Office of Chief Counsel
Internal Revenue Service

memorandum

CC:PSI:5:JAHolmes
POSTN-109692-15

Third Party Communication: None
Date of Communication: Not Applicable

UIL: 42.07-04

date: March 26, 2015

to: Glenn Deloriea
Program Manager, Technical Issues
(Small Business/Self-Employed)

from: Paul Handleman
Chief, Branch 5
(Passthroughs & Special Industries)

---

subject: Low-Income Housing Credit (LIHC) – Noncompliance Resulting from Conflicting Program Requirements

This Chief Counsel Advice responds to your request on whether a SBSE memorandum dated August 20, 2007, with the same title involving conflicting program requirements, should be withdrawn. This advice may not be used or cited as precedent.

ISSUE

Under § 42 of the Internal Revenue Code, does the practice of not renewing a tenant's lease when a tenant's increase in income conflicts with requirements of a local, state, or other federal program, but does not conflict with § 42 because of §§ 42(g)(2)(D)(i) or (ii), mean that a building's qualified basis is reduced to zero because the building is not a qualified low-income building under § 42(c)(2).

CONCLUSION

No. Not renewing a tenant's lease in this situation does not mean that the building is not a qualified low-income building under § 42(c)(2). However, unless good cause exists to not renew the lease, an owner is required to continue the tenancy of a tenant in a low-income unit who upon initial occupancy satisfied the applicable income limitation elected under § 42(g)(1).

SBSE MEMORANDUM

SBSE issued a memorandum dated August 20, 2007, involving conflicting program requirements. The memorandum provides guidance to revenue agents in situations where an owner of a § 42 building, pursuant to a local, state, or other federal program,

has implemented policies or procedures that result in not renewing a tenant's lease in a § 42 low-income unit when the tenant's income rises to a certain income threshold that violates such other program's requirements. An owner does not renew a tenant's lease despite the fact that the initial occupancy satisfied the income limitation elected for the project under § 42(g)(1), and any later income increase, which exceeds the applicable income limitation during the 15-year compliance period, is not in conflict with § 42 requirements because of the rules in § 42(g)(2)(D). Section 42(g)(2)(D)(i) protects initially qualifying households from being displaced as their income rises, and § 42(g)(2)(D)(ii) applies if a tenant's income increases above 140% of the applicable income limit. The memorandum concludes that the local, state, or other federal program creates a conflict with § 42 that violates § 42(g)(2)(D). Because the owner is giving precedence to a local, state, or other federal program, which is in conflict with § 42(g)(2)(D), the memorandum reasons that the project is not in compliance at all times during the 15-year compliance period and no credit under § 42 is allowable under § 42(c)(2). The memorandum determines it is not necessary to determine exactly how many or which units were affected by the conflicting program. No credit is allowable in the year under audit and the taxpayer is also subject to the credit recapture provisions under § 42(j).

LAW AND ANALYSIS

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

Under § 42(c)(2)(A), the term "qualified low-income building" means any building that is part of a qualified low-income project at all times during the 15-year compliance period.

Under § 42(g)(1), a "qualified low-income housing project" means any project for residential rental property if the project meets the minimum set-aside, as elected by the owner on Form 8609, line 10c.

Under § 42(g)(2)(D)(i), except as provided in § 42(g)(2)(D)(ii), notwithstanding an increase in the income of the occupants of a low-income unit above the income limitation applicable under § 42(g)(1), such unit shall continue to be treated as a low-income unit if the income of such occupants initially met such income limitation and such unit continues to be rent-restricted.

Under § 42(g)(2)(D)(ii), if the income of the occupants of the unit increases above 140 percent of the income limitation applicable under § 42(g)(1), § 42(g)(2)(D)(i) shall cease to apply to any such unit if any residential rental unit in the building (or a size comparable to, or smaller than, such unit) is occupied by a new resident who income exceeds such income limitation.

Under § 42(h)(6)(A), no credit is allowed with respect to any building for the taxable year unless an extended low income housing commitment is in effect as of the end of the taxable year.

Under § 42(h)(6)(B)(i), the "extended low-income housing commitment" agreement between the taxpayer and the housing credit agency must prohibit the eviction or the termination of tenancy (other than for good cause) of an existing tenant of any low-income unit.

Under § 42(h)(6)(J), if, during a taxable year, there is a determination that an extended low-income housing agreement was not in effect as of the beginning of such year, such determination shall not apply to any period before such year and § 42(h)(6)(A) shall be applied without regard to such determination if the failure is corrected within 1 year from the date of the determination.

A building can still be a qualified low-income building under § 42(c)(2)(A) if an owner does not renew the lease of a tenant when the tenant's income exceeds the applicable income limitation elected under § 42(g)(1), even though §§ 42(g)(2)(D)(i) or (ii) would allow the unit to continue to qualify as a low-income unit on renewal. However, unless good cause exists to not renew a lease, an owner is required to continue the tenancy of a tenant in a low-income unit who upon initial occupancy satisfied the applicable income limitation. The fact that §§ 42(g)(2)(D)(i) and (ii) allow a unit to continue to qualify as a low-income unit despite the tenant's increase in income above the applicable income limitation means an increase in income, by itself, is not good cause to end the leasing of the unit to such tenant. Agents do not need to determine whether good cause existed when an owner fails to renew the lease of any tenant. Rather, an appropriate party (e.g., the tenant or housing credit agency) can enforce the extended use agreement to the extent there is a question of whether there was good cause for non-renewal of a lease. There should be a cause of action with respect to the non-renewal of a lease without good cause because of the requirement described in § 42(h)(6)(B)(i). Good cause should be determined under the applicable state or local law, and the fact that a local, state, or other federal program's income requirements conflict with §§ 42(g)(2)(D)(i) or (ii) may be relevant for this determination.

We recommend that the August 20, 2007, memorandum be withdrawn and instead revenue agents should determine that an extended low-income housing commitment satisfying the requirements of § 42(h)(6)(B)(i) is in effect at the end of the taxable year(s) at issue. If there is no commitment in effect, or the commitment does not meet the requirements of § 42(h)(6)(B)(i), then no credit is allowable for such building under § 42(h)(6)(A) for such taxable year(s), subject to the one-year correction period in § 42(h)(6)(J).

Please call James A. Holmes at (202) 317-4137 if you have any further questions about this advice.