

Notice 88-80
1988-30 I.R.S. 28

NOTICE 88-80

**LOW-INCOME HOUSING TAX CREDIT- DETERMINATION OF INCOME FOR
PURPOSES OF SECTION 42(g)(1)**

July 25, 1988

The purpose of this Notice is to inform taxpayers that regulations to be issued under section 42(g)(1) of the Internal Revenue Code of 1986 (the 'Code') (relating to the determination of a qualified low-income housing project) will provide that the income of individuals and area median gross income (adjusted for family size) are to be made in a manner consistent with the determination of annual income and the estimates for median family income under section 8 of the United States Housing Act of 1937 (H.U.D. section 8).

For purposes of H.U.D. section 8, annual income is defined under 24 CFR 813.106 (1987). HUD section 8 median family income estimates (i.e., area median gross income estimates) are based on decennial Census data updated with bureau of the Census P-60 income data and Department of Commerce County Business Patterns employment and earnings data. The determination of annual income and median family income estimates are based on definitions of income that include some items of income that are not included in a taxpayer's gross income for purposes of computing Federal Income Tax liability. Thus, the income of individuals and area median gross income (adjusted for family size) for purposes of section 42(g)(1) of the Code will NOT be made by reference to items of income used in determining gross income for purposes of computing Federal Income Tax liability.

This document serves as an 'administrative pronouncement' as that term is described in section 1.661-3(b)(2) of the Income Tax Regulations and may be relied upon to the same extent as a revenue ruling or revenue procedure.

The principal author of this Notice is Christopher J. Wilson of the Legislation and Regulations Division. For further information regarding this Notice contact Mr. Wilson on (202) 566-4336 (not a toll-free call).

Exhibit G IRS Regulations § 1.142-6 Carryover and 1.42-10 Utility Allowance**§1.42-6 Buildings qualifying for carryover allocations.**

(a) *Carryover allocations*—(1) *In general.* A carryover allocation is an allocation that meets the requirements of section 42(h)(1)(E) or (F). If the requirements of section 42(h)(1)(E) or (F) that are required to be satisfied by the close of a calendar year are not satisfied, the allocation is not valid and is treated as if it had not been made for that calendar year. For example, if a carryover allocation fails to satisfy a requirement in §1.42-6(d) for making an allocation, such as failing to be signed or dated by an authorized official of an allocating agency by the close of a calendar year, the allocation is not valid and is treated as if it had not been made for that calendar year.

(2) *10 percent basis requirement.* A carryover allocation may only be made with respect to a qualified building. A qualified building is any building which is part of a project if, by the date specified under paragraph (a)(2)(i) or (ii) of this section, a taxpayer's basis in the project is more than 10 percent of the taxpayer's reasonably expected basis in the project as of the close of the second calendar year following the calendar year the allocation is made. For purposes of meeting the 10 percent basis requirement, the determination of whether a building is part of a single-building project or multi-building project is based on whether the carryover allocation is made under section 42(h)(1)(E) (building-based allocation) or section 42(h)(1)(F) (project-based allocation). In the case of a multi-building project that receives an allocation under section 42(h)(1)(F), the 10 percent basis requirement is satisfied by reference to the entire project.

(i) *Allocation made before July 1.* If a carryover allocation is made before July 1 of a calendar year, a taxpayer must meet the 10 percent basis requirement by the close of that calendar year. If a taxpayer does not meet the 10 percent basis requirement by the close of the calendar year, the carryover allocation is not valid and is treated as if it had not been made.

(ii) *Allocation made after June 30.* If a carryover allocation is made after June 30 of a calendar year, a taxpayer must meet the 10 percent basis requirement by the close of the date that is 6 months after the date the allocation was made. If a taxpayer does not meet the 10 percent basis requirement by the close of the required date, the carryover allocation must be returned to the Agency. Unlike a carryover allocation made before July 1, if a taxpayer does not meet the 10 percent basis requirement by the close of the required date, the carryover allocation is treated as a valid allocation for the calendar year of allocation, but is included in the "returned credit component" for purposes of determining the State housing credit ceiling under section 42(h)(3)(C) for the calendar year following the calendar year of the allocation. See §1.42-14(d)(1).

(b) *Carryover-allocation basis*—(1) *In general.* Subject to the limitations of paragraph (b)(2) of this section, a taxpayer's basis in a project for purposes of section 42(h)(1)(E)(ii) or (F) (carryover-allocation basis) is the taxpayer's adjusted basis in land or depreciable property that is reasonably expected to be part of the project, whether or not these amounts are includible in eligible basis under section 42(d). Thus, for example, if the project is to include property that is not residential rental property, such as commercial space, the basis attributable to the commercial space, although not includible in eligible basis, is includible in carryover-allocation basis. The adjusted basis of land and depreciable property is determined under sections 1012 and 1016, and generally includes the direct and indirect costs of acquiring, constructing, and rehabilitating the property. Costs otherwise includible in carryover-allocation basis are not excluded by reason of having been incurred prior to the calendar year in which the carryover allocation is made.

(2) *Limitations*—For purposes of determining carryover-allocation basis under paragraph (b)(1) of this section, the following limitations apply.

(i) *Taxpayer must have basis in land or depreciable property related to the project.* A taxpayer has carryover-allocation basis to the extent that it has basis in land or depreciable property and the land or depreciable property is reasonably expected to be part of the project for which the carryover allocation is made. This basis includes all items that are properly capitalizable with respect to the land or depreciable property. For example, a nonrefundable downpayment for, or an amount paid to acquire an option to purchase, land or depreciable property may be included in carryover-allocation basis if properly capitalizable into the basis of land or depreciable property that is reasonably expected to be

part of a project.

(ii) *High cost areas.* Any increase in eligible basis that may result under section 42(d)(5)(C) from a building's location in a qualified census tract or difficult development area is not taken into account in determining carryover-allocation basis or reasonably expected basis.

(iii) *Amounts not treated as paid or incurred.* An amount is not includible in carryover-allocation basis unless it is treated as paid or incurred under the method of accounting used by the taxpayer. For example, a cash method taxpayer cannot include construction costs in carryover-allocation basis unless the costs have been paid, and an accrual method taxpayer cannot include construction costs in carryover-allocation basis unless they have been properly accrued. See paragraph (b)(2)(iv) of this section for a special rule for fees.

(iv) *Fees.* A fee is includible in carryover-allocation basis only to the extent the requirements of paragraph (b)(2)(iii) of this section are met and—

(A) The fee is reasonable;

(B) The taxpayer is legally obligated to pay the fee;

(C) The fee is capitalizable as part of the taxpayer's basis in land or depreciable property that is reasonably expected to be part of the project;

(D) The fee is not paid (or to be paid) by the taxpayer to itself; and

(E) If the fee is paid (or to be paid) by the taxpayer to a related person, and the taxpayer uses the cash method of accounting, the taxpayer could properly accrue the fee under the accrual method of accounting (considering, for example, the rules of section 461(h)). A person is a related person if the person bears a relationship to the taxpayer specified in sections 267(b) or 707(b)(1), or if the person and the taxpayer are engaged in trades or businesses under common control (within the meaning of subsections (a) and (b) of section 52).

(3) *Reasonably expected basis.* Rules similar to the rules of paragraphs (a) and (b) of this section apply in determining the taxpayer's reasonably expected basis in a project (land and depreciable basis) as of the close of the second calendar year following the calendar year of the allocation.

(4) *Examples.* The following examples illustrate the rules of paragraphs (a) and (b) of this section.

Example 1. (i) *Facts.* C, an accrual-method taxpayer, receives a carryover allocation from Agency, the state housing credit agency, in May of 2003. As of that date, C has not begun construction of the low-income housing building C plans to build. However, C has owned the land on which C plans to build the building since 1985. C's basis in the land is \$100,000. C reasonably expects that by the end of 2005, C's basis in the project of which the building is to be a part will be \$2,000,000. C also expects that because the project is located in a qualified census tract, C will be able to increase its basis in the project to \$2,600,000. Before the close of 2003, C incurs \$150,000 of costs for architects' fees and site preparation. C properly accrues these costs under its method of accounting and capitalizes the costs.

(ii) *Determination of carryover-allocation basis.* C's \$100,000 basis in the land is includible in carryover-allocation basis even though C has owned the land since 1985. The \$150,000 of costs C has incurred for architects' fees and site preparation are also includible in carryover-allocation basis. The expected increase in basis due to the project's location in a qualified census tract is not taken into account in determining C's carryover-allocation basis. Accordingly, C's carryover-allocation basis in the project of which the building is a part is \$250,000.

(iii) *Determination of whether building is qualified.* C's reasonably expected basis in the project at the close of the second calendar year following the calendar year of allocation is \$2,000,000. The expected increase in eligible basis due to the project's location in a qualified census tract is not taken into account in determining this amount. Because C's carryover-allocation basis is more than 10 percent of C's reasonably expected basis in the project of which the building is a part, the building for which C received the carryover allocation is a qualified building for purposes of section 42(h)(1)(E)(ii) and paragraph (a) of this section.

Example 2. (i) *Facts.* D, an accrual-method taxpayer, received a carryover allocation from Agency, the state

housing credit agency of State X, on September 12, 2003. As of that date, D has not begun construction of the low-income housing building D plans to build and D does not have basis in the land on which D plans to build the building. From September 12, 2003, to the close of March 12, 2004, D incurs some costs related to the planned building, including architects' fees. As of the close of March 12, 2004, these costs do not exceed 10 percent of D's reasonably expected basis in the single-building project as of the close of 2005.

(ii) *Determination of whether building is qualified.* Because D's carryover-allocation basis as of the close of March 12, 2004, is not more than 10 percent of D's reasonably expected basis in the single-building project, the building is not a qualified building for purposes of section 42(h)(1)(E)(ii) and paragraph (a) of this section. Accordingly, the carryover allocation to D must be returned to the Agency. The allocation is valid for purposes of determining the amount of credit allocated by Agency from State X's 2003 State housing credit ceiling, but is included in the returned credit component of State X's 2004 housing credit ceiling.

(c) *Verification of basis by Agency—(1) Verification requirement.* An Agency that makes a carryover allocation to a taxpayer must verify that the taxpayer has met the 10 percent basis requirement of paragraph (a)(2) of this section.

(2) *Manner of verification.* An Agency may verify that a taxpayer has incurred more than 10 percent of its reasonably expected basis in a project by obtaining a certification from the taxpayer, in writing and under penalty of perjury, that the taxpayer has incurred by the close of the calendar year of the allocation (for allocations made before July 1) or by the close of the date that is 6 months after the date the allocation is made (for allocations made after June 30) more than 10 percent of the reasonably expected basis in the project. The certification must be accompanied by supporting documentation that the Agency must review. Supporting documentation may include, for example, copies of checks or other records of payments. Alternatively, an Agency may verify that the taxpayer has incurred adequate basis by requiring that the taxpayer obtain from an attorney or certified public accountant a written certification to the Agency, that the attorney or accountant has examined all eligible costs incurred with respect to the project and that, based upon this examination, it is the attorney's or accountant's belief that the taxpayer has incurred more than 10 percent of its reasonably expected basis in the project by the close of the calendar year of the allocation (for allocations made before July 1) or by the close of the date that is 6 months after the date the allocation is made (for allocations made after June 30).

(3) *Time of verification—(i) Allocations made before July 1.* For a carryover allocation made before July 1, an Agency may require that the basis certification be submitted to or received by the Agency prior to the close of the calendar year of allocation or within a reasonable time following the close of the calendar year of allocation. The Agency will need to verify basis as provided in paragraph (c)(2) of this section to accurately complete the Form 8610, "Annual Low-Income Housing Credit Agencies Report," and the Schedule A (Form 8610), "Carryover Allocation of Low-Income Housing Credit," for the calendar year of the allocation. If the basis certification is not timely made, or supporting documentation is lacking, inadequate, or does not actually support the certification, the Agency should notify the taxpayer and try to get adequate documentation. If the Agency cannot verify before the Form 8610 is filed that the taxpayer has satisfied the 10 percent basis requirement for a carryover allocation made before July 1, the allocation is not valid and is treated as if it had not been made and the carryover allocation should not be reported on the Schedule A (Form 8610).

(ii) *Allocations made after June 30.* An Agency may require that the basis certification be submitted to or received by the Agency prior to the close of the date that is 6 months after the date the allocation was made or within a reasonable period of time following the close of the date that is 6 months after the date the allocation was made. The Agency will need to verify basis as provided in paragraph (c)(2) of this section. If the basis certification is not timely made, or supporting documentation is lacking, inadequate, or does not actually support the certification, the Agency should notify the taxpayer and try to get adequate documentation. If the Agency cannot verify that the taxpayer has satisfied the 10 percent basis requirement for a carryover allocation made after June 30, the allocation must be returned to the Agency. The carryover allocation is a valid allocation for the calendar year of the allocation, but is included in the returned credit component of the State housing credit ceiling for the calendar year following the calendar year of the allocation.

(d) *Requirements for making carryover allocations—(1) In general.* Generally, an allocation is made when an Agency issues the Form 8609, 'Low-Income Housing Credit Allocation Certification,' for a building. See §1.42-1T(d)(8)(ii). An Agency does not issue the Form 8609 for a building until the building is placed in service. However, in cases where allocations of credit are made pursuant to section 42(h)(1)(E) (relating to carryover allocations for buildings) or section 42(h)(1)(F) (relating to

carryover allocations for multiple-building projects), Form 8609 is not used as the allocating document because the buildings are not yet in service. When an allocation is made pursuant to section 42(h)(1) (E) or (F), the allocating document is the document meeting the requirements of paragraph (d)(2) of this section. In addition, when an allocation is made pursuant to section 42(h)(1)(F), the requirements of paragraph (d)(3) of this section must be met for the allocation to be valid. An allocation pursuant to section 42(h)(1) (E) or (F) reduces the state housing credit ceiling for the year in which the allocation is made, whether or not the Form 8609 is also issued in that year.

(2) *Requirements for allocation.* An allocation pursuant to section 42(h)(1) (E) or (F) is made when an allocation document containing the following information is completed, signed, and dated by an authorized official of the Agency—

(i) The address of each building in the project, or if none exists, a specific description of the location of each building;

(ii) The name, address, and taxpayer identification number of the taxpayer receiving the allocation;

(iii) The name and address of the Agency;

(iv) The taxpayer identification number of the Agency;

(v) The date of the allocation;

(vi) The housing credit dollar amount allocated to the building or project, as applicable;

(vii) The taxpayer's reasonably expected basis in the project (land and depreciable basis) as of the close of the second calendar year following the calendar year in which the allocation is made;

(viii) For carryover allocations made before July 1, the taxpayer's basis in the project (land and depreciable basis) as of the close of the calendar year of the allocation and the percentage that basis bears to the reasonably expected basis in the project (land and depreciable basis) as of the close of the second calendar year following the calendar year of allocation;

(ix) The date that each building in the project is expected to be placed in service; and

(x) The Building Identification Number (B.I.N.) to be assigned to each building in the project. The B.I.N. must reflect the year an allocation is first made to the building, regardless of the year that the building is placed in service. This B.I.N. must be used for all allocations of credit for the building. For example, rehabilitation expenditures treated as a separate new building under section 42(e) should not have a separate B.I.N. if the building to which the rehabilitation expenditures are made has a B.I.N. In this case, the B.I.N. used for the rehabilitation expenditures shall be the B.I.N. previously assigned to the building, although the rehabilitation expenditures must have a separate Form 8609 for the allocation. Similarly, a newly constructed building that receives an allocation of credit in different calendar years must have a separate Form 8609 for each allocation. The B.I.N. assigned to the building for the first allocation must be used for the subsequent allocation.

(3) *Special rules for project-based allocations—(i) In general.* An allocation pursuant to section 42(h)(1)(F) (a project-based allocation) must meet the requirements of this section as well as the requirements of section 42(h)(1)(F), including the minimum basis requirement of section 42(h)(1)(E)(ii).

(ii) *Requirement of section 42(h)(1)(F)(i)(III).* An allocation satisfies the requirement of section 42(h)(1)(F)(i)(III) if the Form 8609 that is issued for each building that is placed in service in the project states the portion of the project-based allocation that is applied to that building.

(4) *Recordkeeping requirements—(i) Taxpayer.* When an allocation is made pursuant to section 42(h)(1)(E) or (F), the taxpayer must retain a copy of the allocation document. The Form 8609 that reflects the allocation must be filed for the first taxable year that the credit is claimed and for each taxable year thereafter throughout the compliance period, whether or not a credit is claimed for the taxable year.

(ii) *Agency*. The Agency must retain the original carryover allocation document made under paragraph (d)(2) of this section and file Schedule A (Form 8610) with the Agency's Form 8610 for the year the allocation is made. The Agency must also retain a copy of the Form 8609 that is issued to the taxpayer and file the original with the Agency's Form 8610 that reflects the year the form is issued.

(5) *Separate procedure for election of appropriate percentage month*. If a taxpayer receives an allocation under section 42(h)(1) (E) or (F) and wishes to elect under section 42(b)(2)(A)(ii) to use the appropriate percentage for a month other than the month in which a building is placed in service, the requirements specified in §1.42-8 must be met for the election to be effective.

(e) *Special rules*. The following rules apply for purposes of this section.

(1) *Treatment of partnerships and other flow-through entities*. With respect to taxpayers that own projects through partnerships or other flow-through entities (e.g., S corporations, estates, or trusts), carryover-allocation basis is determined at the entity level using the rules provided by this section. In addition, the entity is responsible for providing to the Agency the certification and documentation required under the basis verification requirement in paragraph (c) of this section.

(2) *Transferees*. If land or depreciable property that is expected to be part of a project is transferred after a carryover allocation has been made for a building that is reasonably expected to be part of the project, but before the close of the calendar year of the allocation (for allocations made before July 1) or by the close of the date that is 6 months after the date the allocation is made (for allocations made after June 30), the transferee's carryover-allocation basis is determined under the principles of this section and section 42(d)(7). See also Rev. Rul. 91-38, 1991-2 C.B. 3 (see §601.601(d)(2)(ii)(b) of this chapter). In addition, the transferee is treated as the taxpayer for purposes of the basis verification requirement of this section, and therefore, is responsible for providing to the Agency the required certifications and documentation.

[T.D. 8520, 59 FR 10069, Mar. 3, 1994, as amended by T.D. 8859, 65 FR 2328, Jan. 14, 2000; 65 FR 16317, Mar. 28, 2000; T.D. 9110, 69 FR 502, Jan. 6, 2004]

Exhibit G IRS Regulations § 1.142-6 Carryover and 1.42-10 Utility Allowance

§1.42-10 Utility allowances.

(a) *Inclusion of utility allowances in gross rent*. If the cost of any utility (other than telephone, cable television, or Internet) for a residential rental unit is paid directly by the tenant(s), and not by or through the owner of the building, the gross rent for that unit includes the applicable utility allowance determined under this section. For purposes of the preceding sentence, if the cost of a particular utility for a residential unit is paid pursuant to an actual-consumption submetering arrangement within the meaning of paragraph (e)(1) of this section, then that cost is treated as being paid directly by the tenant(s) and not by or through the owner of the building. This section only applies for purposes of determining gross rent under section 42(g)(2)(B)(ii) as to rent-restricted units.

(b) *Applicable utility allowances—(1) Buildings assisted by the Rural Housing Service*. If a building receives assistance from the Rural Housing Service (RHS-assisted building), the applicable utility allowance for all rent-restricted units in the building is the utility allowance determined under the method prescribed by the Rural Housing Service (RHS) for the building (whether or not the building or its tenants also receive other state or federal assistance).

(2) *Buildings with Rural Housing Service assisted tenants*. If any tenant in a building receives RHS rental assistance payments (RHS tenant assistance), the applicable utility allowance for all rent-restricted units in the building (including any units occupied by tenants receiving rental assistance payments from the Department of Housing and Urban Development (HUD)) is the applicable RHS utility allowance.

(3) *Buildings regulated by the Department of Housing and Urban Development*. If neither a building nor any tenant in the building receives RHS housing assistance, and the rents and utility allowances of the building are regulated by HUD (HUD-regulated buildings), the applicable utility

allowance for all rent-restricted units in the building is the applicable HUD utility allowance.

(4) *Other buildings.* If a building is neither an RHS-assisted nor a HUD-regulated building, and no tenant in the building receives RHS tenant assistance, the applicable utility allowance for rent-restricted units in the building is determined under the following methods.

(i) *Tenants receiving HUD rental assistance.* The applicable utility allowance for any rent-restricted units occupied by tenants receiving HUD rental assistance payments (HUD tenant assistance) is the applicable Public Housing Authority (PHA) utility allowance established for the Section 8 Existing Housing Program.

(ii) *Other tenants—(A) General rule.* If none of the rules of paragraphs (b)(1), (2), (3), and (4)(i) of this section apply to determine the appropriate utility allowance for a rent-restricted unit, then the appropriate utility allowance for the unit is the applicable PHA utility allowance. However, if a local utility company estimate is obtained for any unit in the building in accordance with paragraph (b)(4)(ii)(B) of this section, that estimate becomes the appropriate utility allowance for all rent-restricted units of similar size and construction in the building. This local utility company estimate procedure is not available for and does not apply to units to which the rules of paragraphs (b) (1), (2), (3), or (4)(i) of this section apply. However, if a local utility company estimate is obtained for any unit in the building under paragraph (b)(4)(ii)(B) of this section, a State or local housing credit agency (Agency) provides a building owner with an estimate for any unit in a building under paragraph (b)(4)(ii)(C) of this section, a cost estimate is calculated using the HUD Utility Schedule Model under paragraph (b)(4)(ii)(D) of this section, or a cost estimate is calculated by an energy consumption model under paragraph (b)(4)(ii)(E) of this section, then the estimate under paragraph (b)(4)(ii)(B), (C), (D), or (E) becomes the applicable utility allowance for all rent-restricted units of similar size and construction in the building. Paragraphs (b)(4)(ii)(B), (C), (D), and (E) of this section do not apply to units to which the rules of paragraphs (b)(1), (2), (3), or (4)(i) of this section apply.

(B) *Utility company estimate.* Any interested party (including a low-income tenant, a building owner, or an Agency) may obtain a local utility company estimate for a unit. The estimate is obtained when the interested party receives, in writing, information from a local utility company providing the estimated cost of that utility for a unit of similar size and construction for the geographic area in which the building containing the unit is located. In the case of deregulated utility services, the interested party is required to obtain an estimate only from one utility company even if multiple companies can provide the same utility service to a unit. However, the utility company must offer utility services to the building in order for that utility company's rates to be used in calculating utility allowances. The estimate should include all component deregulated charges for providing the utility service. The local utility company estimate may be obtained by an interested party at any time during the building's extended use period (see section 42(h)(6)(D)) or, if the building does not have an extended use period, during the building's compliance period (see section 42(i)(1)). Unless the parties agree otherwise, costs incurred in obtaining the estimate are borne by the initiating party. The interested party that obtains the local utility company estimate (the initiating party) must retain the original of the utility company estimate and must furnish a copy of the local utility company estimate to the owner of the building (where the initiating party is not the owner), and the Agency that allocated credit to the building (where the initiating party is not the Agency). The owner of the building must make available copies of the utility company estimate to the tenants in the building.

(C) *Agency estimate.* A building owner may obtain a utility estimate for each unit in the building from the Agency that has jurisdiction over the building provided the Agency agrees to provide the estimate. The estimate is obtained when the building owner receives, in writing, information from the Agency providing the estimated per-unit cost of the utilities for units of similar size and construction for the geographic area in which the building containing the units is located. The Agency estimate may be obtained by a building owner at any time during the building's extended use period (see section 42(h)(6)(D)). Costs incurred in obtaining the estimate are borne by the building owner. In establishing an accurate utility allowance estimate for a particular building, an Agency (or an agent or other private contractor of the Agency that is a qualified professional within the meaning of paragraph (b)(4)(ii)(E) of this section) must take into account, among other things, local utility rates, property type, climate and degree-day variables by region in the State, taxes and fees on utility charges, building materials, and mechanical systems. If the Agency uses an agent or other private contractor to calculate the utility estimates, the agent or contractor and the owner must not be related within the meaning of section 267(b) or 707(b). An Agency may also use actual utility company usage data and rates for the building. However, use of the Agency estimate is limited to the building's consumption data for the twelve-month

period ending no earlier than 60 days prior to the beginning of the 90-day period under paragraph (c)(1) of this section and utility rates used for the Agency estimate must be no older than the rates in place 60 days prior to the beginning of the 90-day period under paragraph (c)(1) of this section. In the case of newly constructed or renovated buildings with less than 12 months of consumption data, the Agency (or an agent or other private contractor of the Agency that is a qualified professional within the meaning of paragraph (b)(4)(ii)(E) of this section) may use consumption data for the 12-month period of units of similar size and construction in the geographic area in which the building containing the units is located.

(D) *HUD Utility Schedule Model.* A building owner may calculate a utility estimate using the “HUD Utility Schedule Model” that can be found on the Low-Income Housing Tax Credits page at <http://www.huduser.org/datasets/lihtc.html> (or successor URL). Utility rates used for the HUD Utility Schedule Model must be no older than the rates in place 60 days prior to the beginning of the 90-day period under paragraph (c)(1) of this section.

(E) *Energy consumption model.* A building owner may calculate utility estimates using an energy and water and sewage consumption and analysis model (energy consumption model). The energy consumption model must, at a minimum, take into account specific factors including, but not limited to, unit size, building orientation, design and materials, mechanical systems, appliances, characteristics of the building location, and available historical data. The utility consumption estimates must be calculated by a properly licensed engineer or other qualified professional. The qualified professional and the building owner must not be related within the meaning of section 267(b) or 707(b). If a qualified professional is not a properly licensed engineer and if the building owner wants to utilize that qualified professional to calculate utility consumption estimates, then the owner must obtain approval from the Agency that has jurisdiction over the building. Further, regardless of the type of qualified professional, the Agency may approve or disapprove of the energy consumption model or require information before permitting its use. In addition, utility rates used for the energy consumption model must be no older than the rates in place 60 days prior to the beginning of the 90-day period under paragraph (c)(1) of this section.

(c) *Changes in applicable utility allowance—(1) In general.* If, at any time during the building's extended use period (as defined in section 42(h)(6)(D)), the applicable utility allowance for units changes, the new utility allowance must be used to compute gross rents of the units due 90 days after the change (the 90-day period). For example, if rent must be lowered because a local utility company estimate is obtained that shows a higher utility cost than the otherwise applicable PHA utility allowance, the lower rent must be in effect for rent due at the end of the 90-day period. A building owner using a utility company estimate under paragraph (b)(4)(ii)(B) of this section, the HUD Utility Schedule Model under paragraph (b)(4)(ii)(D) of this section, or an energy consumption model under paragraph (b)(4)(ii)(E) of this section must submit copies of the utility estimates to the Agency that has jurisdiction over the building and make the estimates available to all tenants in the building at the beginning of the 90-day period before the utility allowances can be used in determining the gross rent of rent-restricted units. An Agency may require additional information from the owner during the 90-day period. Any utility estimates obtained under the Agency estimate under paragraph (b)(4)(ii)(C) of this section must also be made available to all tenants in the building at the beginning of the 90-day period. The building owner must pay for all costs incurred in obtaining the estimates under paragraphs (b)(4)(ii)(B), (C), (D), and (E) of this section and providing the estimates to the Agency and the tenants. The building owner is not required to review the utility allowances, or implement new utility allowances, until the building has achieved 90 percent occupancy for a period of 90 consecutive days or the end of the first year of the credit period, whichever is earlier.

(2) *Annual review.* A building owner must review at least once during each calendar year the basis on which utility allowances have been established and must update the applicable utility allowance in accordance with paragraph (c)(1) of this section. The review must take into account any changes to the building such as any energy conservation measures that affect energy consumption and changes in utility rates.

(d) *Record retention.* The building owner must retain any utility consumption estimates and supporting data as part of the taxpayer's records for purposes of §1.6001-1(a).

(e) *Actual-consumption submetering arrangements—(1) Definition.* For purposes of this section, an actual-consumption submetering arrangement for a utility in a residential unit possesses all of the following attributes:

(i) The utility consumed in the unit is described in paragraph (e)(1)(i)(A) of this section or in §1.42-10T(e)(1)(i)(B);

(A) The utility is purchased from or through a local utility company by the building owner (or its agent or other party acting on behalf of the building owner).

(B) [Reserved]. For further guidance see §1.42-10T(e)(1)(i)(B) through (e)(1)(i)(C)(3).

(ii) The tenants in the unit are billed for, and pay the building owner (or its agent or other party acting on behalf of the building owner) for, the unit's consumption of the utility;

(iii) The billed amount reflects the unit's actual consumption of the utility. In the case of sewerage charges, however, if the unit's sewerage charges are combined on the bill with water charges and the sewerage charges are determined based on the actual water consumption of the unit, then the bill is treated as reflecting the actual sewerage consumption of the unit; and

(iv) The rate at which the building owner bills for the utility satisfies the following requirements:

(A) To the extent that the utility consumed is described in paragraph (e)(1)(i)(A) of this section, the utility rate charged to the tenants of the unit does not exceed the rate incurred by the building owner for that utility; and

(B) To the extent that the utility consumed is described in §1.42-10T(e)(1)(i)(B), the utility rate charged to the tenants of the unit does not exceed the rate described in §1.42-10T(e)(1)(iv)(B).

(2) *Administrative fees.* If the owner charges a unit's tenants a fee for administering an actual-consumption submetering arrangement, the fee is not considered gross rent for purposes of section 42(g)(2). The preceding sentence, however, does not apply unless the fee is computed in the same manner for every unit receiving the same submetered utility service, nor does it apply to any amount by which the aggregate monthly fee or fees for all of the unit's utilities under one or more actual-consumption submetering arrangements exceed the greater of—

(i) Five dollars per month;

(ii) An amount (if any) designated by publication in the Internal Revenue Bulletin (see §601.601(d)(2)(ii) of this chapter); or

(iii) The lesser of—

(A) The dollar amount (if any) specifically prescribed under a State or local law; or

(B) A maximum amount (if any) designated by publication in the Internal Revenue Bulletin (see §601.601(d)(2)(ii) of this chapter).

[T.D. 8520, 59 FR 10073, Mar. 3, 1994, as amended by T.D. 9420, 73 FR 43867, July 29, 2008; T.D. 9755, 81 FR 11109, Mar. 3, 2016]

§1.42-10T Energy obtained directly from renewable sources (temporary).

(a) through (e)(1)(i)(A) [Reserved]. For further guidance see §1.42-10(a) through (e)(1)(i)(A).

(B) *Utility not purchased from or through a local utility company.* The utility is not described in §1.42-10(e)(1)(i)(A) and is produced from a renewable source (within the meaning of paragraph (e)(1)(i)(C) of this section).

(C) *Renewable source.* For purposes of paragraph (e)(1)(i)(B) of this section, a utility is produced from a renewable source if—

(1) It is energy that is produced from energy property described in section 48;

(2) It is energy that is produced from property that is part of a facility described in section 45(d)(1) through (4), (6), (9), or (11); or

(3) It is a utility that is described in guidance published for this purpose in the Internal Revenue Bulletin (see §601.601(d)(2)(ii) of this chapter).

(ii) through (iv)(A) [Reserved]. For further guidance see §1.42-10(e)(1)(ii) through (e)(1)(iv)(A).

(B) The rate described in this paragraph (e)(1)(iv)(B) is the rate at which the local utility company would have charged the tenants in the unit for the utility if that entity had provided it to them.

(2) [Reserved]

(f) *Date of applicability.* This section applies to a building owner's taxable years beginning on or after March 3, 2016. A building owner may apply the provisions of this section to the building owner's taxable years beginning before March 3, 2016.

(g) *Expiration date.* The applicability of this section expires on March 1, 2019.

[T.D. 9755, 81 FR 11110, Mar. 3, 2016]

Exhibit H

Section 42 Internal Revenue Code

ELECTRONIC CODE OF FEDERAL REGULATIONS

[View past updates to the e-CFR.](#)

[Click here to learn more.](#)

e-CFR data is current as of July 12, 2017

[Title 26](#) → [Chapter I](#) → [Subchapter A](#) → [Part 1](#) →

As a reference: see e-CFR for Section 42 regulations

https://www.ecfr.gov/cgi-bin/text-idx?SID=9c73d081616dc5aa33002fc9d0bbc2d7&mc=true&node=se26.1.1_142_60&rgn=div8

EXHIBIT P
GUIDELINES FOR DETERMINING SECTION 501(c)(3) STATUS

Guidelines for Determining Whether Organizations Providing Housing are Described in Section 501(c)(3) or the Code

Announcement 95-37

This announcement issues, in proposed form, a revenue procedure relating to the standards used by the Internal Revenue Service in determining whether certain charities providing housing are eligible for tax-exempt status under section 501(c)(3) of the Internal Revenue Code. The proposed revenue procedure includes a safe harbor for charities that serve the housing needs of the poor and distressed. The Service originally set forth a safe harbor on this issue in Notice 93-1, 1993-1 C.B. 290. This proposed revenue procedure takes into account the comments received by the Service on Notice 93-1.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

The Service invites comments on the proposed revenue procedure. Public comments should be submitted in writing on or before August 14, 1995. Comments should be sent to the following address:

Internal Revenue Service
1111 Constitution Avenue,
N.W. Washington, D.C. 0224
Attn: Lynn Kawecki
CP:E:EO:T:S Room 6539

The Service will consider holding a public hearing if it receives a written request for a hearing from any person who submits timely written comments. If a public hearing is scheduled, notice of the time, date, and place of hearing will be published in the Internal Revenue Bulletin.

DRAFTING INFORMATION

The principal authors of this announcement are Lyn Kawecki and Marvin Friedlander. For further information regarding this announcement, contact Mr. Kawecki at (202) 6227728 or Mr. Friedlander at (202) 622-8715 (not toll-free numbers).

Proposed Revenue Procedure

SECTION 1. PURPOSE

.01 This revenue procedure sets forth a safe harbor under which organizations that provide low-income housing will be considered charitable as described in section 501(c)(3) of the Code because they relieve the poor and distressed as described in section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations. This revenue procedure also describes the facts and circumstances test that will apply to determine whether organizations that fall outside the safe harbor relieve the poor and distressed such that they will be considered charitable organizations described in section 501(c)(3) of the Code. It also clarifies that housing organizations may rely on other charitable purposes to qualify for recognition of exemption from federal income tax as organizations described in section 501(c)(3) of the Code. These other charitable purposes are described in section 1.501(c)(3)-1(d)(2) of the regulations.

This revenue procedure supersedes the application referral described in Notice 93-1, 1993-1 C.B. 290. .02 This revenue procedure does not alter the standards that have long been applied to determine whether low-income housing organizations qualify for tax-exempt status under section 501(c)(3) of the Code. Rather, it is intended to expedite the consideration of applications for tax-exempt status filed by such organizations by providing a safe harbor and by accumulating relevant information on the existing standards for exemption in a single document.

SEC. 2. BACKGROUND OF SAFE HARBOR

.01 Rev. Rule 67-138, 1967-1 C.B. 129, Rev. Rul. 70-585, 1970-2 C.B. 115, and Rev. Rul. 76-408, 1976-2 C.B. 145, hold that the provision of housing for low-income persons accomplishes charitable purposes by relieving the poor and distressed. The Service has long held that poor and distressed beneficiaries must be needy in the sense that they cannot afford the necessities of life. Rev. Rules. 67-138, 70-585, and 76-408 refer to the needs of housing recipients and to their inability to secure adequate housing under all the facts and circumstances to determine whether they are poor and distressed.

.02 The existence of a national housing policy to maintain a commitment to provide decent, safe, and sanitary housing for every American family is reflected in several federal housing acts. See, for example, section 2 of the United States Housing Act of 1937, 42 U.S.C. § 1437; section 2 of the Housing Act of 1949, 42 U.S.C. § 1441; section 2 of the Housing and Urban Development Act of 1968, 12 U.S.C. § 17011; and sections 101, 102, and 202 of the Cranston-Gonzalez National Affordable Housing Act, 42 D.S.C. §§ 12701, 12702, and 12721. Not all beneficiaries of these housing acts, however, are necessarily poor and distressed within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations.

EXHIBIT P
GUIDELINES FOR DETERMINING SECTION 501(c)(3) STATUS

.03 In order to support national housing policy, the safe harbor contained in this revenue procedure identifies those low-income housing organizations that will, with certainty, be considered to relieve the poor and distressed. The safe harbor permits a limited number of units occupied by residents with incomes above the low-income limits in order to assist in the social and economic integration of the poorer residents and, thereby, further the organization's charitable purposes. To avoid giving undue assistance to those who can otherwise afford safe, decent, and sanitary housing, the safe harbor requires occupancy by significant levels of both very low-income and low-income families.

.04 Low-income housing organizations that fall outside the safe harbor may still be considered organizations that offer relief to the poor and distressed based on all the surrounding facts and circumstances. Some of the facts and circumstances that will be taken into consideration in determining whether a low-income housing organization *will* be so considered are set forth in section 4.

.05 Low-income housing organizations may also qualify for tax-exempt status because they serve a charitable purpose described in section 501(c)(3) of the Code other than relief of the poor and distressed. Exempt purposes other than relief of the poor and distressed are discussed in section 5.

.06 To be recognized as exempt from income tax under section 501(c)(3), a low-income housing organization must not only serve a charitable purpose but also meet the other requirements of that section, including the prohibitions against inurement and private benefit. Specific concerns with respect to these prohibitions are set forth in section 6.

SEC. 3. SAFE HARBOR FOR RELIEVING THE POOR AND DISTRESSED

.01 An organization *will* be considered charitable as described in section 501(c)(3) if it satisfies the following requirements:

- (1) The organization establishes for each project that (a) at least 75 percent of the units are occupied by residents that qualify as low-income; and (b) either at least 20 percent of the units are occupied by residents that also meet the very low-income limit for the area or 40 percent of the units are occupied by residents that also do not exceed 120 percent of the area's very low-income limit. Up to 25 percent of the units may be provided at market rates to persons who have incomes in excess of the low-income limit.
- (2) The project is actually occupied by poor and distressed residents. With new construction, a reasonable start-up period is allowed before an organization must meet this requirement. For acquisition transactions, the transition period to satisfy this requirement will be assumed to be reasonable if the transition is completed within one year. If a project operates under a government program that allows a longer transition period, then this longer period will be used to determine reasonableness.
- (3) The housing is affordable to the charitable beneficiaries. This requirement will ordinarily be satisfied by the adoption of a rental policy that follows government imposed rental restrictions or a rental policy that otherwise provides for the relief of the poor and distressed.
- (4) If the project consists of multiple buildings, they must share the same grounds.

.02 In applying this safe harbor, the Service *will* follow the provisions listed below:

- (1) Low-income families and very low-income families will be identified in accordance with the income limits computed and published by the Department of Housing and Urban Development ("HUD") in *Income Limits for Low and Very Low-Income Families Under the Housing Act of 1937*. The term "very low-income" is defined by the relevant housing statute as 50 percent of an area's median income. The term "low-income" is defined by the same statute as 80 percent of an area's median income. However, these income limits may be adjusted by HUD to reflect economic differences, such as high housing costs, in each area. If HUD's program terminates, the Service will use income limits computed under such program as is in effect immediately before such termination. Copies of all or part of HUD's publication may be obtained by calling HUD at (800) 245-2691 (HUD charges a small fee to cover costs of reproduction).
- (2) The retention of the right to evict tenants for failure to pay rent or other misconduct *will* not, in and of itself, cause the organization to fail to meet the safe harbor.
- (3) An organization originally meeting the safe harbor will continue to satisfy the requirements of the safe harbor if a resident's income increases, provided that the resident's income does not exceed 140 percent of the applicable income limit under the safe harbor. If the resident's income exceeds 140 percent of the qualifying limit, the organization *will* not fail to meet the safe harbor if it rents the next comparable non-qualifying unit to someone under the qualifying income limits.
- (4) To be considered charitable, an organization that provides assistance to the aged or physically handicapped who are not poor must satisfy the requirements set forth in Rev. Rul. 72-124, 1972-1 C.B. 145, Rev. Rul. 79-18, 1979-1 C.B. 194, and Rev. Rul. 79-19, 1979-1 C.B. 195. If an organization meets the safe harbor, then it does not need to meet the requirements of these rulings even if all of its residents are elderly or handicapped residents. However, an organization may not tax a combination of elderly or handicapped persons and low-income persons to establish the 75-percent occupancy requirement of the safe harbor. An organization with a mix of elderly or handicapped residents and low-income residents may still qualify for tax-exempt status under the facts and circumstances test set forth in section 4.

EXHIBIT P
GUIDELINES FOR DETERMINING SECTION 501(c)(3) STATUS

SEC. 4. FACTS AND CIRCUMSTANCES TEST FOR RELIEVING THE POOR AND DISTRESSED

.01 If the safe harbor contained in section 3 is not satisfied, an organization may demonstrate that it relieves the poor and distressed by reference to all the surrounding facts and circumstances. Facts and circumstances that demonstrate relief of the poor may include, but are not limited to, the following:

- (1) A substantially greater percentage of residents than required by the safe harbor with incomes up to 120 percent of the area's very low-income limit.
- (2) Limited degree of deviation from the safe harbor percentages.
- (3) Limitation of rents to ensure that they are affordable to low-income and very low-income residents.
- (4) Participation in a government housing program designed to provide affordable housing.
- (5) Operation through a community-based board of directors, particularly if the selection process demonstrates that community groups have input into the organization's operations.
- (6) The provision of additional social services affordable to the poor residents.
- (7) Relationship with an existing 501(c)(3) organization active in low-income housing for at least five years if the existing organization demonstrates control.
- (8) Acceptance of residents who, when considered individually, have unusual burdens such as extremely high medical costs which cause them to be in a condition similar to persons within the qualifying income limits in spite of their higher incomes.
- (9) Participation in a homeownership program designed to provide homeownership opportunities for families that cannot otherwise afford to purchase safe and decent housing.
- (10) Existence of affordability covenants or restrictions running with the property.

.02 Application of the facts and circumstances test is illustrated by the following examples:

- (1) Organization *N* operates pursuant to a government statute to preserve low and moderate income housing projects. Seventy percent of its residents have incomes that do not exceed the area's low-income limit. Fifty percent of its residents have incomes that are below the area's very low-income limit. *N* restricts rents to residents below the qualifying income limits to no more than 30 percent of the residents' incomes. *N* is close to meeting the safe harbor. *N* has a substantially greater percentage of very low-income residents than required by the safe harbor; it participates in a federal housing program; and it restricts its rents. Although *N* does not meet the safe harbor, the facts and circumstances demonstrate that *N* relieves the poor and distressed.
- (2) Organization *O* will finance a housing project using tax-exempt bonds pursuant to section 145(d) of the Code. *O* will meet the 20-50 test under section 142(d)(1)(A). Another 45 percent of the residents will have incomes at or below 80 percent of the area's median income. The final 35 percent of the residents will have incomes above 80 percent of the median income. *O* will restrict rents to residents below the qualifying income limits to no more than 30 percent of the residents' incomes. *O* will provide social services to project residents and to other low-income residents in the neighborhood. Also, *O* will purchase its project through a government program designed to retain low-income housing stock. *O* does not meet the safe harbor. However, the facts and circumstances demonstrate that *O* relieves the poor and distressed.
- (3) Organization *R* provides homeownership opportunities to purchasers determined to be low-income under a federal housing program. Beneficiaries under the program cannot afford to purchase housing without assistance and they cannot qualify for conventional financing. *R*'s residents will have the following composition: 40 percent will not exceed 140 percent of the very low-income limit for the area, 25 percent will not exceed the low-income limit, and 35 percent will exceed the low-income limit but will not exceed 115 percent of the area's median income. *R* does not satisfy the safe harbor. However, the facts and circumstances demonstrate that *R* relieves the poor and distressed.
- (4) Organization *U* will purchase existing residential rental housing financed with tax-exempt bonds under section 145(d) of the Code. *U* will meet the 40-60 test of section 142(d)(1)(B). It will provide the balance of its units to residents with incomes at or above median income levels. *U* has a community-based board of director. *U* does not satisfy the safe harbor. Moreover, the facts and circumstances do not demonstrate that *U* relieves the poor and distressed.
- (5) Organization *V* operates housing in a section of the city where income levels are well below the other parts of the city. One hundred percent of *V*'s residents have incomes under the very low-income limit for the area, yet they pay rents that are above 50 percent of their incomes. *V* has not otherwise demonstrated that the units are affordable to its residents. Although the residents are all considered poor and distressed under the safe harbor, *V* does not relieve the poverty of the residents.
- (6) Organization *W* provides homeownership opportunities to purchasers with incomes up to 115 percent of the area's median income. *W* does not meet the income level required under the safe harbor. *W*'s board of directors is representative of community interests, and *W* provides classes and counseling services for its residents. The facts and circumstances do not demonstrate that *W* relieves the poor and distressed.

SEC. 5. EXEMPT PURPOSES OTHER THAN RELIEVING THE POOR AND DISTRESSED

.01 Relief of the poor and distressed, whether demonstrated by satisfaction of the safe harbor described in section 3 of this Revenue Procedure or by reference to the facts and circumstances test described in section 4, does not constitute the only exempt purpose that a housing organization may have. Such organizations may qualify for exemption without having to satisfy the standards for relief of the poor and distressed by providing housing in a way that accomplishes any of the purposes set forth in section 501(c)(3) of the Code or section 1.501(c)(3)-1(d)(2) of the regulations. Those purposes include, but are not limited to, the following:

- (1) Combating community deterioration is an exempt purpose, as illustrated by Rev. Rul. 68-17, 1968-1 C.B. 247, Rev. Rul. 68-655, 1968-2 C.B. 213, Rev. Rul. 70-585, 1970-2 C.B. 115 (Situation 3), and Rev. Rul. 76-147, 1976-1 C.B. 151. An organization that combats community deterioration must (1) operate in an area with actual or potential deterioration, and (2) directly prevent or relieve that deterioration. Constructing or rehabilitating housing has the potential to combat community deterioration.

EXHIBIT P
GUIDELINES FOR DETERMINING SECTION 501(c)(3) STATUS

(2) Lessening the burdens of government is an exempt purpose, as illustrated by Rev. Rub. 85-1 and 85-2, 1985-1 C.B. 178. An organization lessens the burdens of government if (a) there is an objective manifestation by the governmental unit that it considers the activities of the organization to be the government's burdens, and (b) the organization actually lessens the government's burdens.

(3) Elimination of discrimination and prejudice is an exempt purpose, as illustrated by Rev. Rul. 68-655, 1968-2 C.B. 213, and Rev. Rul.

70-585, 1970-2 C.B. 115 (Situation 2). These rulings describe organizations that further charitable purposes by assisting persons in specific racial groups to acquire housing for the purpose of stabilizing neighborhoods or reducing racial imbalances.

(4) Lessening neighborhood tensions is an exempt purpose, as illustrated by Rev. Rul. 68-655, 1968-2 C.B. 213, and Rev. Rul. 70-585,

1970-2 C.B. 115 (Situation 2). It is generally identified as an additional charitable purpose by organizations that fight poverty and community deterioration associated with overcrowding in lower income areas in which ethnic or racial tensions are high.

(5) Relief of the distress of the elderly or physically handicapped is an exempt purpose, as illustrated by Rev. Rul. 72-124, 1972-1 C.B.

145, Rev. Rul. 79-18, 1979-1 C.B. 194, and Rev. Rul. 79-19, 1979-1 C.B. 195. M organization may further a charitable purpose by meeting the special needs of the elderly or physically handicapped.

SEC. 6. OTHER CONSIDERATIONS

If an organization furthers a charitable purpose such as relieving the poor and distressed, it nevertheless may fail to qualify for exemption because private interests of individuals with a financial stake in the project are furthered. For example, the role of a private developer or management company in the organization's activities must be carefully scrutinized to ensure the absence of inurement or impermissible private benefit resulting from real property sales, development fees, or management contracts.

SEC. 7. EFFECT ON OTHER

DOCUMENTS Notice 93-1 is

superseded.

§1.42-5 Monitoring compliance with low-income housing credit requirements.

(a) *Compliance monitoring requirement*—(1) *In general.* Under section 42(m)(1)(B)(iii), an allocation plan is not qualified unless it contains a procedure that the State or local housing credit agency (“Agency”) (or an agent of, or other private contractor hired by, the Agency) will follow in monitoring for noncompliance with the provisions of section 42 and in notifying the Internal Revenue Service of any noncompliance of which the Agency becomes aware. These regulations only address compliance monitoring procedures required of Agencies. The regulations do not address forms and other records that may be required by the Service on examination or audit. For example, if a building is sold or otherwise transferred by the owner, the transferee should obtain from the transferor information related to the first year of the credit period so that the transferee can substantiate credits claimed.

(2) *Requirements for a monitoring procedure*—(i) *In general.* A procedure for monitoring for noncompliance under section 42(m)(1)(B)(iii) must include—

- (A) The recordkeeping and record retention provisions of paragraph (b) of this section;
- (B) The certification and review provisions of paragraph (c) of this section;
- (C) The inspection provision of paragraph (d) of this section; and
- (D) The notification-of-noncompliance provisions of paragraph (e) of this section.

(ii) *Order and form.* A monitoring procedure will meet the requirements of section 42 (m)(1)(B)(iii) if it contains the substance of these provisions. The particular order and form of the provisions in the allocation plan is not material. A monitoring procedure may contain additional provisions or requirements.

(iii) [Reserved]. For further guidance, see §1.42-5T(a)(2)(iii).

(b) *Recordkeeping and record retention provisions*—(1) *Recordkeeping provision.* Under the recordkeeping provision, the owner of a low-income housing project must be required to keep records for each qualified low-income building in the project that show for each year in the compliance period—

(i) The total number of residential rental units in the building (including the number of bedrooms and the size in square feet of each residential rental unit);

(ii) The percentage of residential rental units in the building that are low-income units;

(iii) The rent charged on each residential rental unit in the building (including any utility allowances);

(iv) The number of occupants in each low-income unit, but only if rent is determined by the number of occupants in each unit under section 42(g)(2) (as in effect before the amendments made by the Omnibus Budget Reconciliation Act of 1989);

(v) The low-income unit vacancies in the building and information that shows when, and to whom, the next available units were rented;

(vi) The annual income certification of each low-income tenant per unit. For an exception to this requirement, see section 42(g)(8)(B) (which provides a special rule for a 100 percent low-income building);

(vii) Documentation to support each low-income tenant's income certification (for example, a copy of the tenant's federal income tax return, Forms W-2, or verifications of income from third parties such as employers or state agencies paying unemployment compensation). For an exception to this requirement, see section 42(g)(8)(B) (which provides a special rule for a 100 percent low-income building). Tenant income is calculated in a manner consistent with the determination of annual income under section 8 of the United States Housing Act of 1937 (“Section 8”), not in accordance with the determination of gross income for federal income tax liability. In the case of a tenant receiving housing assistance payments under Section 8, the documentation requirement of this

paragraph (b)(1)(vii) is satisfied if the public housing authority provides a statement to the building owner declaring that the tenant's income does not exceed the applicable income limit under section 42 (g);

(viii) The eligible basis and qualified basis of the building at the end of the first year of the credit period; and

(ix) The character and use of the nonresidential portion of the building included in the building's eligible basis under section 42 (d) (e.g., tenant facilities that are available on a comparable basis to all tenants and for which no separate fee is charged for use of the facilities, or facilities reasonably required by the project).

(2) *Record retention provision.* Under the record retention provision, the owner of a low-income housing project must be required to retain the records described in paragraph (b)(1) of this section for at least 6 years after the due date (with extensions) for filing the federal income tax return for that year. The records for the first year of the credit period, however, must be retained for at least 6 years beyond the due date (with extensions) for filing the federal income tax return for the last year of the compliance period of the building.

(3) *Inspection record retention provision.* Under the inspection record retention provision, the owner of a low-income housing project must be required to retain the original local health, safety, or building code violation reports or notices that were issued by the State or local government unit (as described in paragraph (c)(1)(vi) of this section) for the Agency's inspection under paragraph (d) of this section. Retention of the original violation reports or notices is not required once the Agency reviews the violation reports or notices and completes its inspection, unless the violation remains uncorrected.

(c) *Certification and review provisions—(1) Certification.* Under the certification provision, the owner of a low-income housing project must be required to certify at least annually to the Agency that, for the preceding 12-month period—

(i) The project met the requirements of:

(A) The 20-50 test under section 42 (g)(1)(A), the 40-60 test under section 42 (g)(1)(B), or the 25-60 test under sections 42 (g)(4) and 142 (d)(6) for New York City, whichever minimum set-aside test was applicable to the project; and

(B) If applicable to the project, the 15-40 test under sections 42(g)(4) and 142 (d)(4)(B) for “deep rent skewed” projects;

(ii) There was no change in the applicable fraction (as defined in section 42(c)(1)(B)) of any building in the project, or that there was a change, and a description of the change;

(iii) The owner has received an annual income certification from each low-income tenant, and documentation to support that certification; or, in the case of a tenant receiving Section 8 housing assistance payments, the statement from a public housing authority described in paragraph (b)(1)(vii) of this section. For an exception to this requirement, see section 42(g)(8)(B) (which provides a special rule for a 100 percent low-income building);

(iv) Each low-income unit in the project was rent-restricted under section 42(g)(2);

(v) All units in the project were for use by the general public (as defined in §1.42-9), including the requirement that no finding of discrimination under the Fair Housing Act, 42 U.S.C. 3601-3619, occurred for the project. A finding of discrimination includes an adverse final decision by the Secretary of the Department of Housing and Urban Development (HUD), 24 CFR 180.680, an adverse final decision by a substantially equivalent state or local fair housing agency, 42 U.S.C. 3616a(a)(1), or an adverse judgment from a federal court;

(vi) The buildings and low-income units in the project were suitable for occupancy, taking into account local health, safety, and building codes (or other habitability standards), and the State or local government unit responsible for making local health, safety, or building code inspections did not issue a violation report for any building or low-income unit in the project. If a violation report or notice was issued by the governmental unit, the owner must attach a statement summarizing the violation report or notice or a copy of the violation report or notice to the annual certification submitted to the Agency under paragraph (c)(1) of this section. In addition, the owner must state whether the violation has been corrected;

(vii) There was no change in the eligible basis (as defined in section 42(d)) of any building in the project, or if

there was a change, the nature of the change (e.g., a common area has become commercial space, or a fee is now charged for a tenant facility formerly provided without charge);

(viii) All tenant facilities included in the eligible basis under section 42(d) of any building in the project, such as swimming pools, other recreational facilities, and parking areas, were provided on a comparable basis without charge to all tenants in the building;

(ix) If a low-income unit in the project became vacant during the year, that reasonable attempts were or are being made to rent that unit or the next available unit of comparable or smaller size to tenants having a qualifying income before any units in the project were or will be rented to tenants not having a qualifying income;

(x) If the income of tenants of a low-income unit in the building increased above the limit allowed in section 42(g)(2)(D)(ii), the next available unit of comparable or smaller size in the building was or will be rented to tenants having a qualifying income;

(xi) An extended low-income housing commitment as described in section 42(h)(6) was in effect (for buildings subject to section 7108(c)(1) of the Omnibus Budget Reconciliation Act of 1989, 103 Stat. 2106, 2308-2311), including the requirement under section 42(h)(6)(B)(iv) that an owner cannot refuse to lease a unit in the project to an applicant because the applicant holds a voucher or certificate of eligibility under section 8 of the United States Housing Act of 1937, 42 U.S.C. 1437f (for buildings subject to section 13142(b)(4) of the Omnibus Budget Reconciliation Act of 1993, 107 Stat. 312, 438-439); and

(xii) All low-income units in the project were used on a nontransient basis (except for transitional housing for the homeless provided under section 42(i)(3)(B)(iii) or single-room-occupancy units rented on a month-by-month basis under section 42(i)(3)(B)(iv)).

(2) *Review.* The review provision must—

(i) Require that the Agency review the certifications submitted under paragraph (c)(1) of this section for compliance with the requirements of section 42;

(ii) [Reserved]. For further guidance, see §1.42-5T(c)(2)(ii).

(iii) [Reserved]. For further guidance, see §1.42-5T(c)(2)(iii).

(3) [Reserved]. For further guidance, see §1.42-5T(c)(3).

(4) *Exception for certain buildings—(i) In general.* The review requirements under paragraph (c)(2)(ii) of this section may provide that owners are not required to submit, and the Agency is not required to review, the tenant income certifications, supporting documentation, and rent records for buildings financed by the Rural Housing Service (RHS), formerly known as Farmers Home Administration, under the section 515 program, or buildings of which 50 percent or more of the aggregate basis (taking into account the building and the land) is financed with the proceeds of obligations the interest on which is exempt from tax under section 103 (tax-exempt bonds). In order for a monitoring procedure to except these buildings, the Agency must meet the requirements of paragraph (c)(4)(ii) of this section.

(ii) *Agreement and review.* The Agency must enter into an agreement with the RHS or tax-exempt bond issuer. Under the agreement, the RHS or tax-exempt bond issuer must agree to provide information concerning the income and rent of the tenants in the building to the Agency. The Agency may assume the accuracy of the information provided by RHS or the tax-exempt bond issuer without verification. The Agency must review the information and determine that the income limitation and rent restriction of section 42 (g)(1) and (2) are met. However, if the information provided by the RHS or tax-exempt bond issuer is not sufficient for the Agency to make this determination, the Agency must request the necessary additional income or rent information from the owner of the buildings. For example, because RHS determines tenant eligibility based on its definition of “adjusted annual income,” rather than “annual income” as defined under Section 8, the Agency may have to calculate the tenant's income for section 42 purposes and may need to request additional income information from the owner.

(iii) *Example.* The exception permitted under paragraph (c)(4)(i) and (ii) of this section is illustrated by the following example.

Example. An Agency selects for review buildings financed by the RHS. The Agency has entered into an agreement described in paragraph (c)(4)(ii) of this section with the RHS with respect to those buildings. In reviewing the RHS-financed buildings, the Agency obtains the tenant income and rent information from the RHS for 20 percent of the low-income units in each of those buildings. The Agency calculates the tenant income and rent to determine whether the tenants meet the income and rent limitation of section 42 (g)(1) and (2). In order to make this determination, the Agency may need to request additional income or rent information from the owners of the RHS buildings if the information provided by the RHS is not sufficient.

(5) *Agency reports of compliance monitoring activities.* The Agency must report its compliance monitoring activities annually on Form 8610, "Annual Low-Income Housing Credit Agencies Report."

(d) *Inspection provision—(1) In general.* Under the inspection provision, the Agency must have the right to perform an on-site inspection of any low-income housing project at least through the end of the compliance period of the buildings in the project. The inspection provision of this paragraph (d) is a separate requirement from any tenant file review under paragraph (c)(2)(ii) of this section.

(2) *Inspection standard.* For the on-site inspections of buildings and low-income units required by paragraph (c)(2)(ii) of this section, the Agency must review any local health, safety, or building code violations reports or notices retained by the owner under paragraph (b)(3) of this section and must determine—

(i) Whether the buildings and units are suitable for occupancy, taking into account local health, safety, and building codes (or other habitability standards); or

(ii) Whether the buildings and units satisfy, as determined by the Agency, the uniform physical condition standards for public housing established by HUD (24 CFR 5.703). The HUD physical condition standards do not supersede or preempt local health, safety, and building codes. A low-income housing project under section 42 must continue to satisfy these codes and, if the Agency becomes aware of any violation of these codes, the Agency must report the violation to the Service. However, provided the Agency determines by inspection that the HUD standards are met, the Agency is not required under this paragraph (d)(2)(ii) to determine by inspection whether the project meets local health, safety, and building codes.

(3) *Exception from inspection provision.* An Agency is not required to inspect a building under this paragraph (d) if the building is financed by the RHS under the section 515 program, the RHS inspects the building (under 7 CFR part 1930), and the RHS and Agency enter into a memorandum of understanding, or other similar arrangement, under which the RHS agrees to notify the Agency of the inspection results.

(4) *Delegation.* An Agency may delegate inspection under this paragraph (d) to an Authorized Delegate retained under paragraph (f) of this section. Such Authorized Delegate, which may include HUD or a HUD-approved inspector, must notify the Agency of the inspection results.

(e) *Notification-of-noncompliance provision—(1) In general.* Under the notification-of-noncompliance provisions, the Agency must be required to give the notice described in paragraph (e)(2) of this section to the owner of a low-income housing project and the notice described in paragraph (e)(3) of this section to the Service.

(2) *Notice to owner.* The Agency must be required to provide prompt written notice to the owner of a low-income housing project if the Agency does not receive the certification described in paragraph (c)(1) of this section, or does not receive or is not permitted to inspect the tenant income certifications, supporting documentation, and rent records described in paragraph (c)(2)(ii) of this section, or discovers by inspection, review, or in some other manner, that the project is not in compliance with the provisions of section 42.

(3) *Notice to Internal Revenue Service—(i) In general.* The Agency must be required to file Form 8823, "Low-Income Housing Credit Agencies Report of Noncompliance," with the Service no later than 45 days after the end of the correction period (as described in paragraph (e)(4) of this section, including extensions permitted under that paragraph) and no earlier than the end of the correction period, whether or not the noncompliance or failure to certify is corrected. The Agency must explain on Form 8823 the nature of the noncompliance or failure to certify and indicate whether the owner has corrected the noncompliance or failure to certify. Any change in either the applicable fraction or eligible basis under paragraph (c)(1)(ii) and (vii) of this section, respectively, that results in a decrease in the qualified basis of the project under section 42 (c)(1)(A) is noncompliance that must be reported to the Service under this paragraph (e)(3). If an Agency reports on Form 8823 that a building is entirely out of compliance and will not be in compliance at any time in the future, the Agency need not file Form 8823 in subsequent years to report that building's noncompliance. If the noncompliance or failure to certify is corrected within 3 years after the end of the correction period, the Agency is required to file Form 8823 with the Service

reporting the correction of the noncompliance or failure to certify.

(ii) *Agency retention of records.* An Agency must retain records of noncompliance or failure to certify for 6 years beyond the Agency's filing of the respective Form 8823. In all other cases, the Agency must retain the certifications and records described in paragraph (c) of this section for 3 years from the end of the calendar year the Agency receives the certifications and records.

(4) *Correction period.* The correction period shall be that period specified in the monitoring procedure during which an owner must supply any missing certifications and bring the project into compliance with the provisions of section 42. The correction period is not to exceed 90 days from the date of the notice to the owner described in paragraph (e)(2) of this section. An Agency may extend the correction period for up to 6 months, but only if the Agency determines there is good cause for granting the extension.

(f) *Delegation of Authority—(1) Agencies permitted to delegate compliance monitoring functions—(i) In general.* An Agency may retain an agent or other private contractor (“Authorized Delegate”) to perform compliance monitoring. The Authorized Delegate must be unrelated to the owner of any building that the Authorized Delegate monitors. The Authorized Delegate may be delegated all of the functions of the Agency, except for the responsibility of notifying the Service under paragraphs (c)(5) and (e)(3) of this section. For example, the Authorized Delegate may be delegated the responsibility of reviewing tenant certifications and documentation under paragraph (c) (1) and (2) of this section, the right to inspect buildings and records as described in paragraph (d) of this section, and the responsibility of notifying building owners of lack of certification or noncompliance under paragraph (e)(2) of this section. The Authorized Delegate must notify the Agency of any noncompliance or failure to certify.

(ii) *Limitations.* An Agency that delegates compliance monitoring to an Authorized Delegate under paragraph (f)(1)(i) of this section must use reasonable diligence to ensure that the Authorized Delegate properly performs the delegated monitoring functions. Delegation by an Agency of compliance monitoring functions to an Authorized Delegate does not relieve the Agency of its obligation to notify the Service of any noncompliance of which the Agency becomes aware.

(2) *Agencies permitted to delegate compliance monitoring functions to another Agency.* An Agency may delegate all or some of its compliance monitoring responsibilities for a building to another Agency within the State. This delegation may include the responsibility of notifying the Service under paragraph (e)(3) of this section.

(g) *Liability.* Compliance with the requirements of section 42 is the responsibility of the owner of the building for which the credit is allowable. The Agency's obligation to monitor for compliance with the requirements of section 42 does not make the Agency liable for an owner's noncompliance.

(h) *Effective/applicability dates—(1) In general.* Allocation plans must comply with these regulations by June 30, 1993. The requirement of section 42 (m)(1)(B)(iii) that allocation plans contain a procedure for monitoring for noncompliance becomes effective on January 1, 1992, and applies to buildings for which a low-income housing credit is, or has been, allowable at any time. Thus, allocation plans must comply with section 42(m)(1)(B)(iii) prior to June 30, 1993, the effective date of these regulations. An allocation plan that complies with these regulations, with the notice of proposed rulemaking published in the FEDERAL REGISTER on December 27, 1991, or with a reasonable interpretation of section 42(m)(1)(B)(iii) will satisfy the requirements of section 42(m)(1)(B)(iii) for periods before June 30, 1993. Section 42(m)(1)(B)(iii) and these regulations do not require monitoring for whether a building or project is in compliance with the requirements of section 42 prior to January 1, 1992. However, if an Agency becomes aware of noncompliance that occurred prior to January 1, 1992, the Agency is required to notify the Service of that noncompliance. In addition, the requirements in paragraphs (b)(3) and (c)(1)(v), (vi), and (xi) of this section (involving recordkeeping and annual owner certifications) and paragraphs (c)(2)(ii)(B), (c)(2)(iii), and (d) of this section (involving tenant file reviews and physical inspections of existing projects, and the physical inspection standard) are applicable January 1, 2001. The requirement in paragraph (c)(2)(ii)(A) of this section (involving tenant file reviews and physical inspections of new projects) is applicable for buildings placed in service on or after January 1, 2001. The requirements in paragraph (c)(5) of this section (involving Agency reporting of compliance monitoring activities to the Service) and paragraph (e)(3)(i) of this section (involving Agency reporting of corrected noncompliance or failure to certify within 3 years after the end of the correction period) are applicable January 14, 2000.

(2) [Reserved]. For further guidance, see §1.42-5T(h)(2).

(i) [Reserved]. For further guidance, see §1.42-5T(i).

[T.D. 8430, 57 FR 40121, Sept. 2, 1992; 57 FR 57280, Dec. 3, 1992; 58 FR 7748, Feb. 9, 1993; T.D. 8563, 59 FR 50163, Oct. 3, 1994; T.D. 8859, 65 FR 2326, Jan. 14, 2000; 65 FR 16317, Mar. 28, 2000; T.D. 9753, 81 FR 9336, Feb. 25, 2016]

http://edocket.access.gpo.gov/cfr_2003/aprqtr/26cfr1.42-5.htm

MAINTENANCE AND OPERATING EXPENSE REVIEW

Maintenance and Operating Expense Review and Underwriting Certification
(Section A to be completed by Owner/Section B is to be signed by Lender)

Section A

NOTE: IN PROVIDING THE BELOW REQUESTED INFORMATION AND CERTIFICATION, THE LENDING INSTITUTION MUST REFERENCE AND BE AWARE OF INFORMATION CONTAINED IN THE MINNESOTA HOUSING FORM 402 PREPARED BY THE APPLICANT AND THE UNDERWRITING REQUIREMENTS CONTAINED IN THE MINNESOTA HOUSING FINANCE UNDERWRITING STANDARDS AVAILABLE ON MINNESOTA HOUSING'S WEB SITE. MINNESOTA HOUSING WILL LOOK FOR THESE STANDARDS TO BE MAINTAINED UNLESS IT HAS APPROVED ADJUSTMENTS.

Development Name _____

Development Address _____

Annual Gross Potential Rent	\$ _____
Less Vacancy Rate of ____: \$ _____	
Annual Other Income	\$ _____
Less Maintenance & Operating Expenses	
M&O Expenses per unit/year	\$ _____
Total M&O Expenses for all units/yr	\$ _____
Less Real Estate Tax	\$ _____
Less Replacement and Decorating Reserves	\$ _____
(\$300 per unit senior/\$450 per unit family & other)	
Subtotal Net Operating Income (NOI)	\$ _____
Debt Service Coverage Ratio	\$ _____

Mortgage Amount _____ Rate _____ Term _____

Fully Amortized? Yes No Insured? Yes No

Section B

We certify the above named development was underwritten utilizing the information provided in this exhibit. We are certifying that this information meets or exceeds the Minnesota Housing Underwriting Standards referenced above and reflects the pro forma structure in the applicant's 402.

(Note: If certain components of the above are not meeting with Minnesota Housing standards, the Lending Institution must provide a detailed explanation as an attachment to this form.)

Lending Institution _____

Signature _____

Print/Type _____

Title _____

Date _____

