Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

Telephone Number:

Refer Reply To:
CC::PSI:6-PLR-103259-00
Date:
Aug 31 2000

Re:

Legend

P =

X =

Y =

Z =

Building =

$a =

$b =

Dear :

Pursuant to a power of attorney on file in this office, this responds to a letter dated February 4, 2000, submitted on behalf of P requesting a ruling concerning the ability of P to take into account, for purposes of the rehabilitation credit, certain expenditures incurred by X with respect to the rehabilitation of Building.

FACTS

P is a limited liability partnership engaged in the business of owning, operating, and maintaining certain real property and improvements commonly known as Building. Building is listed on the National Register of Historic Places. X is a nonprofit corporation that is an exempt entity under section 501(c)(3) of the Internal Revenue Code. One of X's charitable purposes is to provide affordable housing through the rehabilitation of substandard buildings. X is the managing partner of P. Y is a bank and is the investor partner of P.

X purchased Building from Z on Because Building itself was in

serious disrepair, all of the purchase price was allocated to the land. X undertook the restoration of Building in two phases. The first phase was completed in , and involved the rehabilitation of the second floor into six apartments. The roof and exterior of Building were also partially restored at this time. The rehabilitation expenditures allocable to this phase of the restoration totaled $a. The apartments were rented during this phase.

The second phase of the restoration began in and involved the restoration of the first floor of Building into commercial office suites, a community conference room, and restrooms. Final renovations to the exterior of Building were completed during this phase, and the restoration of Building was completed on or about The rehabilitation expenditures allocable to this phase of the restoration totaled $b. The commercial office suites, conference room, and restrooms were not held out for rental or used by X at this time.

On , X and Y formed P. X received a capital and profits interest in P in exchange for contributing Building and assigning all of its rights and liabilities relating to the restoration to P. Y received a capital and profits interest in P in exchange for a capital contribution. After its formation P held out for rental the facilities located on the first floor of Building.

In the Secretary of the Interior (National Park Service) certified the rehabilitation of Building.

P requests a ruling that, for purposes of the rehabilitation credit, it can be treated as having incurred the rehabilitation expenditures incurred by X allocable to the restoration of the first floor and associated common elements of Building. It is represented that neither X nor any other entity will claim rehabilitation credit with respect to the rehabilitation expenditures attributable to the first floor and associated common elements.

LAW, ANALYSIS, AND CONCLUSION

Section 38(b) of the Code provides a credit against income taxes for certain business credits, including the investment credit determined under section 46.

Section 46 of the Code provides that, for purposes of section 38, the amount of the investment credit includes the rehabilitation credit.

Section 47(a)(2) of the Code provides that the rehabilitation credit for any taxable year includes an amount equal to 20% of the qualified rehabilitation expenditures with respect to any certified historic structure. Section 47(c)(3)(A) provides that the term “certified historic structure” includes any building listed on the National Register of Historic Places.

Section 47(c)(2)(A) of the Code provides that the term “qualified rehabilitation expenditures” includes amounts properly chargeable to capital account incurred for real property for which depreciation is allowable under section 168, including nonresidential real property and residential rental property, and made in connection with the rehabilitation of a qualified rehabilitated building.

Sections 47(c)(2)(B)(iv) and 47(c)(2)(C) of the Code provide that qualified rehabilitation expenditures do not include expenditures attributable to the rehabilitation of a certified historic structure unless the rehabilitation is certified by the Secretary of the Interior as being consistent with the historic character of the property.

Section 47(c)(1)(A) of the Code provides that, in the case of a certified historic structure, the term “qualified rehabilitated building” means a building that has been substantially rehabilitated, was placed in service before the beginning of the rehabilitation, and is depreciable.

Section 47(c)(1)(C) of the Code provides that, in general, a building shall be treated as having been substantially rehabilitated for a taxable year only if the qualified rehabilitation expenditures during a 24-month period selected by the taxpayer and ending with or within the taxable year exceed the greater of the adjusted basis of the building (and its structural components) or $5000.

Section 47(b) of the Code provides that qualified rehabilitation expenditures with respect to any qualified rehabilitated building shall be taken into account for the taxable year in which the qualified rehabilitated building is placed in service. Section 1.46-3(d)(1)(ii) of the Income Tax Regulations provides that for purposes of the credit allowed by section 38, property shall be considered placed in service in the taxable year in which the property is placed in a condition or state of readiness and availability for a specifically assigned function.

Section 1.48-12(c)(3)(ii) of the regulations provides that where qualified rehabilitation expenditures are incurred with respect to a building by a person other than the taxpayer and the taxpayer subsequently acquires the building, or a portion of the building, to which some or all of the expenditures are allocable, the taxpayer acquiring the property shall be treated as having incurred the rehabilitation expenditures actually incurred by the transferor provided that 1) the building, or portion of the building, acquired by the taxpayer was not used or placed in service after the rehabilitation expenditures were incurred and prior to the date of acquisition, and 2) no credit with respect to the rehabilitation expenditures is claimed by anyone other than the taxpayer who acquired the property. The regulation further provides that where a building is divided into condominium units, expenditures attributable to the common elements shall be allocable to the individual condominium units in accordance with the principles of section 1.48-12(c)(10)(ii), and that a condominium unit’s share of the common elements shall not be considered to have been used or placed in service prior to the time that the particular condominium unit is used (whether personal or business use).

Section 1.48-12(c)(10)(ii) of the regulations provides that where expenditures only partially qualify as qualified rehabilitation expenditures because a portion of the expenditures are attributable to an enlargement of a building, the expenditures must be apportioned between those portions of the building constituting the enlargement and the original building. The regulation further provides that the expenditures must be specifically allocated to the original portion of the building and the enlargement to the extent possible. If it is not possible to make a specific allocation of the expenditures, the expenditures must be allocated to each portion on some reasonable basis.

Our analysis of the present case assumes that Building qualifies as a certified historic structure, and the rehabilitation of Building as a certified rehabilitation, within the meaning of the applicable rehabilitation credit provisions under section 47 of the Code, and that the first floor of Building was not placed in service after the rehabilitation expenditures were incurred and prior to the transfer of Building to P. This letter expresses no opinion with regard to these matters. In addition, no opinion is expressed regarding 1) the allocation of the entire purchase price of Building to the land, 2) the amount of qualified rehabilitation expenditures incurred during the rehabilitation phases of Building, and 3) P's basis in Building . These matters concern facts subject to verification by the District Director.

Because the rehabilitated second floor of Building was placed in service by X prior to the time Building was transferred to P, P cannot be treated as having incurred the qualified rehabilitation expenditures incurred by X attributable to that phase of the restoration. Section 1.48-12(c)(3)(ii) of the regulations. However, the regulation contemplates situations where a taxpayer acquires a rehabilitated building, or a portion of a building, containing multiple units, some of which have already been placed in service, and indicates that the taxpayer can be treated as having incurred the rehabilitation expenditures attributable to units that have not been placed in service prior to the acquisition. The regulation also provides that expenditures for the common elements of such a building should be allocated to the individual units based on principles found in section 1.48-12(c)(10)(ii), and that a unit's share of the common elements shall not be considered placed in service prior to the time the particular unit is used.

While section 1.48-12(c)(3)(ii) of the regulations specifically mentions condominium units, the regulation's principles are equally applicable to the present situation. Here, the rehabilitated first floor of Building was not placed in service by X prior to the transfer of Building to P. The first floor and associated common elements of Building are analogous to the condominium units and associated common elements discussed in the regulation. Under section 1.48-12(c)(3)(ii) the common elements associated with the first floor of Building are not considered to be placed in service prior to the time the first floor is placed in service. In addition, it is represented that neither X nor any other entity will claim credit with respect to the rehabilitation expenditures incurred by X attributable to the first floor and associated common elements. Accordingly, based solely on the representations submitted with the ruling request and

the applicable law discussed above, we rule that P can be treated as having incurred the rehabilitation expenditures incurred by X allocable to the restoration of the first floor and associated common elements of Building, provided that the allocation of rehabilitation expenditures is made in accordance with the principles of section 1.48-12(c)(10)(ii).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of the transaction described above under any other provision of the Code. This ruling is directed only to the taxpayer on whose behalf it was requested. Section 6110(k)(3) provides that it may not be cited or used as precedent.

In accordance with the power of attorney, we are sending a copy of this letter ruling to P. We also are sending a copy of the letter ruling to the District Director of the District.

Sincerely yours,
PETER C. FRIEDMAN
Assistant Branch Chief, Branch 6
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures: 2
Copy of this letter
Copy for § 6110 purposes

cc: