GCM 35648

ISSUE

Whether the corporation described below qualifies as a cooperative housing corporation within the meaning of Int. Rev. Code of 1954, § 216(b)(1)(B) [hereinafter cited as Code].

CONCLUSION

We concur in the position of the proposed revenue ruling that the corporation does not qualify as a cooperative housing corporation within the meaning of Code § 216(b)(1)(B), because the stockholders are not entitled to occupy for dwelling purposes an "apartment in a building " We recommend, however, that certain revisions be made in the proposed revenue ruling, including a modification of the definition of the term "apartment in a building " A copy of the revised proposed revenue ruling is attached herewith.

FACTS

The taxpayer corporation purchased for 20x dollars a single family dwelling. The corporation paid 4x dollars in cash and executed a note secured by a mortgage for the balance. Subsequent to the purchase, the corporation sold shares of its single class of outstanding stock to several individuals. The ownership of the stock entitles each stockholder to the perpetual right to use and occupy the house. Each stockholder has a private room and shares in common with the other stockholders the right to use and occupy the rest of the dwelling which includes cooking and sanitation facilities. The house has no self-contained living units. All of the gross income received by the corporation is derived from the tenant-stockholders. The operating and maintenance expenses, real estate taxes, interest, and amortization payments under the mortgage are paid by the corporation and then collected from the stockholders in proportion to the number of shares owned by each. Except upon a complete or partial liquidation, none of the stockholders of the corporation is entitled to receive any distribution other than out of the earnings and profits of the corporation.

ANALYSIS

We concur in the position taken in the proposed revenue ruling and in the rationale employed. However, we have revised the proposed revenue ruling by condensing the facts and by deleting your reference to H.R. Rep. No. 83-1337, 83rd Cong., 2d Sess. 30 (1954). While implicit in that reference are the types of dwellings covered by Code § 216, its main thrust is to indicate that the deduction for property taxes and interest has been extended to tenant-stockholders in a cooperative development of homes in addition to those in apartments. Your reference to Treas.

Reg. § 1.216-1(d)(2), has also been deleted as its language merely tracks that of Code § 216(b)(1)(B).

We also believe the wording of the second paragraph on page 4 of the proposed revenue ruling which contains the definition of the term "apartment in a building" should be modified to read:

For purposes of section 216 of the Code, the term "apartment in a building" means an independent housekeeping unit consisting of one or more rooms, which contains facilities for cooking, sleeping, and sanitation normally found in a principal residence.

The proposed modification of this paragraph brings the definition of the term "apartment" in line with the definition of "apartment" used by the Department of Housing and Urban Development.

Federal Housing Administration, United States Department of Housing and Urban Development, No. 2600, Minimum Property Standards for Multifamily Housing (1971) defines the term "apartment" the same as the term "living unit" A living unit is defined in that manual at 13 as:

... a residential unit providing complete independent living facilities for one family including permanent provisions for living, sleeping, eating, cooking, and sanitation.

We recommend the use of the HUD definition for the term "apartment in a building" not only for purposes of consistency, but because the HUD definition is the result of a comprehensive study of numerous types of housing and living accommodations. It is not an arbitrary definition, but, rather, one that was developed by experts in the housing field setting forth the minimum standards necessary for HUD programs.

In adopting this definition, however, we recognize a possible inconsistency with the definition of "dwelling unit" as used in Code § 167(k). Code § 167(k), which was part of the Tax Reform Act of 1969, was enacted to provide rehabilitated rental housing for low-income families. To accomplish this, Code § 167(k) provides an incentive to the real estate and construction industry by allowing an accelerated depreciation rate for expenditures incurred in rehabilitating this type of housing.

Proposed Treas. Reg. § 1.167(k)-3(c)(1) defined the term "dwelling unit" as a house or an apartment used to provide living accommodations in a building or structure. It went on to state that a house or an apartment will not be considered as used to provide living accommodations unless the unit contains the facilities generally found in a principal place of residence (such as kitchen and sleeping accommodations). This definition of "dwelling unit" however, was amended in the final draft of Treas. Reg. § 1.167(k)-3(c)(1) to read:

... The term "dwelling unit" means a house or apartment used to provide living accommodations in a building or structure. It is not required that the dwelling unit be occupied subject to a lease.

The deletion of the reference to a self-contained unit in the amended definition of apartment was the result of a decision by the Regulations Policy Committee to extend the scope of the type housing the term "dwelling unit" was intended to encompass under Code § 167(k)(3)(c) to include nursing homes, old age homes, and college dormitories.

These types of housing, then, were implicit additions to the terms "house" and "apartment" already covered under "dwelling unit" even though they were still susceptible to the transient unit rule under Treas. Reg. § 1.167(k)-3(c)(2).

It was noted at the time this policy decision was adopted that the Committee Reports made no reference to these types of units. In addition, these types of units were normally not occupied on a rental basis as required by Code § 167(k)(2)(B). Furthermore, a kitchen is normally found in an apartment whereas units of these types do not normally contain one.

Indeed, the statute used the term "house" not in order to allow a house containing numerous families in various separate quarters to qualify for the deductions but to limit the application of this section to the situation in which a house is rented by a single family. If the term "house" covered a multiple occupancy situation, there would have been no reason to have added the term "apartment"

Thus, it is apparent that Code § 167(k) was enacted to provide an indirect benefit to low-income families who do not need or who, by virtue of the fact that they are lessees, do not qualify for a depreciation deduction. This benefit is accomplished by directly benefiting the real estate and construction industry by providing additional deductions in the form of accelerated depreciation under Code § 167(j) or the 60 month rule under Code § 167(k)(1) on these types of rehabilitated structures.

The rationale behind Code § 216, however, is entirely different. Its purpose is to place the tenant-stockholders of a cooperative apartment in the same position as the owner of a dwelling house as far as deductions for interest and taxes are concerned. Code § 216 does not use the term "dwelling unit" but only the terms "apartment" and "house" This section, which was part of the Revenue Act of 1942, was promulgated at a time when rooming and boarding houses were predominant. Yet, there is no indication in the legislative history or in the history behind the regulations thereunder that this section was intended to apply to units which constituted anything less than a standard house or apartment. In addition, Code § 216 was not considered when the regulations under Code § 167(k) were drafted.

In addition, the rationale behind Code § 167(k) would not appear applicable to a cooperative housing corporation, because depreciation could only be deducted if the apartment were used in a trade or business or for the production of income. Thus, although the owner of a house or an apartment building could use either one as a nursing home, thereby qualifying for an accelerated

depreciation deduction, the owner of an individual apartment in a cooperative housing corporation is not likely to use his apartment as a nursing home in order to qualify for a depreciation deduction. Therefore, a limitation to a purely structural basis of the definition of the term "apartment in a building" for purposes of cooperative housing corporations under Code § 216 would not appear to be inconsistent with the rationale of not structurally limiting the definition of that term under Treas. Reg. § 1.167(k)-3(c)(1) for purposes of allowing nursing homes to be depreciated at an accelerated rate. In view of the different purposes for which these two Code sections were enacted, we do not think we create any conflict between the two sections by structurally restricting the type of unit which qualifies as an apartment in a building as defined in the proposed revenue ruling.

The judicial decisions in this area also lend support to the proposed definition of the term "apartment in a building" In Fifth Avenue Tenth Corp., 55 Misc. 2d 80, 284 N.Y.S. 2d 497 (N.Y.C. Civ. 1967), penthouse living quarters that did not contain a bathroom were held not to constitute an apartment.

In Vaughn v. Neal, 60 A. 2d 234 (D.C. Mun. App. 1948), it was held that in view of the housing regulations defining "apartments' as units that provide a separate household unit with bath and kitchen exclusively for the use of the persons occupying such units, one who had only a sleeping room with an alcove used for cooking did not occupy a self-contained "apartment"

Finally, in the instant case upon which the proposed revenue ruling is premised

*** the attorney for the taxpayers herein, stressed in a letter to the Individual Income Tax Branch that:

... there will be no individual apartments in said premises, but that all members of the corporation will have a private room and share in common with the other stockholders of the corporation the right to use and occupy the entire dwelling.

Thus, such an arrangement would not satisfy the definition of the term "apartment in a building" as set forth in the proposed revenue ruling. Accordingly, the corporation does not qualify as a cooperative housing corporation within the meaning of Code § 216(b)(1)(B).

MEADE WHITAKER

Chief Counsel

Internal Revenue Service

Attachment:

Administrative file

Proposed Revenue Ruling

Control No. 73-6-14347

INT. REV. CODE OF 1954, § 216.-DEDUCTION OF TAXES, INTEREST, AND BUSINESS DEPRECIATION BY COOPERATIVE HOUSING CORPORATION TENANT-STOCKHOLDER.

26 C.F.R. § 1.216-1: Amounts representing taxes and interest paid to cooperative housing corporation.

REV. RUL.

Advice has been requested whether, under the circumstances described below, a corporation qualifies as a "cooperative housing corporation" within the meaning of section 216(b)(1)(B) of the Internal Revenue Code of 1954.

The corporation purchased a single-family house and the land on which it was located for 20x dollars. The stockholders of the corporation are entitled to the perpetual right to use and occupy a private room in the house and to share in common with the other stockholders the rest of the dwelling which includes common cooking and sanitation facilities. None of the private rooms contains cooking or sanitation facilities.

Section 216(b)(1)(B) of the Code provides that the term "cooperative housing corporation" means a corporation each of the stockholders of which is entitled, solely by reason of his ownership of stock in the corporation, to occupy for dwelling purposes a house, or an apartment in a building, owned or leased by such corporation.

For purposes of Section 216(b)(1)(B) of the Code, the term "apartment in a building" means an independent housekeeping unit consisting of one or more rooms which contains facilities for cooking, sleeping, and sanitation normally found in a principal residence.

Since a stockholder's room in the house purchased by the corporation does not have cooking and sanitation facilities, it does not constitute an apartment in a building. Accordingly, the corporation does not qualify as a "cooperative housing corporation" within the meaning of section 216(b)(1)(B) of the Code.