the Project; (8) All terms and conditions of section 42 and related sections, including substantial rehabilitation in excess of the minimum provided by section 42(e)(3), will be met except for the 10-year holding period requirement provided by section 42(d)(2)(B)(ii). Partnership asks that this requirement be waived under the authority granted the Secretary of the Treasury by section 42(d)(6)(A)(ii); and (9) This application for the waiver is timely filed as it is within 12 months after the acquisition of the Project.

Section 42(d) provides rules for determining the eligible basis of a new or existing building, a factor used in computing the amount of credit earned. 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)(ii) provides an exception of the 10-year holding period requirement of section 42(d)(2)(B)(ii) to the effect that on application by the taxpayer, the Secretary may waive this requirement 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 a claim against a federal mortgage insurance fund (of the Department of Housing and Urban Development or the Farmers' Home Administration).

Section 42(d)(6)(B) defines the term "federally-assisted buildings as including any building that is substantially assisted, financed, or operated under section 8 of the United States Housing Act of 1937, section 221(d)(3) or 236 of the National Housing Act, or section 515 of the Housing Act of 1949, as such Acts are in effect on the date of enactment of the Tax Reform act of 1986 (October 22, 1986).

Section 1.42-2 contains requirements that must be satisfied to permit the waiver referred to in section 42(d)(6)(A). Partnership has represented that it is in compliance with these requirements.

After examining the representations submitted, we have determined that the buildings in the Project are federally-assisted buildings, within the meaning of section 42(d)(6)(B)(i) and that federal funds are at risk under section 42(d)(6)(A)(ii). In addition, the requirements of section 1.42-2 have been satisfied.

Therefore, based on the above facts and representations as submitted, we rule as follows: The 10-year holding period requirement under section 42(d)(2)(B)(ii) is waived with respect to Partnership's proposed 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 otherwise qualify for the low-income housing credit under section 42.

This ruling is directed only to Partnership which requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent. A copy of this letter should be filed with the federal income tax return for Partnership and the respective partners for the taxable year in which the transaction covered by this ruling is consummated.

We are sending a copy of this letter to the HUD in accordance with that agency's request. We are also sending a copy of this letter to \*\*\*.

Sincerely yours,

JAMES F. RANSON

Chief, Branch 5

Office of the Assistant Chief Counsel

(Passthroughs and Special Industries)