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LEGEND

Sub-CDE   =

Allocatee   =

Fund   =

X   =

Y   =

D1   =

D2   =

D3   =

D4   =

D5   =

D6   =

D7   =

a   =

b   =
c   =

Dear   :

This letter responds to your letter dated November 22, 2013, and related correspondence, submitted on behalf of Sub-CDE, requesting a letter ruling involving the new markets tax credit (NMTC) under § 45D of the Internal Revenue Code. The ruling concerns the application of the 6-month cure period under § 1.45D-1(e)(6) of the Income Tax Regulations to the transaction described below.

FACTS

The information submitted states that Allocatee, a nonprofit corporation, and Sub-CDE, a limited liability company (LLC), were formed to serve or provide investment capital for low-income communities or low-income persons. Allocatee became a qualified community development entity (CDE) on D1. Sub-CDE became a CDE on D2.

X, a national banking association, wholly owns Y, an LLC. Y wholly owns Fund, also an LLC. Both Y and Fund are treated as disregarded entities for federal tax purposes.

Pursuant to an allocation agreement effective D3, the Department of Treasury Community Development Financial Institutions Fund made a NMTC allocation to Allocatee. Based on that allocation, Allocatee sub-allocated $*a* of NMTC to Sub-CDE. On D4, X, through Y, made a capital contribution in the amount of $*a* to Fund. Fund, in turn, made a capital contribution of $*a* in cash to Sub-CDE in exchange for a *b*% membership interest. Allocatee holds the remaining *c*% membership interest in Sub-CDE. On or about D3, Sub-CDE designated Fund's capital contribution in Sub-CDE as a qualified equity investment (QEI).

Sub-CDE, X, and Fund have worked diligently to find qualified low-income community investments (QLICIs) to invest the cash by D5, in order to satisfy the substantially-all requirement under § 45D(b)(1)(B) by the end of the 12-month period specified in § 1.45D-1(c)(5)(iv). The parties have considered a number of projects. Due to difficult circumstances, however, the parties have not been able to close on any of the projects. On D6, Sub-CDE became aware (or reasonably should have become aware) of its inability to invest in any of the QLICIs by D5.

RULING REQUESTED

The 6-month cure period described in § 1.45D-1(e)(6) is available to correct <u>Sub-CDE</u>'s failure to invest substantially all of the proceeds of the QEI in a QLICI within the 12-month period specified in § 1.45D-1(c)(5)(iv).

LAW AND ANALYSIS

Section 45D(a)(1) provides that, for purposes of § 38, in the case of a taxpayer who holds a QEI on a credit allowance date of such investment which occurs during the taxable year, the NMTC for such taxable year is an amount equal to the applicable percentage of the amount paid to the CDE for such investment at its original issue. Section 45D(a)(3) provides that the term "credit allowance" date means, with respect to any QEI, (A) the date on which such investment is initially made, and (B) each of the 6 anniversary dates of such date thereafter.

Section 45D(b)(1) provides that the term QEI means any equity investment in a CDE if (A) such investment is acquired by the taxpayer at its original issue (directly or through an underwriter) solely in exchange for cash, (B) substantially all of such cash is used by the CDE to make QLICIs, and (C) such investment is designated for purposes of § 45D(b) by the CDE.

Section 45D(d)(1) provides that the term QLICI means (A) any capital or equity investment in, or loan to, any qualified active low-income community business, (B) the purchase from another CDE of any loan made by such entity which is a QLICI, (C) financial counseling and other services to businesses located in, and residents of, low-income communities, and (D) any equity investment in, or loan to, any CDE.

Section 1.45D-1(c)(5)(i) provides that, except for the seventh year of the 7-year credit period, the term "substantially all" means at least 85 percent. The substantially all requirement must be satisfied for each annual period in the 7-year credit period using either the direct-tracing calculation or the safe-harbor calculation as provided in the section. For the first annual period, the substantially-all requirement is treated as satisfied if either the direct-tracing calculation or the safe-harbor calculation is performed on a single testing date and the result of the calculation is at least 85 percent.

Section 1.45D-1(c)(5)(iv) provides that the taxpayer's cash investment received by a CDE is treated as invested in a QLICI only to the extent that the cash is so invested within the 12-month period beginning on the date the cash is paid by the taxpayer (directly or through an underwriter) to the CDE.

Section 1.45D-1(e)(6) provides that, if a QEI fails the substantially-all requirement, the failure is not a recapture event if the CDE corrects the failure within 6 months after the date the CDE becomes aware (or reasonably should have become

aware) of the failure. Only one correction is permitted for each QEI during the 7-year credit period.

CONCLUSION

Under § 45D(a)(3)(A), the first NMTC is claimed on the date on which the QEI is initially made. Section 45D(b)(1)(B) includes within the definition of a QEI any equity investment in a CDE if substantially all of such cash is used by the CDE to make QLICIs. Section 1.45D-1(c)(5)(iv) provides that the taxpayer's cash investment received by a CDE is treated as invested in a QLICI only to the extent that the cash is so invested within the 12-month period beginning on the date the cash is paid by the taxpayer (directly or through an underwriter) to the CDE. Failure to meet the substantially-all requirement within the 12-month period means that the taxpayer's cash investment is not treated as a QEI on the date the taxpayer's initial investment is made. However, § 1.45D-1(e)(6) provides a one-time 6-month cure period if a QEI fails the substantially-all requirement.

Based on the information submitted and representations made, we conclude that the 6-month cure period under § 1.45D-1(e)(6) is available to correct Sub-CDE's failure to invest substantially all of the proceeds the QEI in a QLICI by D5. However, the 6-month cure period is not automatically tacked on to the 12-month period specified in § 1.45D-1(c)(5)(iv). As the rule states, the 6-month cure period begins on the date the CDE becomes aware (or reasonably should have become aware) of the failure to invest substantially all of the QEI proceeds in a QLICI within the 12 month period. On D6, Sub-CDE became aware (or reasonably should have become aware) of its inability to invest in any QLICIs by D5. Therefore, Sub-CDE must correct its failure to invest substantially all of the proceeds of the QEI in a QLICI no later than D7.

We express no opinion regarding the application of any other provisions of the Code or regulations.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter ruling will be sent to your authorized representative.

Sincerely,

Paul F. Handleman
Chief, Branch 5
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter
Copy for § 6110 purposes