

# Low-Income Housing Credit Newsletter

*Internal Revenue Service*

*Issue #42, November 2010*

*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.*

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## LIHC Compliance Unit has New Address

The LIHC Compliance Unit has moved from its location in Bensalem, north of Philadelphia, to a new office right in the center of downtown Philadelphia. Their new address is:

Department of the Treasury  
Internal Revenue Service Center  
Philadelphia, PA 19255-0549

- All correspondence should be sent to the new address beginning January 1, 2011.
- It is particularly important that the entire zip code, including the "0549" be included, since "0549" directs mail to the LIHC Compliance Unit.

## Compliance Monitoring by State Agencies

From an IRS perspective, one of the most unusual aspects of IRC §42 is the co-administrative responsibilities shared with the state-level housing agencies. Each agency receives a specific amount of credit each year, based on the state's population. The amount is linked to a cost of living index and is currently \$2.30 per person. The agencies determine which housing projects will be allocated IRC §42 credit, as well as how much credit. The agencies are also responsible for monitoring the projects throughout the 15-year compliance period and reporting noncompliance to the IRS.

### Annual Reports

Under Treas. Reg. §1.42-5(c), taxpayers owning IRC §42 projects are required to annually certify that their projects were in compliance with IRC §42 for the preceding 12-month period. They must report in the form and manner the agency specifies and must certify, under the penalty of perjury, that the information provided is true, accurate, and in compliance with the requirements of IRC §42. Treas. Reg. §1.42-5(c)(1)

lists twelve specific requirements that must be addressed in the certification.

The agencies are required to review the certifications. The taxpayer is considered noncompliant if the certification is inaccurate, incomplete, or the taxpayer discloses non-compliance with any IRC §42 requirement.

### Physical Inspections

Treas. Reg. §1.42-5(c)(2)(ii) requires state agencies to physically inspect a randomly selected sample of low-income rental units by the end of the second calendar year following the year the last building in the project is placed in service and then, on an on-going basis, at least once every three years. The purpose is to confirm that the rental units are suitable for occupancy. See IRC §42(i)(3)(B)(ii).

### Tenant File Reviews

Treas. Reg. §1.42-5(c)(2)(ii) also requires agencies to review the tenant files for the households occupying the low-income units randomly selected for the physical inspection. The purpose is to confirm that the rental units are occupied by income-qualified households.

### And All the Other Stuff...

The agencies must also consider the taxpayer's compliance with other requirements under IRC §42; e.g., rent restrictions, the General Public Use Rule, the Next Available Unit, the Unit Vacancy Rule, utility allowances, and the list (it seems) goes on and on.

### Compliance Monitoring Timeline

1. *Notification of Inspection/Review* – as a practical matter state agencies provide taxpayers with advance notice of an upcoming inspection/review so that the taxpayer can notify tenants and assemble tenant records. The IRS has recommended that if the inspection/review must be postponed, the delay should not exceed 45 days from the originally scheduled date.
2. *Inspection/Reviews* – State agencies conduct inspections/reviews to confirm continuous compliance with IRC §42

or, in other words, to identified currently existing noncompliance.

3. *Notifications of Inspection/Review Results* – Once the inspection/review is completed, the agency must *promptly* provide the taxpayer with a written notice if the IRC §42 project is not in compliance; i.e., (1) the taxpayer did not submit its annual certification, (2) the agency was not allowed to review the tenant files, or (3) the agency discovers by inspection, review, or in some other manner, that the project is not in compliance. See Treas. Reg. §1.42-5(e)(2). Many agencies also provide notice to close the inspection/review when no noncompliance issues are discovered.
4. *Correction Period* - The date of the agency’s notice to the taxpayer starts the correction period during which the taxpayer can resolve any noncompliance issues identified by the agency. The correction period is not defined by regulation, but is not to exceed 90 days. Agencies also have authority under Treas. Reg. 1.42-5(e)(4) to extend the correction period to a total of six months, but only if the agency determines there is good cause for doing so.
5. *Reporting Noncompliance to the IRS* – Regardless of whether the noncompliance is corrected within the designated correction period, agencies must report any observed noncompliance to the IRS within 45 days after the end of the correction period.
  - Form 8823, Low-Income Housing Agencies Report of Noncompliance or Building Disposition, is used to report noncompliance to the IRS.
  - The IRS has provided the agencies with a guide for completing Form 8823 to help them consistently interpret and apply IRC §42 and consistently report noncompliance to the IRS. The guide is also available to the public on industry websites or by contacting Grace Robertson by e-mail at [Grace.F.Robertson@irs.gov](mailto:Grace.F.Robertson@irs.gov).

#### Documenting Agency Reviews

Under Treas. Reg. 1.42(e)(3)(ii), agencies are required to retain records of noncompliance or failure to certify for six years after filing of the associated Forms 8823. In all other cases, the agency must retain the documentation for three years from the end of the calendar year in which the documentation was received.

#### Annual IRC §42(l)(3) Report

Under IRC §42(l)(3), agencies submit an annual report to the IRS specifying the amount of credit allocated during the year, information about the building receiving the allocation and the taxpayer owning the building, and information about the agency’s compliance with IRC §42 requirements.

State agencies satisfy this reporting requirement by filing Form 8610, Annual Low-Income Housing Credit Agencies Report. The report is due February 28<sup>th</sup> of the following year and is signed by the state agency’s official under penalties of perjury.

Part III specifically addresses the agency’s compliance monitoring activities for that year:

1. *Question 11*: Does the state’s qualified allocation plan... including compliance monitoring procedures as required in IRC §42(m)(1)(B)(iii) and Treas. Reg. §1.42-5(a)(2), including monitoring for habitability standards through regular site visits?
2. *Question 12*: Has the housing credit agency... complied with all applicable requirements under the compliance monitoring procedures in its qualified allocation plan?
3. *Question 13*: Has the housing credit agency... complied with the requirements of its monitoring procedures to fulfill its notification of noncompliance under Treas. Reg. §1.42(5)(e)?

Questions 14, 15, and 16 address specific compliance monitoring requirement based on when the low-income buildings were placed in service.

#### Q&A – State Agencies

1. How long does an agency have to issue the notification of the inspection/review results?

The notice should be issued “promptly.” According to my Webster’s dictionary, “promptly” means “readily or immediately. Word’s thesaurus suggests “punctually” or “without delay.” Keep in mind that (1) without the notification, the taxpayer really doesn’t know if the agency found noncompliance issues that need to be corrected, and (2) the correction period doesn’t begin until the notification letter is issued.

2. When is a compliance inspection/review considered completed for reporting purposes on Form 8610?

For reporting purposes, the inspection/review process can be considered completed when the letter providing notice of the results is sent to the taxpayer. If no compliance issues were discovered, the notice closes the inspection/review process. If noncompliance issues are discovered, then the correction period, which may vary in length, begins.

3. What if the taxpayer doesn’t respond to the notification letter?

If a taxpayer fails to communicate with an agency after issuing a notice indicating noncompliance issues, then the agency should file the Form 8823 with the IRS no

later than 45 days after the close of the correct period. There is no requirement or responsibility to continually follow-up if the taxpayer fails to respond.

4. What happens if an agency fails to comply with its own Qualified Allocation Plan and compliance monitoring procedures?

As noted in Chief Counsel Advisory (CCA) 200913013, "If upon review, SBSE [Small Business/Self-Employed, an operational unit within the IRS] determines that an Agency is not meeting its compliance monitoring requirements or that the Agency is not making allocations of credit pursuant to a qualified allocation plan (as defined in IRC §42(m)(1)(B)) that meets the requirements under IRC §42(m)(1)(A), then the Service has the authority to reduce the amount of low-income housing credit allocated by an Agency to a building to zero." In other words, the state agency may lose its authority to allocate credit.

#### Q&A - Taxpayers

1. What happens to a taxpayer subject to compliance monitoring by an agency which doesn't timely complete physical inspections and tenant reviews at least once every three years?

Assuming that the taxpayer filed annual reports with the state agency and certifies its continuous compliance with all IRC §42 requirements, the state agency's failure to timely conduct inspections or reviews will have no immediate affect for the taxpayer. Having said that, keep in mind that:

- The taxpayer has lost the opportunity for an inspection or review *in real time*, which allows for the correction of noncompliance before the end of the taxpayer's tax year when the allowable credit is computed. The taxpayer may be able to avoid disallowance of credit for the current year and the recapture of a portion of the credit claimed in prior years.
- Regardless of the state agency's failure, the taxpayer is subject to audit by the IRS. Conducted after the end of the tax year, IRS audits do not *provide* for correction of noncompliance during the audit so that noncompliance "goes away." The amount of allowable credit will be determined based on the facts and circumstances as they existed at the end of the tax year being audited. The taxpayer may lose credit and be subject to recapture under IRC §42(j).

### **Administrative Reminders**

**Expanding Audits, Project/Tracking Code:** All LIHC cases should include Project Code 0670 and ERCS Tracking Code 9812. If the audit is expanded to include additional years or

related taxpayers, the additional returns should also carry the LIHC project code and tracking code designation.

**Form 5344, Revenue Protection:** The Examination Closing Record, Form 5344, requires entries if you are reducing the amount of credit to be carried forward to a tax year you are not going to audit. Enter the amount of credit carryforward to be disallowed for Item 46. Code "L" should be entered for Item 47. See IRM 4.4.12.4.58 for an example.

**Surveying LIHC Tax Returns:** If you believe it is appropriate to survey an LIHC return, please fax Form 1900 to Grace Robertson, at 202-283-7008, for signature approval.

### **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 ♪**

Yesterday was a particularly busy day in the office and my westward drive home through rush hour traffic particularly tiring. As I rolled along, at a particular moment, I looked up to see a particularly beautiful sunset vista of oranges and pinks and yellow-whites and bands of long clouds splitting sunrays like a prism. These late afternoon sunsets only coincide with my commute in late fall, after turning back the clock. I'd almost forgotten.

Its early morning now and I find myself again working by the window. My big cat Hannah is keeping me company and watching the golden Maple leaves twirl around in the wind outside. Olivia, a petite Siamese, is curled at my feet, one paw touching my foot just to make sure I'm still here. Directly across the street my neighbor's huge oak tree is a flaming red torch in the morning sun, like a prima donna in the spotlight. I've never before been sitting right here at exactly this time of day at this time of year. I'm awake and sitting here at this hour only because, coincidentally, I'm working at home.

Autumn is my favorite time of year.

Hannah, now bored with the floating leaves, has settled beside my computer. She'd probably doze off except she's watching my hands and is curious about the clicking of the computer keys (her ears are twitching). I'm pretty sure she'll try tapping the keys herself any second now, so I've hit the save key. Olivia has stirred from her early morning nap and is complaining, as only a Siamese can, that she's hungry and wants her mid-morning snack, preferably right now. The sky is bright blue and the sun, now shining high in the sky, is streaming through the window. While there's still the chill of Indian summer in the air...I've got to get going...places to be and things to do...right now.

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