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Person To Contact:
,
Telephone Number:

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Date:
February 28, 2006

In Re:

LEGEND

Taxpayer =

State =

City =

Agency =

Year 1 =

Year 2 =

Year 3 =

a =

Dear :

This letter responds to a letter dated December 22, 2005, submitted on behalf of Taxpayer concerning the applicable percentage under § 42(b) of the Internal Revenue Code and the eligible basis rules for existing buildings under § 42(d)(2).

Taxpayer represents that the facts are as follows:

FACTS

Taxpayer, a State limited partnership, is the owner of a a-unit apartment complex in City (Property 1). Taxpayer began construction on Property 1 in Year 2 and completed in the fall of Year 3. Property 1, which is fully occupied and operating, has been the subject of ongoing litigation between Taxpayer and City since early in Year 2. The litigation has been heard in the local circuit court numerous times, the appellate court, and the State Supreme Court. Property 1 is currently the subject of a federal discrimination lawsuit with Property 1's lender as the plaintiff and City as the defendant. Property 1's tenants are part of the lawsuit as intervenors.

Taxpayer originally submitted an application for an allocation of low-income housing credits to Agency in Year 1 and again in Year 2. Due to the ongoing litigation, Agency cancelled Taxpayer's credit reservation.

At the urging of the court, City has indicated a willingness to settle with Taxpayer if Taxpayer purchases an adjacent property (Property 2) and tears it down to reduce density. In order to enter maintain Property 1 as affordable housing, Taxpayer would create a new entity to which it would sell Property 1. The new entity would then acquire Property 2 and submit an application for a new allocation of low-income housing credits to Agency. The current ownership of Taxpayer would own more than 10 percent of the new entity. Property 2 was placed in service by its current owner less than 10 years ago.

RULING REQUESTED

Taxpayer requests a ruling that would allow: (a) the 70-percent present value low-income housing credit on the acquisition by the new entity of Property 2; (b) the 70-percent present value low-income housing credit be calculated on the entire acquisition price of Property 2, including the land, regardless of the fact that it violates § 42(d)(2)(B)(ii) and that Property 2 will be torn down; (c) the 70-percent present value low-income housing credit on the acquisition by the new entity of Property 1; and (d) a determination that there is no violation of § 42(d)(2)(B)(iii).

LAW AND ANALYSIS

Section 42(a) provides that the amount of the low-income housing credit for any taxable year in the credit period is an amount equal to the applicable percentage of the qualified basis of each qualified low-income building.

Section 42(b)(2)(A) provides, in the case of any qualified low-income building placed in service by the taxpayer after 1989, that the term "applicable percentage" means the appropriate percentage prescribed by the Secretary for the month applicable under § 42(b)(2)(A)(i) or (ii). Section 42(b)(2)(B) provides that the percentages

prescribed by the Secretary for any month shall be the percentages that will yield over a 10-year period amounts of credit that have a present value equal to (i) 70 percent of the qualified basis of new buildings that are not federally subsidized for the taxable year (the 70-percent present value low-income housing credit), and (ii) 30 percent of the qualified basis of new buildings that are federally subsidized for the taxable year and existing buildings (the 30-percent present value low-income housing credit).

Section 42(c)(1)(A) provides that the qualified basis of any qualified low-income building for any taxable year is an amount equal to the (i) applicable fraction (determined as of the close of the taxable year) of (ii) the eligible basis of the building (determined under § 42(d)(5)).

Section 42(d)(2)(A) provides that the eligible basis of an existing building is (i) in the case of a building that meets the requirements of § 42(d)(2)(B), its adjusted basis as of the close of the first taxable year of the credit period, and (ii) zero in any other case. Section 42(d)(2)(B) provides that a building meets the requirements of § 42(d)(2)(B) if (i) the building is acquired by purchase (as defined in § 179(d)(2)), (ii) there is a period of at least 10 years between the date of its acquisition by the taxpayer and the later of (I) the date the building was last placed in service, or (II) the date of the most recent nonqualified substantial improvement of the building, (iii) the building was not previously placed in service by the taxpayer or by any person who was a related person with respect to the taxpayer as of the time previously placed in service, and (iv) except as provided in § 42(f)(5), a credit is allowable under § 42(a) by reason of § 42(e) with respect to the building.

The legislative history to § 42 states:

> Eligible basis consists of (1) the cost of new construction, (2) the cost of rehabilitation, or (3) the cost of acquisition of existing buildings acquired through a purchase and the cost of rehabilitation, if any, to such buildings incurred before the close of the first taxable year of the credit period. Only the adjusted basis of the building may be included in eligible basis. The adjusted basis is determined by taking into account the adjustments described in § 1016 (other than paragraphs (2) and (3) of § 1016(a), relating to depreciation deductions), including, for example, the basis adjustment provided in § 48(g) for any rehabilitation credits allowed under § 38. The cost of land is not included in adjusted basis.

H.R. Rep. No. 841, 99th Cong., 2d Sess. 89 (1986), 1986-3 C.B. (Vol. 4) 89.

Section 42(d)(2)(D)(iii)(II) provides that for purposes of § 42(d)(2)(B)(iii), a person is related to any person if the related person bears a relationship to such person specified in § 267(b) or § 707(b)(1) (substituting “10 percent” for “50 percent”), or the

related person and such person are engaged in trades or businesses under common control (within the meaning of § 52(a) and (b)).

Section 42(e)(1) provides that rehabilitation expenditures paid or incurred by the taxpayer with respect to any building shall be treated for purposes of § 42 as a separate new building. Under § 42(f)(5)(A), the credit period for an existing building shall not begin before the first taxable year of the credit period for rehabilitation expenditures with respect to the building.

Accordingly, based solely on the plain language of § 42 and its legislative history and the representations of fact made by Taxpayer, we rule as follows:

(a) Property 2 is not eligible for the 70-percent present value low-income housing credit because the 70-percent present value low-income housing credit is only available to new buildings that are not federally subsidized for the taxable year.

(b) If an eligible basis were calculated for the new entity's acquisition of Property 2, it would be zero because, under § 42(d)(2)(B)(ii), there is not a period of at least 10 years between the date of its acquisition by the new entity and the date the building was last placed in service. Even if this were not the case, the eligible basis would not include the cost of the land because the legislative history to § 42 states that the cost of land is not included in adjusted basis. In addition, because Property 2 will not be rehabilitated and will be torn down, the new entity may not claim low-income housing credits for Property 2.

(c) Property 1 is not eligible for the 70-percent present value low-income housing credit upon its acquisition by the new entity because the 70-percent present value low-income housing credit is only available to new buildings that are not federally subsidized for the taxable year.

(d) If an eligible basis were calculated for the new entity's acquisition of Property 1, it would be zero because, under § 42(d)(2)(B)(iii), the building was previously placed in service by a person who was a related person with respect to the new entity as of the time previously placed in service.

Except as specifically set forth above, no opinion is expressed or implied concerning the federal income tax consequences of the above described facts under any provision of the Code or regulations. Specifically, nothing in this ruling shall be construed to imply that either Property 1 or Property 2 are eligible for the 30-percent present value low-income housing credit under § 42.

In accordance with the power of attorney filed for this request, we are sending a copy of this letter to Taxpayer's authorized representative. This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,

/s/ Paul F. Handleman

Paul F. Handleman
Senior Technician Reviewer
Branch 5
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

cc: