January 30, 2013

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2012-25)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Mr. Paul F. Handleman
Chief, Branch 5
Office of Associate Chief Counsel
Department of the Treasury
Internal Revenue Service
Washington, DC 20224

and

Mr. Mark J. Mazur
Assistant Secretary (Tax Policy)
Department of the Treasury
1500 Pennsylvania Ave., NW
Room 3120
Washington, DC 20220

RE: Notice 2012-25, Guidance Priority List

Dear Ladies and Gentlemen:

The LIHTC Working Group was established to provide a platform for low-income housing tax credit ("LIHTC") industry participants to work together to resolve technical and administrative LIHTC program issues. On behalf of the members of the LIHTC Working Group, we are requesting guidance on questions regarding the potential loss of rural status for affordable housing projects whose income is determined using the national non-metro median income in accordance with Internal Revenue Code Section 42(i)(8). We request that you add this issue to the list of current Internal Revenue Service ("IRS") regulation projects and issue an IRS Notice outlining the guidance that the regulations will provide.

Internal Revenue Code Section 42 ("Section 42") provides LIHTCs to investors through their investments in the construction of low-income housing projects, contingent on continued compliance with Section 42 guidelines over a 15-year compliance period[1]. It is up to the

[1] Internal Revenue Code Section 42(h)(6)(D)(ii)(II)

managers of these housing projects to ensure the projects continue to operate as a going concern over this compliance period; therefore, the project must collect sufficient rental revenues to cover property expenses while observing rent limits imposed by Section 42.

Achievement of this goal has been historically difficult for projects based in areas which are considered to be "rural." Income and rental limits associated with these projects tend to be low, eliminating a considerable portion of potential tenants and preventing management from charging rent at rates necessary to cover operating expenses. These difficulties often cast a pall of uncertainty over the feasibility of affordable housing projects in rural areas.

Since its inception in 1949, it has been the USDA's mission to assist with the development of housing in rural areas, including support for the development of affordable housing projects. The USDA's Rural Development ("RD") programs provide these projects access to specialized credit, mortgage loans, and other forms of capital which, among their many benefits, fund development costs of rural projects. The USDA has, historically, employed census population figures in the determination of a project's eligibility for its RD programs, granting access to those communities with populations below a particular threshold, traditionally 20,000.

In 1983, however, an amendment was made to the Housing Act of 1949 which protected areas in which the population had grown past USDA limits from losing their rural designations. This "grandfather" clause has been renewed multiple times, most recently to allow communities with populations up to 25,000 to retain eligibility if they were eligible under the 1990 or 2000 census.[2] Nevertheless, with the most recent expiration of the aforementioned clause on September 30, 2012, numerous projects in areas qualified under the "grandfathering" principle now face a sudden loss of their rural status, and benefits of said status, which would affect future development of LIHTC properties and would affect access to loans and other sources of funding for new and existing properties, thus greatly reducing the feasibility of rural projects.

In addition to the loss of access to USDA sources of financing in any instance of future refinancing or rehabilitations, projects financed with 9% credits in affected areas would also lose the ability use the national nonmetropolitan median income ("NNMI") in the determination of Section 42 rent and income limits.[3] This option not only allows rural projects where NNMI is greater than area medina gross income ("AMGI") to increase rent limits, therefore increasing annual rental revenue to cover operating expenses, but also increases the number of potential tenants who meet qualifications for occupancy. Given that vacancy issues is one of the most prevalent problems plaguing the development of affordable housing in rural areas, the loss of this option may be catastrophic to the continuing operation of these projects as going concerns.

For example, a project located in Jasper County, Missouri with 40 units, electing the 40/60 minimum set-aside, and is 100% affordable that uses the NNMI could generate $30,240 more revenue each year, because such a project could generate $377,280 of annual rental income as

---

[2] Housing Act of 1949, Section 520

[3] Internal Revenue Code Section 42(i)(8)

compared to a project without NNMI, which could generate only $347,040 of annual rental income. This disparity in rental revenue is a result of the higher income limit, and consequent rent limit, enabled by the use of NNMI. The above project using the NNMI would be subject to an income limit of $31,440 and a rent limit of $786. Conversely, a similar project not using the NNMI would be subject to the lower income limit of $28,920 and consequently lower rent limit of $723. The hypothetical project using the NNMI would be able to cover a greater amount of operating expenses, as well as support more debt payments, making the project more economically feasible. Such a project would also be able to target 5% more of the population, which would help keep vacancy loss lower than a project that is not able to use NNMI.

In lieu of an act of Congress to extend the "grandfather" clause for rural areas, projects in danger of losing their rural distinction may yet avoid the loss of the option afforded them under Internal Revenue Code Section 42(i)(8). According to Internal Revenue Code Section 142, any determination of a project's AMGI for any calendar year after 2008 cannot be lower than the AMGI initially determined for the same project.[4] As Section 42(i)(8) indicates, any income limitation that makes reference to AMGI will be replaced by the greater of NNMI or AMGI. However, it is unclear, whether or not this hold harmless provision applies to projects which have lost rural status and, therefore, are no longer eligible to employ NNMI in place of AMGI. In LIHC Newsletter #48, Grace Robertson with the IRS indicated that if a project loses its rural status they would have to start using AMGI when the new limits are released. However, as the use of NNMI in favor of AMGI by qualified projects is ultimately treated similarly to the use of AMGI by any other project, and such use of NNMI has made qualified rural projects economically feasible, it stands to reason that such a hold harmless provision should be applied.

We request that the IRS issue guidance stating that if a project losses it rural status the project would be able to continue to be held harmless at the highest NNMI that the project achieved before it lost its rural status. We would, therefore, request that such guidance be administered, that this issue be added to the 2012-2013 Guidance Priority List and a list of current IRS regulation projects.

---

[4] Internal Revenue Code Section 142(d)(2)(E)(i)

We appreciate the opportunity to comment on this issue. The furtherance of this issue will help the LIHTC program better provide affordable housing and help increase the number of jobs in our communities by providing clarification and lessening the risks in the LIHTC program compliance. Thank you in advance for your time and careful consideration of this issue. Please do not hesitate to contact us if you have any questions regarding our comments or if we can be of further assistance.

THE LIHTC WORKING GROUP

Very truly yours,

NOVOGRADAC & COMPANY LLP

by

Michael J. Novogradac

NOVOGRADAC & COMPANY LLP

by

Stacey L. Stewart