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DEPARTMENT OF THE TREASURY

Internal Revenue Service

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Compliance Monitoring and Miscellaneous Issues Relating to the Low-Income Housing Credit

AGENCY: Internal Revenue Service (IRS), Treasury.

**Background**

On March 28, 1997, the General Accounting Office (GAO) submitted a report to Congress, "Tax Credits: Opportunities to Improve Oversight of the Low-Income Housing Program," (GAO/GGD/RCED-97-55), recommending certain revisions to existing Agency procedures for compliance with the low-income housing credit and requirements under qualified allocation plans for verifying taxpayers' sources and uses of funds for low-income housing projects. Consistent with these proposals, the proposed regulations amend existing regulation §1.42-5 to require Agencies: (i) to report annually their compliance monitoring activities to the IRS; (ii) to conduct on-site habitability inspections of low-income housing projects; and (iii) to review local government reports on building code violations. In addition, the proposed regulations provide that qualified allocation plans require taxpayers to submit independent verification on sources and uses of funds for low-income projects.

The proposed regulations also contain amendments to the Income Tax Regulations (26 CFR part 1) including §1.42-6 (carryover allocations), §1.42-11

(provision of services), §1.42-12 (effective dates and transitional rules), and §1.42-13 (correction of administrative errors and omissions) that are issued under the authority granted by section 42(n).

## **Explanation of Provisions**

### Compliance Monitoring

Section 42(m)(1)(B)(iii) provides that an allocation plan is not qualified unless it contains a procedure that the Agency (or an agent of, or private contractor hired by, the Agency) will follow in monitoring compliance with the provisions of section 42. The Agency is to notify the IRS of any noncompliance of which the Agency becomes aware.

Section 42(m)(1)(B)(iii) is effective on January 1, 1992, and applies to all buildings for which the low-income housing credit determined under section 42 is, or has been, allowable at any time. Allocation plans must have complied with the requirements of §1.42-5 by June 30, 1993. Section 42(m)(1)(B)(iii) and §1.42-5 do not require monitoring for whether a low-income housing 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 IRS of that noncompliance.

The current compliance monitoring regulations require an Agency, at a minimum, to review tenant income certifications and rent charges of projects using one of the following three monitoring options: (1) review the owners' annual income certifications, including the documentation supporting the certifications for at least 50 percent of the Agency's low-income projects, and tenant rent records in at least 20 percent of the

low-income units in these projects; (2) make annual on-site inspections of at least 20 percent of the projects, and review the low-income certification, the documentation supporting the certification, and rent record for each tenant in at least 20 percent of the low-income units in those projects; or (3) obtain from all project owners tenant income and rent records for each low-income unit and, for at least 20 percent of the projects, review the annual tenant income certification, backup income documentation, and rent record for each low-income tenant in at least 20 percent of the low-income units in those projects.

The GAO report recommended that an Agency conduct regular on-site inspections of projects and obtain building code inspection reports performed by the local government unit. The GAO found that desk audits (monitoring options 1 and 3 above) failed to detect violations involving the physical condition of buildings. In addition, site visits allow an Agency to directly assess the compliance status of projects and the physical condition of buildings. Consistent with these proposals, the proposed regulations remove the three monitoring options and require, at least once every three (3) years, that each Agency conduct on-site inspections of all buildings in each low-income housing project and, for each tenant in at least 20 percent of the project's low-income units selected by the Agency, review the low-income certification, the documentation supporting such certification, and the rent record. The proposed regulations also require, at a minimum, by the end of the calendar year following the year the last building in a project is placed in service, that the Agency conduct on-site inspections of the projects and review the low-income certification, the documentation

supporting such certification, and the rent record for each tenant in the project. As part of the inspection requirements, the proposed regulations also require the Agency to determine whether the project is suitable for occupancy, taking into account local health, safety, and building codes. Agencies may delegate this determination only to a state or local government unit responsible for making building code inspections. The three-year inspection requirement is proposed to be effective on the date the final regulations are published in the **Federal Register**. The placed-in-service year inspection requirement is proposed to be effective for buildings placed in service on or after the date the final regulations are published in the **Federal Register**.

The current compliance monitoring regulations require the owner of a project, at a minimum, to certify annually that for the preceding 12-month period each building in the project was suitable for occupancy, taking into account local health, safety, and building codes. Based on the GAO recommendation, the proposed regulations revise this certification by also requiring the owner of the project to certify that for the preceding 12-month period the state or local government unit responsible for making building code inspections did not issue a report of a violation for the project. If the governmental unit issued a report of a violation, the owner will be required to attach a copy of the report of the violation to the annual certification submitted to the Agency.

The proposed regulations also adopt the GAO recommendation that Agencies report annually to the IRS on compliance monitoring activities. It is anticipated Form 8610, "Annual Low-Income Housing Credit Agencies Report," will be revised to require an Agency to confirm annually that it has satisfied the new compliance

monitoring requirements involving: (1) the once every three-year on-site inspections and review of the low-income certification, the documentation supporting such certification, and the rent record for each tenant in at least 20 percent of the low-income units selected by the Agency; and (2) the on-site inspections relating to the placed-in-service year and review of the low-income certification, the documentation supporting such certification, and the rent record for each low-income tenant in the project.

The current compliance monitoring regulations require Agencies to report a correction of noncompliance or failure to certify if the correction occurs within the correction period defined in §1.42-5(e)(4). The proposed regulations clarify that the Agency is required to file Form 8823, "Low-Income Housing Credit Agencies Report of Noncompliance," with the IRS reporting the correction of the noncompliance or failure to certify regardless of when the correction occurs during the compliance period. This requirement is proposed to be effective on the date the final regulations are published in the **Federal Register**.