NYC Finance

June 11, 2009

RE: Ruling Request

Real Property Transfer Tax
FLR: 094895-021

Dear Ms.

This letter responds to your request, received April 30, 2009, on behalf of --- (the "Taxpayer"), for a ruling regarding the application of the New York City Real Property Transfer Tax (the "RPTT") to the proposed transfer of interests in a low-income housing development, as described below. This office received additional information concerning this request on May 8, 13, 14, 28, and June 2, 2009.

FACTS

The facts presented are as follows:

The Taxpayer. The Taxpayer, a New York not-for-profit corporation, was formed by the ------------------ Housing Development Fund Corporation (the "Sponsor") in April 2009, under the New York State Not-for-Profit Corporation Law and Article XI of the New York State Private Financing Law. The Taxpayer's Certificate of Incorporation provides that the Taxpayer is "organized exclusively for the purpose of owning, constructing, rehabilitating, leasing, managing, equipping, maintaining, developing and operating a housing project for persons of low income" and that "[a]ll income and earnings of the [Taxpayer] will be used exclusively for corporate purposes." It also provides that "[n]o part of its assets, income or profits shall be distributed or inure to the benefit of any private individual or individuals, provided that nothing shall prevent the [Taxpayer] from paying reasonable compensation for services rendered to or for the [Taxpayer] in furtherance of one or more of its purposes." In addition, it provides that, in the event of a dissolution, any assets remaining in the Taxpayer after satisfying its liabilities must be distributed to organizations qualifying under section 501(c)(3) of the Internal Revenue Code (the "IRC") and that the Taxpayer is not authorized to carry on propaganda or otherwise attempt to influence legislation.

The Sponsor, a New York not-for-profit corporation exempt from federal income tax under IRC section 501(c), is the sole member of the Taxpayer. The directors of the Taxpayer are directors of the Sponsor.

The Taxpayer intends to apply for a determination from the Internal Revenue Service (the "IRS") that it is exempt from federal income taxation, and its Certificate of Incorporation provides that it will not engage in any activities not permitted to be carried on by a corporation that is exempt from federal income taxation.

The Taxpayer proposes to acquire a limited partner interest in ----------------, Redevelopment Associates L.P., a District of Columbia limited partnership (the “Partnership”). The Partnership owns and operates a low-income housing project (the “Project”).

The Project. The Project, located on at --- (the “Property”), had previously been owned by New York City. The Project is composed of 35 residential units and one superintendent’s unit. The Sponsor and New York City, acting through its Department of Housing Preservation and Development (“HPD”), undertook to develop the Property for use as affordable housing for people of low-income. To finance the development of the Project, the HPD provided a loan that was secured by a mortgage to the Property (the “Mortgage”), and it was decided to use federal low income housing tax credits under IRC section 42.

Because private investors are necessary to take advantage of the federal low-income housing tax credits, the Sponsor set up the Partnership as a limited partnership on November 14, 1989. On December 1, 1989, the Partnership was amended. A business corporation formed and wholly owned by the Sponsor, ---., became the general partner, (the “General Partner”), with a 1.0 percent interest in the Partnership, and -------------------------- Housing Organization, Inc., became a Special Limited Partner (the “Special Limited Partner”), with a 0.01 percent interest (the “Special Limited Partnership Interest”). The Partnership included four limited partners as investors (the “Investor Limited Partners”) to take advantage of the federal low-income housing credits: -------------, with a 33 percent investor interest (the “Investor Limited Partnership Interest”), ----------., with a 33 percent Investor Limited Partnership Interest, --------------, with a 16.495 percent Investor Limited Partnership Interest, and ---------------------------- with a 16.495 percent Investor Limited Partnership Interest (collectively, the “Investor Limited Partnership Interests”). The Partnership’s net ordinary profits and losses are allocated to the percentages-in-interest held by the General Partner, the Special Limited Partner, and Investor Limited Partners.

In addition, as part of the Program, the Partnership entered into a regulatory agreement, dated February 14, 1989 (the “Regulatory Agreement”), with HPD, under which federal low-income housing tax credits were allocated to the proposed project. The Regulatory Agreement, among other things, provides restrictions on tenants to ensure that it is occupied by low-income tenants; currently 100 percent of the units must be rented to homeless persons referred by HPD or another referral source acceptable to HPD. In addition, the Regulatory Agreement sets out a marketing plan (the “Marketing Plan”) that the Partnership must follow to insure that the selection of occupants complies with the Regulatory Plan.

The Regulatory Agreement is currently effective through the later of: (i) the period any part of the Mortgage remains unpaid; (ii) the 15 year period provided under federal income tax law for the Project to receive low income housing tax credits allocated to it by HPD; (iii) the period any exemption or abatement from taxation of the Property continues to remain in effect under section 11-243 of the New York City Administrative Code (the "Code"); or (iv) 30 years.

By deed dated February 14, 1989, the Partnership acquired the Property from the City and has owned and operated the Project under as affordable housing since that time. The Taxpayer has represented that the units continue to be occupied in accordance with the terms of the Regulatory Agreement. There has been no change in the partners in the Partnership.

The Proposed Transaction. Under the agreements with HPD, after 15 years the Sponsor or its designee has an option to acquire the Project at a preferential price. As the Project has operated for over 15 years, the Sponsor, set up the Taxpayer to do so.

You have proposed that the Taxpayer would acquire the Investor Limited Partnership Interests. Following that proposed acquisition, there would be no private investors in the Project. It is also proposed that, at a later time, the Taxpayer would acquire the Special Limited Partnership Interest. It is anticipated that in the future, the Taxpayer would be the sole owner of the Project.

As part of the proposed transaction, the Taxpayer would assume the obligations of the Regulatory Agreement. The Regulatory Agreement would be amended to extend for an additional 15 years. As amended, the Regulatory Agreement would require that all units must be leased to tenants whose annual household income does not exceed “60% of AMI.” The Agreement defines “60% of AMI” to mean “120% of the income levels as modified by household size for 50 percent of median income families (a.k.a. ‘very low-income families’).” In addition, the Regulatory Agreement, as amended, would require that 30 percent of units be provided to homeless families.

The Partnership has entered into an agreement (the “Management Agreement”) with -------------------------------- (the “Manager”), an entity formed and wholly-owned by the Sponsor. Under the Management Agreement, the Manager’s responsibilities include leasing the units, selecting the tenants, collecting the rents, enforcing the leases, repairing and maintaining the Project, ensuring utilities and other services are available in the Project, arranging for necessary on-site personnel, and keeping books and records. In addition, the Management Agreement includes detailed leasing guidelines to ensure that The Manager complies with the Regulatory Agreement in selecting tenants for the Project.

As compensation for its management services, the Manager would receive a designated percent of the rents collected from the Project. You have represented that because all the profits of the Manager are disbursed to the Sponsor, “no part of the net income, net earnings or assets of the Manager will inure to the benefit or profit of any private shareholder, firm, corporation, association or individual (except that reasonable compensation may be paid for services rendered to or for the Manager), and no private shareholder, firm, corporation, association or individual will be entitled to share in the distribution of any assets on dissolution of the Manager.”

The Project is and would continue to be exempt from real property taxes under section 420-c of the Real Property Tax Law.

By letter dated May 28, 2009, HPD has consented to transfer of the Investor Limited Partnership Interests and the Special Limited Partnership Interest to the Taxpayer according to the terms of the proposed transaction.

ISSUE

You have requested a ruling that the RPTT will not be imposed upon the proposed transfer of the Investor Limited Partnership Interests and the Special Limited Partnership Interest (collectively, the “Limited Partnership Interests”) to the Taxpayer as a transfer of a controlling economic interest to an exempt entity under Code section 11-2106(b)(2).

CONCLUSION

Based upon the facts presented and the representations submitted, we conclude that the RPTT will not be imposed upon the proposed transfer of the Limited Partnership Interests to the Taxpayer by reason of Code section 11-2106(b)(2). Thus, the conveyance will be exempt from the RPTT. However, the Taxpayer will be required to inform this office in the event that its application for exemption under IRC section 501(c)(3) is denied.

DISCUSSION

The RPTT applies to the delivery of every deed conveying an interest in real property located in New York City where the consideration for the deed exceeds $ 25,000. The RPTT also applies to every transaction whereby a controlling economic interest in real property located in New York City is transferred if the consideration exceeds $ 25,000. Code § 11-2102.

A controlling economic interest in real property includes a 50 percent interest in the capital, profits, or beneficial interests of a partnership owning directly or indirectly an interest in real property in New York City. Related transfers of economic interests are aggregated in determining whether a controlling interest is transferred. 19 RCNY § 23-02, "Controlling Interest," ¶ (2). Because the Partnership owns the Property and the Limited Partnership Interests to be transferred in the aggregate amount to a 99 percent interest in the Partnership, a controlling economic interest is being transferred. As a result, the proposed transfer of the Limited Partnership Interests would be subject to the RPTT unless it is otherwise exempt.

<u>Code section 11-2106(b) exemption</u>. Code section 11-2106(b) exempts certain deeds, instruments, and transactions from the RPTT. When that section applies, both the grantor and the grantee are exempt. Code section 11-2106(b) (2) exempts conveyances of real property by or to any corporation:

> organized and operated exclusively for religious, charitable, or educational purposes, ... and no part of the net earnings of which inures to the benefit of any private shareholder or individual and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation; provided, however, that nothing in this paragraph shall include an organization operated for the primary purpose of carrying on a trade or business for profit, whether or not all of its profits are payable to one or more organizations described in this paragraph ....

Applying that provision to the facts presented, The Taxpayer's Certificate of Incorporation provides that the Taxpayer is "organized exclusively for the purpose of owning, constructing, rehabilitating, leasing, managing, equipping, maintaining, developing and operating a housing project for persons of low income" and that "[a]ll income and earnings of the [Taxpayer] will be used exclusively for corporate purposes." It also provides that "[n]o part of its assets, income or profits shall be distributed or inure to the benefit of any private individual or individuals, provided that nothing shall prevent the [Taxpayer] from paying reasonable compensation for services rendered to or for the [Taxpayer] in furtherance of one or more of its purposes." In addition, it provides that, in the event of a dissolution, any assets remaining in the Taxpayer after satisfying its liabilities must be distributed to organizations qualifying under section 501(c)(3) of the Internal Revenue Code (the "IRC") and that the Taxpayer is not authorized to carry on propaganda or otherwise attempt to influence legislation.

In addition, to be exempt under Code section 11-2106, the Taxpayer must be organized and operated exclusively for religious, charitable, or educational purposes. In this case, only "charitable" might apply. Thus, assuming that the Taxpayer is organized and operated for charitable purposes, Code section 11-2106(b)(2) will apply.

<u>Organized for charitable purposes</u>. Code section 11-2106(b)(2) closely resembles IRC section 501(c)(3), which exempts certain religious, charitable, and educational organizations from federal income tax. Code section 11-2106(b)(2) does not expressly require an organization to have received a federal exemption under IRC section 501(c)(3) to be exempt from the RPTT. However, because of the substantial similarity between the IRC and Code provisions, this Department will take notice of judicial and administrative interpretations of IRC section 501(c)(3) in applying Code section 11-2106(b)(2).

In Revenue Ruling 70-585, 1970-2 C.B. 115, the Internal Revenue Service (the "IRS") addressed the question of when an organization formed and operated to provide housing qualifies as "charitable." In Situation 1, the IRS considered an organization formed and operated to provide housing for low-income persons and concluded that "[b]y providing homes for low-income families who otherwise could not afford them, the organization is relieving the poor and distressed [and thus] is organized and operated exclusively for charitable purposes" under IRC section 501(c)(3). In Situation 4 of that ruling, the IRS considered an organization formed to provide rental housing at cost to moderate income families; the IRS found that organization did not provide relief to the poor or carry out any other function within the definition of "charitable."

In this case, according to its Certificate of Incorporation, the Taxpayer is “organized exclusively for the purpose of owning, constructing, rehabilitating, leasing, managing, equipping, maintaining, developing and operating a housing project for persons of low income” and that “[a]ll income and earnings of the [Taxpayer] will be used exclusively for corporate purposes.” As a result, the Taxpayer, like the Taxpayer in situation 1, is organized for the express purpose of “relieving the poor and distressed,” and meets the definition of charitable set out in Revenue Ruling 70-585.

<u>Operated for charitable purposes</u>. Under federal income tax law, “poor and distressed” beneficiaries must be needy in the sense that they cannot afford the necessities of life. <u>See, e.g.</u>, Revenue Ruling 67-138, 1967-1 C.B. 129, Revenue Ruling 70-585, 1970-2 C.B. 115, and Revenue Ruling 76-408, 1976-2 C.B. 145. In Notice 93-1, 1993-1 CB 290, the IRS established a safe-harbor guideline to distinguish low-income housing from moderate-income housing for purposes of determining whether an organization qualifies under Revenue Ruling 70-585 as engaging in charitable activities. In 1996, the IRS promulgated Revenue Procedure 96-32, 1996-1 CB 717, superseding Notice 93-1.

Section 3 of the Revenue Procedure 96-32 set out the conditions that must be satisfied for the safe harbor to apply. To meet the safe harbor, the organization must establish 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. <u>Id</u>., at .01(1)

That revenue procedure further defines “low-income” as 80 percent of the area’s median income and “very low income” as 50 percent of an area’s median income. <u>Id</u>., at .02(1).

In this case, as part of the Program, the Partnership entered into the Regulatory Agreement, which, among other things, addresses the mix of tenants at the Project. Since being entered into in 1989, the Regulatory Agreement has included provisions to ensure that the Project has been occupied by low-income residents. As amended, the Regulatory Agreement would require that all units must be leased to tenants with an annual household income that does not exceed “60% of AMI.” The Agreement defines “60% of AMI” to mean “120% of the income levels as modified by household size for 50 percent of median income families (a.k.a. ‘very low-income families’).” In addition, the Regulatory Agreement, as amended, would require that 30 percent of units be provided to homeless families.

Revenue Procedure 96-32 includes tests concerning “low-income” and “very low-income” tenants. Section 3.01(1)(a) of the procedure concerns “low-income” tenants, those with income that does not exceed 80 percent of area median income, and requires that at least 75 percent of a projects units must be occupied by low-income residents. In this case, the Regulatory Agreement requires that 100 percent of the Project’s units must be occupied by tenants with income at or below 60 percent of the area median income. As a result, over 75 percent of the units will be occupied by low-income tenants and the requirement of section 3.01(1)(a) has been meet.

Section 3.01(1)(b) of Revenue Procedure 96-32 sets out two alternative tests concerning "very-low-income" tenants, tenants with income that does not exceed 50 percent of area median income. The second test in that section requires that at least 40 percent of units be occupied by residents with incomes that do not exceed of 120 percent of the "very-low-income" limit. Because all units must be rented to tenants with annual household income does not exceed 120 percent of the 50 percent, very-low income, limit, the second test is met. In addition, because 30 percent of the units must be provided to homeless families, it seems likely that the Project would meet the alternative test, requiring that 20 percent of the units be occupied by low-income residents. As a result, the test set out in section 3.01(1)(b) of the Revenue Procedure 96-32 has been meet**.**

Revenue Procedure 96-32 also includes the following requirements that are applicable to this ruling:

- It requires the "project is actually occupied by poor and distressed residents." Id., section 3 at .01(2). You have represented that the Project, since its inception, has been occupied by low-income residents as required by the Regulatory Agreement. As a result, based on your representations, we conclude that the Project is actually occupied by poor and distressed residents.

- It requires that a Project adopt a rental policy that complies with the governmental imposed rental restrictions. Id., section 3 at .01(3). The Regulatory Agreement includes the Marketing Plan that sets out such a policy. In addition, the Management Agreement includes detailed leasing guidelines to ensure that the Manager complies with the Regulatory Agreement in selecting tenants for the Project.

- It provides even 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." Id., section 7. It further adds that the role of a private developer or management company that benefits from sales, development fees, or management contracts may constitute result in an organization failing to qualify. Id., at section 7.

  In this case, under the Management Agreement, the Manager's responsibilities include leasing the units, selecting the tenants, collecting the rents, enforcing the leases, repairing and maintaining the Project, ensuring utilities and other services are available in the Project, arranging for necessary on-site personnel, and keeping books and records. The Manager was formed by the Sponsor, a New York not-for-profit corporation exempt from federal income tax under IRC section 501(c). In addition, you have represented that because all the profits of the Manager are disbursed to the Sponsor, "no part of the net income, net earnings or assets of the Manager will inure to the benefit or profit of any private shareholder, firm, corporation, association or individual (except that reasonable compensation may be paid for services rendered to or for the Manager), and no private shareholder, firm, corporation, association or individual will be entitled to share in the distribution of any assets on dissolution of the Manager." Thus, based on the facts presented, we conclude that private interests of individuals with a financial stake in the project would not be furthered and test of section 7 of Revenue Procedure 96-32 is satisfied.

As a result, we conclude that, applying safe harbor tests of Revenue Procedure 96-32, the Project "relieves the poor and distressed," as that phrase has been used in the federal income tax law, and thus the Taxpayer is organized and operated for charitable purposes under Code section 11-2106(b)(2).

Summary. Based upon the facts presented and the representations submitted, we conclude that the RPTT will not be imposed upon proposed transfer of the Limited Partnership Interests to the Taxpayer by reason of Code section 11-2106(b)(2). Thus, the transfer would be exempt from the RPTT. However, the Taxpayer will be required to inform this office in the event that its application for exemption under IRC section 501(c)(3) is denied.

Notwithstanding the exemption hereby granted pursuant to this ruling, the Taxpayer must report the transfer on form NYC-RPT and should attach a copy of this ruling to that return.

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The Department reserves the right to verify the information submitted.

Very truly yours,

Dara Jaffee
Assistant Commissioner
Office of Legal Affairs

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