

# Low-Income Housing Credit Newsletter

Internal Revenue Service

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The LIHC newsletter provides a forum for networking and sharing information about IRC §42, the Low-Income Housing Credit and communicating technical knowledge and skills, guidance and assistance for developing LIHC issues. We are committed to the development of technical expertise among field personnel. Articles and ideas for future articles are welcome!!

*The contents of this newsletter should not be used or cited as authority for setting or sustaining a technical position.*

## Requesting Information: Preparing Information Document Requests

In the last newsletter, we discussed the forms used by taxpayers owning LIHC projects to claim the credit on their tax returns and how the information on the forms can be reconciled, as well as some of the common errors.

The same information is used by IRS examiners, along with other internal information, to analyze tax returns and prepare for an audit before a taxpayer is contacted. Once the analysis is completed, the examiner will formally notify the taxpayer by mail that an audit is to be conducted. The letter will include a request for information and documents to be made available for the audit. This list of items is provided on a Form 4564, Information Document Request, or in IRS jargon, the "IDR."

Since it's that time of year when lists are made and checked twice, here's what you might expect to see on the first IDR for the audit of a taxpayer owning IRC §42 property, which is almost always a partnership.

### General Information

1. Partnership Agreement.
2. Prospectus/Offering Memorandum related to the organization or syndication of the partnership.
3. Documentation for the partners' capital contributions and current balance.
4. Credit Allocation Application.
5. Market Study.
6. Credit Allocation Award or Carryover Allocation.
7. Extended Use Agreement.
8. All Forms 8609 issued to the taxpayer.
9. Internal audit reports.

### Tax Returns

1. Copies of tax returns for the tax year prior to the earliest year under audit, and all tax returns for years subsequent to the tax years under audit.

2. Trial balance and any workpapers used to prepare the tax return under audit.
3. Depreciation schedules.

### Eligible Basis

1. Final cost certification submitted to the state agency with supporting documentation.
2. Documentation of all financing sources.
3. Development contracts or agreements.
4. Documentation of cost allocations between land, nonqualifying land improvements and depreciable residential rental property included in eligible basis.

### Low-Income Households

1. For the years under audit, rent rolls identifying the households and family size for each low-income unit.
2. Documentation of internal controls in place to ensure that income-qualified households occupy the low-income units.

### 1<sup>st</sup> and 11<sup>th</sup> Year of the Compliance Period

If the first year of the compliance period is audited, the special rule for computing the Applicable Fraction under IRC §42(f)(2) is used. The taxpayer should provide:

1. Certificates of Occupancy,
2. A schedule indicating when each low-income unit was first occupied by an income-qualified household.
3. Computation of First Year Applicable Fraction, including the computation of the Applicable Fraction on a monthly basis.

If the eleventh year of the compliance period is audited and the taxpayer has claimed credit, the taxpayer should provide the information identified above as well as a copy of the tax return for the first year of the credit period.

### Additions to Qualified Basis

1. Provide a list of units first occupied by qualifying tenants after the end of the first year of the credit period and identify when a qualifying household first occupied the unit, or
2. Confirm that all units were occupied by qualifying household by the end of the first year of the credit period.

#### Rents & Other Sources of Income or Funds

1. Description of residential rental units, including total number of units, total number of low-income units, size (bedrooms) and rents charged for low-income and market units.
2. Documentation that rents are correctly restricted.
3. Sources of rent subsidies.
4. Documentation for computation of any utility allowances.
5. Fees for services provided to tenants in addition to housing.
6. Other income from related activities; i.e., vending machines, laundry facilities, etc.
7. Other income from sources such as commercial use of a portion of the property.
8. Documentation of funds received from other sources; e.g., federal grants or subsidies received during the year, additional capital contributions, or loan proceeds.

#### Noncompliance

If the audit resulted from the filing of Forms 8823 by the state agency, the taxpayer should provide documentation for corrective actions taken to restore the project to compliance.

#### Dispositions

If the property was sold, documentation regarding the sale should be requested. Particularly, the sales contract and settlement documents, computation of the capital gain/loss, how the gain/loss was distributed among the partners, and whether the sale required the new owner to operate property as a qualified low-income project for the remainder of the 15-year compliance period.

#### Conclusion: Recordkeeping and Record Retention

Take a deep breath....this is the all-inclusive, master wish list for the *first* IDR. Examiners will tailor the request to fit the facts of the case, but also remember that there may be follow-up IDRs later on.

Can't remember where you stashed this stuff? No excuses! In addition to the general recordkeeping requirements under IRC §6001, owners of IRC §42

projects are subject to specific recordkeeping (it's another long list) and record retention requirements under Treas. Reg. 1.42-5(b). These records must be retained for at least six years after the due date (with extensions) for filing the federal income tax return for that year AND the records for the first year of the credit period must be retained for at least six years beyond the due date (with extensions) for filing the federal income tax return for the last year of the 15-year compliance period of the building.

#### **Administrative Reminders**

It's a holiday...we'll just skip this particular list this time....but just this once!

#### **Subscribing to the LIHC Newsletter**

The LIHC Newsletter is distributed free of charge through e-mail. If you would like to subscribe, just contact Grace at [Grace.F.Robertson@irs.gov](mailto:Grace.F.Robertson@irs.gov).

#### *♪ Grace Notes ♪*

I just want to wish everyone the warmest of holiday seasons and the very best for the coming year, but I'm getting hung up on "wishing" and "warmest," and honestly, is there something any better than best? And do years actual come and go, or do we move through them? Okay, way too much Star Trek here.

My dilemma is rooted in a long ago experience when I was once a member of committee tasked with writing a document describing various IRS procedures. Doesn't sound particularly tough to do, except that many of the procedures we were trying to describe were excruciatingly similar in nature and difficult to differentiate. It didn't take long to realize that adjectives needed to be used cautiously and including "very" this and "really" that just wasn't going to satisfy our need to precision and clarity. To be honest, I can't write "complex" or "complicated" without remembering the agonizing two hour discussion of the subtle differences in their meanings and whether either, or which, of the two we should use. I fear I have no more patience now than I had then, so.....

In this complex and complicated world,  
Whether you celebrate the season in solitude,  
Within a circle of loved ones or with strangers,  
Wherever you are, I hope you will find peace.

Grace

