DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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August 4, 1999

MEMORANDUM FOR

OP:EX:CS:M

FROM:

CC:DOM:P&SI:5

SUBJECT: Noncompliance question - § 42

This memorandum is in response to your request dated September 30, 1998, for guidance regarding a dispute between the owner of low-income housing tax credit projects (Taxpayer) and the
(Agency) over the adequacy of documentation used by Taxpayer with respect to student tenant eligibility and tenant employment verification. The issues are: (1) whether Agency is within its right to request specific documentation for Taxpayer's projects; and (2) whether Agency can treat Taxpayer's projects as in noncompliance if Agency determines that Taxpayer's documentation is inadequate.

CONCLUSION

In the present case, Agency is within its right to request specific documentation for Taxpayer's projects regarding student tenant eligibility and tenant employment verification. Further, because Agency deems Taxpayer's documentation to be inadequate, Agency can treat Taxpayer's project(s) as in noncompliance with § 42.

FACTS

Agency performed compliance monitoring on three of Taxpayer's low-income housing tax credit projects which resulted primarily in two findings. First, Agency found Taxpayer's "Student Questionnaire Form" not useful for determining theeligibility of student tenants. Further, because of unreliable records, Agency was unable to determine the eligibility of student tenants. Agency has advised Taxpayer to obtain third party statements from the tenants' educational institutions to substantiate the tenants' status as students. Second, Agency found that

Taxpayer's standardized tenant employment verification forms were misleading and unreliable, and, as such, Agency cannot make a determination regarding the tenants' employment. Accordingly, Agency is treating Taxpayer's projects as out of compliance. Agency has asked that Taxpayer use Agency's form.

LAW and ANALYSIS

Section 42 provides a tax credit for investment in qualified low-income buildings placed in service after December 31, 1986. In general, the credit is allowable only if the owner of a qualified low-income building receives a housing credit dollar amount allocation from the housing credit agency in whose jurisdiction the building is located. The housing credit dollar amount that a housing credit agency may allocate in any calendar year is limited to its portion of the state housing credit ceiling for the calendar year.

Section 42(m) outlines the responsibilities of housing credit agencies for administering the low-income housing tax credit program under § 42. Section 42(m)(1)(A) requires that housing credit agencies make allocations of the low-income housing tax credit pursuant to a qualified allocation plan. Section 42(m)(1)(B)(iii) provides that an allocation plan is not qualified unless it contains a procedure that the housing credit agency (or an agent of, or private contractor hired by, the agency) will follow in monitoring compliance with the provisions of § 42. The housing credit agency is to notify the IRS of any noncompliance of which such agency becomes aware.

Section 42(m)(1)(B)(iii) is effective on January 1, 1992, and applies to all buildings for which the low-income housing credit determined under § 42 is, or has been, allowable at any time. Section 42(m)(1)(B)(iii) and §1.42-5 do not require monitoring for whether a low-income housing project is in compliance with the requirements of § 42 prior to January 1, 1992. However, if a housing credit agency becomes aware of noncompliance that occurred prior to January 1, 1992, such agency is required to notify the IRS of that noncompliance.

Section 1.42-5 requires a housing credit agency, at a minimum, to do the following: (1) review tenant income certifications and rent charges of projects; (2) require the owner of a project to certify annually that the preceding 12-month period each building in the project was suitable for occupancy, taking into account local health, safety, and building codes; and (3) report a correction of noncompliance or failure to certify if the correction occurs within the correction period defined in § 1.42-5(e)(4). Section 1.42-5(a)(2)(ii) provides that the monitoring procedure may contain additional provisions or requirements.

We believe that because the compliance monitoring regulations under §1.42-5 establish minimum standards, housing credit agencies have the right to control the documentation required within their respective jurisdictions in order to

fulfill their compliance monitoring responsibilities. See, e.g., § 1.42-5(c)(2)(ii)(C). If a housing credit agency determines that documentation provided by an owner of a property receiving the low-income housing tax credit is inadequate, then it is reasonable for such agency to request from the owner either new or additional documentation that such agency deems to be adequate. To the extent that inadequate documentation prevents a housing credit agency from determining whether a project is in compliance with § 42, we believe that such agency can properly hold the project out of compliance.

If you have any questions, please contact at .