

Internal Revenue Service

Department of the Treasury

Index Nos.: 42.04-06

42.08-04

Number: 199917046

Release Date: 4/30/1999

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CC:DOM:P&SI:5 — PLR-118685-98

Date: 01/29/99

In re: Request for Private Letter Ruling under § 42(h)(4)(B)

Legend:

Partnership =

State X =

City Y =

County Z =

District =

a =

b =

c =

d =

e =

f =

g =

h =

i =

j =

k =

l =

m =

n =

o =

p =

q =

Dear :

This letter responds to a letter dated September 23, 1998, and subsequent correspondence, submitted on behalf of the Partnership by the Partnership's authorized representative. In that letter, rulings are requested regarding the rehabilitation of a building financed by tax-exempt bonds for purposes of § 42(h)(4)(B) of the Internal Revenue Code.

The Partnership has made the following representations:

The Partnership was organized on a as a State X limited partnership. The Partnership is under the examination jurisdiction of the District. The Partnership was formed to acquire, rehabilitate, construct, and operate a low-income housing project located in City Y. The property is located in census tract b that the Partnership represents to be a qualified census tract for purposes of § 42(d)(5)(C)(ii).

On c, County Z issuing authority issued bonds with a face amount of \$d for the project. The Partnership represents that the interest on the bonds is tax exempt under § 103 and the bonds will be taken into account under § 146. The Partnership anticipates that all bond proceeds will be used to finance real property rehabilitation costs for the project.

As represented by the Partnership, the project consists of one building that is listed on the National Register of Historic Places. The Partnership has submitted parts 1 and 2 of the Historic Preservation Certification Application to the Department of Interior National Park Service. The Partnership anticipates that the building will qualify as a certified historic structure and that rehabilitation expenditures will be qualified rehabilitation expenditures eligible for the 20 percent credit under § 47.

The Partnership purchased the property from the County Z Improvement Corporation on e for \$f. Closing costs associated with the land were \$g. The Partnership represents that depreciable costs are estimated to be \$h, which includes acquisition closing costs of \$i, land improvements of \$j, personal property of \$k, and furnishings of \$l. The Partnership expects qualified rehabilitation expenditures to be \$m resulting in a credit of \$n under § 47. Depreciable basis after adjustment for the historic tax credit is projected to be \$o. The Partnership anticipates that construction will be complete by p. The Partnership expects to claim historic and low-income tax credits under §§ 47 and 42, respectively, on its q federal income tax return.

The Partnership requests rulings that the basis of the project for purposes of § 42(h)(4)(B) is the project's adjusted basis under § 1011, and not eligible basis under § 42(d), including any increase in eligible basis for buildings located in high cost areas under § 42(d)(5)(C).

Section 38(a) provides as a credit against the tax imposed for the taxable year an amount equal to the sum of the business credit carryforwards carried to the taxable year, the amount of the current year business credit, and the business credit carrybacks carried to the taxable year. Section 38(b)(5) provides that the amount of the current year business credit includes the low-income housing credit determined under § 42(a).

Section 42(a) provides that for purposes of section 38, the amount of the low-income housing credit for any taxable 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)(1)(A) provides that the qualified basis of any qualified low-income building for any taxable year is an amount equal to (i) the applicable fraction (determined as of the close of such taxable year) of (ii) the eligible basis of such building (determined under § 42(d)(5)).

Section 42(d)(1) provides that the eligible basis of a new building is its adjusted basis as of the close of the first taxable year of the credit period. Under § 42(e)(1), 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.

Section 42(d)(5)(C)(i)(II) provides that in the case of any building located in a qualified census tract or difficult development areas that is designated for purposes of § 42(d)(5)(C), the rehabilitation expenditures taken into account under § 42(e) shall be 130 percent of such expenditures determined without regard to § 42(d)(5)(C).

Section 42(d)(5)(C)(ii)(I) provides that the term “qualified census tract” means any census tract that is designated by the Secretary of Housing and Urban Development and, for the most recent year for which census data are available on household income in such tract, in which 50 percent or more of the households have income that is less than 60 percent of the area median gross income for such year. If the Secretary of Housing and Urban Development determines that sufficient data for any period are not available to apply § 42(d)(5)(C)(ii) on the basis of census tracts, such Secretary shall apply § 42(d)(5)(C)(ii) for such period on the basis of enumeration districts.

Section 42(h)(1)(A) provides that the amount of credit determined under § 42 for any taxable year with respect to any building shall not exceed the housing credit dollar amount allocated to such building under § 42(h).

Section 42(h)(4)(A) provides that § 42(h)(1) shall not apply to the portion of any credit allowable under § 42(a) that is attributable to eligible basis financed by any obligation the interest on which is exempt from tax under § 103 if such obligation is taken into account under § 146 and principal payments on such financing are applied within a reasonable period to redeem obligations the proceeds of which were used to provide such financing.

Section 42(h)(4)(B) provides that for purposes of § 42(h)(4)(A), if 50 percent or more of the aggregate basis of any building and the land on which the building is located is financed by an obligation described in § 42(h)(4)(A), § 42(h)(1) shall not apply to any portion of the credit allowable under § 42(a) with respect to such building.

Under § 50(c)(1), if the investment credit under § 46 applies to any property, the basis of the property is reduced by the amount of the credit. Section 46 defines the investment credit as including the rehabilitation credit under § 47. Section 47(a)(2) provides, that for purposes of § 46, the rehabilitation credit for any taxable year is 20 percent of the qualified rehabilitation expenditures with respect to any certified historic structure.

Under § 1011(a), the adjusted basis for determining gain or loss from the sale or other disposition of property is the basis (determined under § 1012) adjusted as provided in § 1016. Section 1012 provides that the basis of property shall be the cost of such property. Section 1016(a)(19) adjusts the basis of property to the extent provided in § 50(c).

The Partnership contends basis should be defined as adjusted basis under § 1011 and not eligible basis under § 42(d). If basis is defined as the building's eligible basis, increasing the project's eligible basis by 30 percent under § 42(d)(5)(C) will result in the Partnership not satisfying the requirement in § 42(h)(4)(B) that the tax-exempt bonds finance 50 percent or more of the project's aggregate basis of any building and land on which the building is located. Defining basis as adjusted basis, which excludes the amount of the rehabilitation credit allowable under § 47 from basis by reason of §§ 1016(a)(19) and 50(c)(1), results in the project satisfying the 50 percent requirement in § 42(h)(4)(B).

Buildings meeting the requirement of § 42(h)(4)(B) do not need an allocation of § 42 credits by a state or local housing agency under § 42(h)(1) provided 50 percent or more of the aggregate basis of any building and the land on which the building is located is financed by tax-exempt bonds. While § 42 contains provisions in which the term basis has been further defined (for example, qualified basis under § 42(d) and eligible basis under § 42(c)), no such qualifying language is provided in § 42(h)(4)(B) to suggest that basis should read as adjusted basis or eligible basis. The plain meaning of the statute may be read as aggregating the building's basis and the land's basis. Thus, basis for purposes of § 42(h)(4)(B) is the cost of the property as defined in § 1012. If we define basis as the building's cost basis under § 1012, the Partnership's project's total costs of \$f, \$g, and \$h will not satisfy the 50 percent requirement in § 42(h)(4)(B).

Accordingly, based upon the above facts and representations, including the Partnership's representation that its project is located in a qualified census tract under § 42(d)(5)(C)(ii), we rule as follows:

The basis of the Partnership's building for purposes of § 42(h)(4)(B) is determined by using the building's cost basis under § 1012 and is determined without regard to any eligible basis adjustment allowed for buildings located in high cost areas under § 42(d)(5)(C).

No opinion is expressed or implied regarding the application of any other provisions of the Code or regulations. Specifically, no opinion is expressed regarding whether Partnership's project qualifies as a low-income housing project under § 42.

This ruling is directed only to the taxpayer who requested 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, a copy of this letter is being sent to the Partnership's authorized legal representative.

Sincerely yours,

/s/ Susan J. Reaman
SUSAN J. REAMAN
Chief, Branch 5
Office of Assistant
Chief Counsel
(Passthroughs and Special
Industries)

Enclosure:
6110 copy