Part III - Administrative, Procedural and Miscellaneous

Section 42. Low-Income Housing Credit

Notice 2009-44

PURPOSE

The purpose of this notice is to clarify that, under § 1.42-10 of the Income Tax Regulations (the utility allowance regulations), utility costs paid by a tenant based on actual consumption in a sub-metered rent-restricted unit as described herein are treated as paid directly by the tenant for purposes of § 42(g)(2)(B)(ii) of the Internal Revenue Code.

BACKGROUND

Section 42 sets forth rules for determining the amount of the low-income housing credit, which is allowed as a credit against income tax pursuant to § 38. Section 42(a) provides that the amount of the low-income housing credit determined under § 42 for any taxable year in the credit period is an amount equal to the applicable percentage of the qualified basis of each qualified low-income building. A qualified low-income building is defined in § 42(c)(2) as any building that is part of a qualified low-income housing project.

A qualified low-income housing project is defined in § 42(g)(1) as any project for residential rental property if the project meets one of the following tests elected by the taxpayer: (A) At least 20 percent of the residential units in the

project are rent-restricted and occupied by individuals whose income is 50 percent or less of area median gross income; or (B) at least 40 percent of the residential units in the project are rent-restricted and occupied by individuals whose income is 60 percent or less of area median gross income. Failure to qualify as a rent-restricted unit may result in ineligibility for the section 42 credit, reduction in the amount of the credit, and/or recapture of previously allowed credits. In order to qualify as a rent-restricted unit within the meaning of § 42(g)(2), the gross rent for the unit must not exceed 30 percent of the applicable income limitation. Section 42(g)(2)(B)(ii) provides that gross rent includes a utility allowance determined by the Secretary after taking into account the procedures under section 8 of the United States Housing Act of 1937.

Section 1.42-10, which was recently amended by Treasury decision 9420 on July 29, 2008 (73 FR 43863), sets forth the circumstances under which gross rent includes a utility allowance and provides rules for determining the applicable utility allowance. Under § 1.42-10(a), 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 a utility allowance.

If gross rent includes a utility allowance, § 1.42-10(b) provides rules for determining the applicable utility allowance depending upon whether (1) the building receives rental assistance from the Rural Housing Service (RHS) ("RHS-assisted building"), (2) the building has any tenant that receives RHS rental assistance payments ("RHS tenant assistance"), (3) the rents and utility

allowances of the building are reviewed by the Department of Housing and Urban Development (HUD) ("HUD-regulated building"), or (4) the building is not described in (1), (2), or (3) ("other building"). Section 1.42-10(b)(1) and (2) provides that, for an RHS-assisted building and a building with RHS tenant assistance, the applicable utility allowance is the applicable RHS utility allowance. Section 1.42-10(b)(3) provides that, for a HUD-regulated building, the applicable utility allowance is the applicable HUD utility allowance. With respect to other buildings, § 1.42-10(b)(4)(i) provides that, for all rent-restricted units occupied by tenants receiving HUD tenant assistance, the applicable utility allowance is the applicable Public Housing Authority (PHA) utility allowance established for the Section 8 Existing Housing Program. With respect to all other tenants in other buildings, § 1.42-10(b)(4)(ii) provides that the applicable utility allowance is the applicable PHA utility allowance under § 1.42-10(b)(4)(ii)(A), a local utility company estimate under § 1.42-10(b)(4)(ii)(B), an estimate from the State or local housing credit agency that has jurisdiction over the building under § 1.42-10(b)(4)(ii)(C), the HUD Utility Schedule Model under § 1.42-10(b)(4)(ii)(D), or an energy consumption model under § 1.42-10(b)(4)(ii)(E).

Some buildings in qualified low-income housing projects are sub-metered. Sub-metering measures tenants' actual utility consumption, and tenants pay for the utilities they use. A sub-metering system typically includes a master meter, which is owned or controlled by the utility supplying the electricity, gas, or water, with overall utility consumption billed to the building owner. In a sub-metered system, building owners (or their agents) use unit-based meters to measure

utility consumption and prepare a bill for each residential unit based on consumption. The building owners (or their agents) retain records of resident utility consumption, and tenants receive documentation of utility costs as specified in the lease.

DISCUSSION

For purposes of § 1.42-10(a) of the utility allowance regulations, utility costs paid by a tenant based on actual consumption in a sub-metered rent-restricted unit are treated as paid directly by the tenant, and not by or through the owner of the building. For RHS-assisted buildings under § 1.42-10(b)(1), buildings with RHS tenant assistance under § 1.42-10(b)(2), HUD-regulated buildings under § 1.42-10(b)(3), and rent-restricted units in other buildings occupied by tenants receiving HUD rental assistance under § 1.42-10(b)(4)(i), the applicable RHS or HUD rules apply. For all other tenants in rent-restricted units in other buildings under § 1.42-10(b)(4)(ii):

(1) The utility rates charged to tenants in each sub-metered rent-restricted unit must be limited to the utility company rates incurred by the building owners (or their agents);

(2) If building owners (or their agents) charge tenants a reasonable fee for the administrative costs of sub-metering, then the fee will not be considered gross rent under § 42(g)(2). The fee must not exceed an aggregate amount per unit of 5 dollars per month unless State law provides otherwise; and

(3) If the costs for sewerage are based on the tenants' actual water consumption determined with a sub-metering system and the sewerage costs are on a combined water and sewerage bill, then the tenants' sewerage costs are treated as paid directly by the tenants for purposes of the utility allowances regulations.

The utility allowance regulations will be amended to incorporate the guidance set forth in this notice.

EFFECTIVE DATE

This notice is effective for utility allowances subject to the effective date in § 1.42-12(a)(4). Consistent with § 1.42-12(a)(4), building owners (or their agents) may rely on this notice for any utility allowances effective no earlier than the first day of the building owner's taxable year beginning on or after July 29, 2008.

REQUEST FOR COMMENTS

The Treasury Department and IRS invite taxpayers to submit written comments on issues relating to this notice. Send comments to: CC:PA:LPD:PR (Notice 2009-44), Room 5205, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (Notice 2009-44), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC. Submissions may also be sent electronically via the Internet to the following e-mail address: Notice.comments@irscounsel.treas.gov. Include the notice number (Notice

2009-44) in the subject line. Comments must be received on or before July 27, 2009. All comments will be available for public inspection and copying.

DRAFTING INFORMATION

The principal author of this notice is David Selig, Office of the Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, please contact Mr. Selig at (202) 622-3040 (not a toll-free call).