Internal Revenue Service

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Person To Contact:

,

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Refer Reply To:
CC:PSI:5
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Date:
December 22, 2005

LEGEND

Taxpayer =

Project =

Seller =

Limited Partner =

General Partner A =

General Partner B =

General Partner C =

Corporation A =

Individual A =

Estate =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

Date 10 =

Year 1 =

Year 2 =

Year 3 =

a =

b =

c =

d =

e =

f =

g =

h =

i =

Dear :

This letter responds to a letter dated August 18, 2005, and subsequent correspondence dated October 19, 2005, November 8, 2005, and December 21, 2005, submitted on behalf of Taxpayer concerning whether for purposes of § 42(d)(2)(B)(ii) of the Internal Revenue Code, there is a period of 10 years between the date on which Taxpayer acquired Project and the date Project was last placed in service.

Taxpayer represents that the facts are as follows:

FACTS

Taxpayer, which is engaged in the operation and leasing of multifamily apartment housing, is a calendar year taxpayer using the cash method of accounting.

On Date 1, Seller was formed by and among Limited Partner as the sole limited partner and General Partner A and General Partner B as the sole general partners for the purpose of owning and operating Project. Project consists of a units contained in b buildings.

For taxable years Year 1 through Year 2, Limited Partner was the sole limited partner of Seller, with a c percent interest in partnership capital and profits. General Partner A owned a d percent general partner interest and General Partner B owned an e percent general partner interest. During taxable year Year 3, General Partner A and General Partner B conveyed their cumulative f percent general partner interest in Seller to General Partner C.

Limited Partner had a promissory note payable to Corporation A, who was unrelated to Limited Partner for federal income tax purposes. On Date 2, the promissory note matured and Limited Partner defaulted on its payment obligation under the note. The promissory note was secured by a pledge of Limited Partner's c percent limited partner interest in Seller. Corporation A foreclosed on the Note and, in full satisfaction thereof, took possession of Limited Partner's limited partnership interest in Seller effective Date 3. Immediately thereafter on Date 3, Corporation A sold and assigned the c percent limited partner interest to Individual A pursuant to a sale and assignment agreement dated Date 3 under which Individual A purchased the c percent limited partner interest in Seller and various interests in g other partnerships otherwise unrelated to Seller for a total aggregate purchase price of $h. At the time Individual A acquired the c percent limited partner interest in Seller, Individual A was a shareholder in Corporation A, owning less than a i percent interest in Corporation A's then outstanding stock.

On its Form 1065, "U.S. Partnership Return of Income," for the taxable year ended Date 4, Seller made an election under § 754 and § 1.754-1 of the Income Tax Regulations to adjust the basis of Seller's property pursuant to §§ 734(b) and 743(b).

On Date 5, Corporation A filed with the United States Bankruptcy Court for the District of State a voluntary petition for protection under Chapter 11 of Title 11 of the United States Code. During the course of the bankruptcy case, Corporation A entered into settlement agreements with various claim holders, including Individual A. On or about Date 6, Individual A died and his c percent limited partnership interest in Seller was transferred to Estate.

Following Individual A's death, Corporation A continued its negotiations with Estate. On Date 7, Corporation A and Estate reached a settlement agreement that was approved by the United State Bankruptcy Court on Date 8. Under the settlement agreement, Estate agreed, among other things, to transfer the c percent limited partner interest in Seller. The actual transfer was consummated as of Date 9, when Estate transferred the c percent limited partner interest in Seller to a wholly-owned second tier limited liability company of Corporation A that is disregarded as an entity separate from its owner pursuant to § 301.7701-3. Thus, as of Date 9, Corporation A was, for federal income tax purposes, the sole limited partner of Seller.

On Date 10, Taxpayer purchased Project from Seller. Taxpayer intends to rehabilitate Project and qualify for both acquisition and rehabilitation low-income housing credits under § 42.

Taxpayer makes the following additional representations:

1) Taxpayer acquired Project by a purchase as defined in § 179(d)(2).

2) To Taxpayer's knowledge there were at least 10 years between the date Project was acquired by Taxpayer and the date of the most recent nonqualified substantial improvement to any of Project's buildings within the meaning of § 42(d)(2)(D)(i).

3) None of Project's buildings were previously placed in service by Taxpayer or any person who was a related person within the meaning of § 42(d)(2)(D)(iii)(II) with respect to Taxpayer as of the time the buildings were previously placed in service.

4) To the knowledge of Taxpayer there were no transfers of ownership of Project within the ten-year period ending on Date 9 except for those described above.

RULING REQUESTED

Taxpayer requests the Service to rule that, for purposes of § 42(d)(2)(B)(ii), there is a period of at least 10 years between the date Project was acquired by Taxpayer and the date Project was last placed in service.

LAW AND ANALYSIS

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

Section 42(b) provides, in part, that the term "applicable percentage" means the appropriate percentage prescribed by the Secretary for the month applicable under § 42(b)(2)(A)(i) or (ii). Section 42(b)(2)(B) provides that the percentages prescribed by the Secretary for any month shall be the percentages that will yield over a 10-year period amounts of credit that have a present value equal to: (i) 70 percent of the qualified basis of new buildings that are not federally subsidized for the taxable year, and (ii) 30 percent of the qualified basis of new buildings that are federally subsidized for the taxable year and existing buildings.

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 the (i) applicable fraction (determined as of the close of the taxable year) of (ii) the eligible basis of the building (determined under § 42(d)(5)).

Section 42(d)(2)(A) provides that the eligible basis of an existing building is (i) in the case of a building that meets the requirements of § 42(d)(2)(B), its adjusted basis as of the close of the first year of the credit period, and (ii) zero in any other case. Section 42(d)(2)(B) provides that a building meets the requirements of § 42(d)(2)(B) if (i) the building is acquired by purchase (as defined in § 179(d)(2)), (ii) there is a period of at least 10 years between the date of its acquisition by the taxpayer and the later of (I) the date the building was last placed in service, or (II) the date of the most recent

nonqualified substantial improvement of the building, (iii) the building was not previously placed in service by the taxpayer or by any person who was a related person with respect to the taxpayer as of the time previously placed in service, and (iv) except as provided in § 42(f)(5), a credit is allowable under § 42(a) by reason of § 42(e) with respect to the building.

Section 42(d)(2)(D)(ii)(I) provides that, for purposes of determining when a building was last placed in service under § 42(d)(2)(B)(ii), there shall not be taken into account any placement in service in connection with the acquisition of the building in a transaction in which the basis of the building in the hands of the person acquiring it is determined in whole or in part by reference to the adjusted basis of such building in the hands of the person from whom acquired.

Section 708(a) provides that a partnership shall be considered as continuing if it is not terminated. Section 708(b)(1)(B) provides that, for purposes of § 708(a), a partnership shall be considered terminated if within a 12-month period there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits.

Section 1.708-1(b)(1)(i) provides that upon the death of one partner in a 2-member partnership, the partnership shall not be considered as terminated if the estate or other successor in interest of the deceased partner continues to share in the profits or losses of the partnership business.

Section 1.708-1(b)(4) provides that if a partnership is terminated by a sale or exchange of an interest, the following is deemed to occur: The partnership contributes all of its assets and liabilities to a new partnership in exchange for an interest in the new partnership; and, immediately thereafter, the terminated partnership distributes interests in the new partnership to the purchasing partner and the other remaining partners in proportion to their respective interests in the terminated partnership in liquidation of the terminated partnership, either for the continuation of the business by the new partnership or for its dissolution and winding up. Section 1.708-1(b)(4) applies to terminations of partnerships under § 708(b)(1)(B) occurring on or after May 9, 1997; however, § 1.708-1(b)(4) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply § 1.708-1(b)(4) to the termination in a consistent manner.

Section 1.708-1(b)(5) provides that if a partnership is terminated by a sale or exchange of an interest in the partnership, a § 754 election (including a § 754 election made by the terminated partnership on its final return) that is in effect for the taxable year of the terminated partnership in which the sale occurs, applies with respect to the incoming partner. Therefore, the bases of partnership assets are adjusted pursuant to §§ 743 and 755 prior to their deemed contribution to the new partnership.

Section 721(a) provides that no gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in

exchange for an interest in the partnership. Section 721(b) provides that § 721(a) will not apply to gain realized on the transfer of property to a partnership if such gain, when recognized, will be includible in the gross income of a person other than a United States person.

Section 723 provides that the basis of property contributed to a partnership by a partner shall be the adjusted basis of such property to the contributing partner at the time of the contribution increased by the amount (if any) of gain recognized under § 721(b) to the contributing partner at such time.

Section 754 provides that if a partnership files an election in accordance with regulations prescribed by the Secretary, the basis of partnership property is adjusted, in the case of a distribution of property, in the manner provided in § 734, and, in the case of a transfer of partnership interest, in the manner provided in § 743. Such an election shall apply with respect to all distributions of property by the partnership and to all transfers of interest in the partnership during the taxable year with respect to which the election was filed and all subsequent taxable years.

Section 743(b) provides that, in the case of a transfer of an interest in a partnership by sale or exchange or upon the death of a partner, a partnership with respect to which an election under § 754 is in effect shall (1) increase the adjusted basis of the partnership property by the excess of the basis to the transferee partner of the transferee partner's interest in the partnership over the transferee partner's proportionate share of the adjusted basis of the partnership property, or (2) decrease the adjusted basis of the partnership property by the excess of the transferee partner's proportionate share of the adjusted basis of the partnership property over the basis of the transferee partner's interest in the partnership.

Under the preceding described facts, there are four specified transfers of c percent limited partnership interests that Taxpayer seeks to assure will not be taken into account for purposes of determining under § 42(d)(2)(B)(ii) when Project was last placed into service. The four specified transfers include; (1) the Date 3 transfer from Limited Partner to Corporation A, (2) the Date 3 transfer from Corporation A to Individual A, (3) the transfer by Individual A to Estate following the death of Individual A, and (4) the Date 9 transfer from Estate to Corporation A pursuant to the settlement agreement approved by the United States Bankruptcy Court.

On Date 3, Corporation A acquired Limited Partner's c percent limited partnership interest in Seller by means of foreclosure. This resulted in a technical termination of Seller under § 708(b)(1)(B). As a result, and pursuant to § 1.708-1(b)(4), Seller was deemed to have contributed Project to a new partnership (new partnership 1) in exchange for an interest in new partnership 1, and, immediately thereafter, distributed its interest in new partnership 1 to General Partner C and Corporation A in proportion to their respective interests in Seller in liquidation of Seller for the continuation of Project's operation by new partnership 1. In addition, pursuant to § 1.708-1(b)(5), because an

election was in effect under § 754 with respect to the Date 3 transfer from Limited Partner to Corporation A of Limited Partner's c percent limited partnership interest in Seller, the adjusted basis of Project was adjusted under § 743 while still in the hands of Limited Partner and prior to the deemed contribution by Seller of Project to new partnership 1. As a result of Seller's deemed contribution of Project to new partnership 1, under § 723, the adjusted basis of Project in the hands of new partnership 1 was the same (carryover basis) as the adjusted basis of Project in the hands of Seller. This satisfies the exception of § 42(d)(2)(D)(ii)(I) with the result that the transfer of Limited Partner's c percent limited partnership interest in Seller to Corporation A is not taken into account for purposes of determining under § 42(d)(2)(B)(ii) when Project was last placed in service.

Immediately following the above transfer that resulted in the § 708(b)(1)(B) termination of Seller, and also on Date 3, Corporation A sold and assigned its c percent limited partnership interest in new partnership 1 to Individual A. This resulted in a technical termination of new partnership 1 under § 708(b)(1)(B). As a result, and pursuant to § 1.708-1(b)(4), new partnership 1 was deemed to have contributed Project to a new partnership (new partnership 2) in exchange for an interest in new partnership 2, and, immediately thereafter, distributed its interest in new partnership 2 to General Partner C and Individual A in proportion to their respective interests in new partnership 1 in liquidation of new partnership 1 for the continuation of Project's operation by new partnership 2. In addition, pursuant to § 1.708-1(b)(5), because an election was in effect under § 754 with respect to the Date 3 transfer from Corporation A to Individual A of the c percent limited partnership interest in new partnership 1, the adjusted basis of Project was adjusted, under § 743, while still in the hands of new partnership 1 and prior to the deemed contribution by new partnership 1 of Project to new partnership 2. As a result of new partnership 1's contribution of Project to new partnership 2, under § 723, the adjusted basis of Project in the hands of new partnership 2 was the same (carryover basis) as the adjusted basis of Project in the hands of new partnership 1. This satisfies the exception of § 42(d)(2)(D)(ii)(I) with the result that the sale by Corporation A to Individual A of its c percent limited partnership interest in new partnership 1 is not taken into account for purposes of determining under § 42(d)(2)(B)(ii) when Project was last placed in service.

On or about Date 6, Individual A died. Individual A's c percent limited partnership interest in new partnership 2 was transferred to Estate. Under § 1.708-1(b)(1)(i), new partnership 2 is not considered as terminated as a result of the transfer from Individual A to Estate of his c percent limited partnership interest in new partnership 2. Also, the transfer of Individual A to Estate of his c percent limited partnership interest in new partnership 2 is not a sale or exchange for purposes of § 1.708-1(b)(2). Accordingly, the transfer of the c percent limited partnership interest is not taken into account for purposes of determining under § 42(d)(2)(B)(ii) when Project was last placed in service.

On Date 9, pursuant to a settlement agreement approved by the United States Bankruptcy Court, Estate transferred its c percent limited partnership interest in new

partnership 2 to a wholly-owned second tier limited liability company of Corporation A that Taxpayer represents is disregarded as an entity separate from its owner pursuant to § 301.7701-3. Thus, as of Date 9, Corporation A became, for federal income tax purposes, the sole limited partner of new partnership 2. This resulted in a technical termination of new partnership 2 under § 708(b)(1)(B). As a result, and pursuant to § 1.708-1(b)(4), new partnership 2 was deemed to have contributed Project to a new partnership (new partnership 3) in exchange for an interest in new partnership 3, and, immediately thereafter, distributed its interest in new partnership 3 to General Partner C and Corporation A in proportion to their respective interests in new partnership 2 in liquidation of new partnership 2 for the continuation of Project's operation by new partnership 3. As a result, under § 723, the adjusted basis of Project in the hands of new partnership 3 was the same (carryover basis) as the adjusted basis of Project in the hands of new partnership 2. This satisfies the exception of § 42(d)(2)(D)(ii)(I) with the result that the transfer by Estate to Corporation A of its c percent limited partnership interest in new partnership 2 is not taken into account for purposes of determining under § 42(d)(2)(B)(ii) when Project was last placed in service.

Based solely upon the above facts and Taxpayer's representations we rule that, as regards the four specified transfers described above, for purposes of § 42(d)(2)(B)(ii), there is a period of at least 10 years between the date that Project acquired by Taxpayer and the date Project was last placed in service.

No opinion is expressed or implied regarding the application of any other provision in the Code or regulations. Specifically, no opinion is expressed or implied regarding whether Taxpayer's costs of acquisition and rehabilitation of Project will otherwise qualify for the low-income housing credit under § 42.

In accordance with the power of attorney filed with this request, we are sending a copy of this letter to Taxpayer's authorized representative. This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. A copy of this letter should be filed with the federal income tax return for Taxpayer and its partners for the first taxable year in which the low-income housing credit for Project is claimed.

Sincerely,

/s/ Paul F. Handleman
Paul F. Handleman
Senior Technician Reviewer
Branch 5
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure: 6110 copy

cc: