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[Code Sec. 42]

Low-income housing credit.

This letter is in response to your letter dated May 27, 1994, and subsequent correspondence, submitted on behalf of Taxpayer, in which you request a letter ruling regarding the low-income housing credit under § 42 of the Internal Revenue Code. Specifically, Taxpayer requests a ruling that the space rented pursuant to each lease of an SRO unit will be treated as a separate "low-income unit" within the meaning of § 42(i)(3). The represented facts are set forth below.

Taxpayer is a State M limited partnership. Taxpayer is the contract vendee under an agreement to purchase a low-income housing project currently under construction and located at Address in City (the Project). The Project received a 1994 low-income housing credit carry-over allocation under § 42(h)(1)(E)/(F) from the Authority, and is expected to generate low-income housing tax credits (Credits) under § 42.

The Taxpayer was formed for the purposes of acquiring, owning, and operating the Project as a low-income housing project in compliance with § 42, applicable Authority requirements, and other legal restrictions imposed on the Project. The Taxpayer intends to lease and operate the Project in a manner that causes 100% of the units in the Project to be occupied by low-income tenants, thus qualifying all of the units in the Project for credits.

The Project, as initially designed and as partially constructed, currently consists of a partially complete a-unit residential condominium project, with the ground floor condominium space zoned for retail use. In order to better accommodate the special populations that will occupy the Project, the construction of the Project will be completed in a manner that reconfigures the a-apartment unit condominium project and converts it into a b-unit residential building with one-bedroom apartment, single room occupancy (SRO) units. Some of the low-income tenants who will occupy the Project are expected to be single persons with AIDS, and some will be elderly. The

initial lease term in the Project will be for a period of not less than 6 months.

The conversion will be accomplished by creating SRO units within a portion of the Project that is currently partially constructed as two- and three-bedroom apartment units. The creation of SRO units will be accomplished by adding walls, doors and other appropriate fixtures. Each SRO unit will be occupied exclusively by one individual who will not be related to the occupant(s) of other SRO units, thereby affording that individual sole and exclusive possession of the SRO unit. SRO unit doors will have individual locks. The unrelated occupants of each group of SRO units will share kitchen and possibly a small living area. In some cases, bathrooms will be shared, and in some cases each SRO unit will have its own bathroom, to be used exclusively by the occupant. Each occupant of a SRO unit will enter into a separate lease agreement for exclusive possession of the SRO unit and enclosed bathroom, if applicable, and non-exclusive, shared rights to the shared living facilities, consisting of a kitchen, a small living/dining area, and possibly a bathroom. Units that are not SRO units will be either studio apartments or one-bedroom apartments, which will contain sanitary and food preparation facilities.

This arrangement of SRO units has been determined by the Authority to meet its definition of an Arrangement for SRO units.

The Project currently complies with local zoning regulations as a permanent residence. In connection with the conversion of the Project into a b-unit residence as described above, the zoning classification of the Project will be changed to a community facility. This is the classification in the Resolution for an Arrangement. Notwithstanding this classification, the Project will constitute residential rental property, as defined in § 168(e)(2)(A)(i).

The proposed reconfiguration of the Project is necessary to accommodate the needs of the elderly and persons with AIDS. Because the Project will constitute permanent housing and each tenant's privacy is important, it is necessary to create SRO units physically separate from the remainder of the units with access restricted by lockable doors. Although kitchen and some bathroom facilities will be shared, they will be shared only by one or two other SRO tenants. This arrangement maximizes privacy, while insuring that the benefits of communal housing (companionship and cooperative activities) which are important to these special populations, can be attained.

Elderly and AIDS tenants with incomes well below the 60% area median gross income maximum will be able to afford the rent that will be charged for each SRO unit treated as a "low-income unit." The revenue generated by b low-income units will be necessary to support the expenses of the Project.

The Project will meet HUD Section 8 housing quality standards. The Project will not be financed with any tax-exempt bond funds or HOME Investment Partnership Act funds. Rent charged for all units in the building will not exceed the amount permitted under § 42(g)(2)(C)(i) for a unit occupied by 1 person.

Section 38(a) provides for a general business credit against tax that includes the amount of the current year business credit. Section 38(b)(5) provides that the amount of the current year business credit includes the low-income housing credit determined under § 42(a).

Section 42(a) provides that, for purposes of § 38, the amount of the low-income housing credit determined under § 42 for any tax year in the credit period shall be an amount equal to the applicable percentage of the qualified basis of each qualified low-income building.

Section 42(c)(2) defines the term "qualified low-income building" as any building: (A) which is part of a qualified low-income housing project at all times during the period (i) beginning on the first day in the compliance period on which such building is part of such a project, and (ii) ending on the last day of the compliance period with respect to such building, and (B) to which the amendments made by § 201(a) of the Tax Reform Act of 1986 apply.

Section 42(g)(1) defines the term "qualified low-income housing project" as any project for residential rental property if the project meets the requirements of subparagraphs (A) or (B), whichever the taxpayer elects. The election is irrevocable. The project meets the requirements of § 42(g)(1)(A) if 20 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 50 percent or less of area median gross income. The project meets the requirements of § 42(g)(1)(B) if 40 percent or more of the residential units in the project are both rent-restricted and occupied by individuals whose income is 60 percent or less of area median gross income.

Section 42(g)(2)(A) provides that, for purposes of § 42(g)(1), a unit is rent-restricted if the gross rent (defined in § 42(g)(2)(B)) that is paid for the unit does not exceed 30 percent of the

imputed income limitation applicable to the unit. Section 42(g)(2)(C) defines the imputed income limitation applicable to the unit as the income limitation that would apply to the unit under § 42(g)(1) to individuals occupying the unit if the number of individuals occupying the unit were (1) in the case of a unit that does not have a separate bedroom, 1 individual, and (2) in the case of a unit that has 1 or more separate bedrooms, 1.5 individuals for each separate bedroom.

Section 42(i)(3) defines a low-income unit as any unit in a building that is (1) rent-restricted under § 42(g)(2), and (2) occupied by individuals that meet the income limitation applicable under § 42(g)(1) to the project of which the building is a part.

The ruling requested by Taxpayer concerns whether these reconverted SRO units qualify as low-income units under § 42(i)(3). Assuming that these units are, in fact, SRO units, these units qualify as low-income units because they meet the requirements of § 42(i)(3).

The Project SRO units will be rent-restricted. The imputed income limitation applicable to any SRO unit is the income limitation that would apply under § 42(g)(1) to individuals occupying the unit if the number of individuals occupying the unit is 1. Projects SRO units will be occupied exclusively by one individual and the rent charged to each SRO unit occupant will not exceed the amount permitted under § 42(g)(2)(C)(i).

All of the units in the Project will be occupied by individuals whose income do not exceed 60 percent of area median gross income. Thus, Project SRO units meet the income limitation applicable under § 42(g)(1).

The initial lease term in the Project will be for a period of not less than 6 months. Thus, the units will be used on other than a transient basis.

Finally, the Project will meet HUD Section 8 housing quality standards. In the absence of regulations under § 42(i)(3)(B)(ii), these standards satisfy the suitability for occupancy requirements of § 42(i)(3)(B)(i).

Therefore, based upon the above facts and representations, we conclude that, the space rented pursuant to each lease of a SRO unit is a separate "low-income unit" within the meaning of § 42(i)(3).

No opinion is expressed or implied regarding the application of any other provisions of the Code or regulations. This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3)

provides that it may not be used or cited as precedent.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent. Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling may be modified or revoked if the adopted temporary or final regulations are inconsistent with any conclusion of this ruling. See § 11.04 of Rev. Proc. 94-1, 1994-1 I.R.B. 10, 39. However, when the criteria in § 11.05 of Rev. Proc. 94-1 are satisfied, a ruling is not revoked or modified retroactively, except in rare or unusual circumstances.

A copy of this letter should be attached to the appropriate federal income tax return for the taxable year in which the transaction covered by this ruling is consummated. In accordance with the power of attorney on file, this letter is being sent to you as the authorized representative of Taxpayer.

Sincerely yours, James Ranson, Chief,
Branch 5, Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)