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Letter Ruling 08-13: Senior Living Community Project

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October 31, 2008

You have requested a letter ruling on behalf of "A," a general contractor licensed in Massachusetts. You ask whether building materials and supplies purchased by "A," for use in the construction of a low-income housing project sponsored by a group of non-profit organizations, are exempt from the sales tax imposed under G.L. c. 64H, § 2.

I. FACTS

Your ruling request represents the facts to be as follows: On ***** "A" as general contractor and "B," a limited partnership, as owner, entered into a contract (the "Contract") pursuant to which "A" was to construct a Low Income Housing Tax Credit ("LIHTC") and HUD 202 mixed finance project commonly referred to as the ***** Senior Living Community Project (the "Project"), located in ***** Massachusetts. The charitable purpose of the Project is to construct a 99 unit affordable housing facility with supportive services for low income seniors and is subject to affordable housing covenants.

In accordance with LIHTC and HUD 202 mixed financing regulations, "B," a single purpose entity with its only asset and activity being the Project, was organized as a Massachusetts Limited Partnership, with "C" as General Partner and "D" as Limited Partner. "C" is a Massachusetts charitable corporation organized in accordance with General Laws chapter 180 whose sole member is "E," which is exempt from federal income tax under Internal Revenue Code (IRC) § 501(c)(3) and holds an ST-2 certificate issued by the Department. "D" is also a § 501(c)(3) tax exempt corporation with an ST-2. Initially, "C" held a .0001% interest in "B" and "D" held a 99.9999% interest in "B." At that time, "A" used a Form ST-5C (Contractor's Sales Tax Exempt Purchase Certificate) in connection with several subcontracts for labor and materials for the Project. In some subcontracts, "A" paid a deposit of \$100 as binding consideration. You believe that these contracts contain a conditional transfer of title provision, and thus the date of the sale is the date the contracts were signed. You refer the Department to *Continental-Hyannis Furniture Co., Inc. v. State Tax Commission*, 366 Mass. 308, 318 N.E.2d 618 (1974) to support your position.

On ***** the ownership structure of "B" underwent a conversion required for tax credit purposes. In this transaction, the interest of the General Partner "C" converted from .0001% to .0005%, the interest of the Limited Partner "D" converted from 99.999% to .005%, and a new Limited Partner, "F," owned by the non-profit tax credit syndicate, "G," received a partnership interest in "B" of 99.99%. "G" is based in Chicago, Illinois, and is a § 501(c)(4) corporation.^[1] "G" is solely owned and controlled by "H," a §501(c)(3) corporation. "H" was organized in ***** in the state of New York

as a non-profit corporation by the ***** Foundation. The charitable purpose of "H" is to help non-profit community development organizations transform distressed neighborhoods into healthy and sustainable communities by utilizing corporate, government and philanthropic resources and providing funding, policy support and technical assistance. "G" serves the mission of its owner, "H," by utilizing the Low-Income Housing Tax Credit program under the Tax Reform Act of 1986 (Section 42 of the Internal revenue Code) to help build affordable housing. "G" is not the outright owner of the Project for two reasons. First, having "G" as the investment entity segregates, shields and protects "H" from any potential liability stemming from the Project. Second, the arrangement facilitates administrative matters, such as the implementation of the syndication of tax credits, and keeps the Project separate from other "H" investments.

The tax credits were awarded to the Project through an open, competitive process governed by the Massachusetts Department of Housing and Community Development's Qualified Allocation Plan. The entity formally receiving the tax credits is the owner and developer of the Project, "B," a single purpose Massachusetts Limited Partnership. The limited partnership form of entity is one of the approved forms of entity under the Low Income Housing Tax Credit program regulations, and is used for tax credit projects as it readily allows for the admission of tax credit limited partners who invest capital in the project in exchange for an allocation of tax credits. The tax credit limited partner in the "B" limited partnership is "F," a corporation which is owned by "G." "F," without any involvement or control by "B," ultimately assigns and allocates the tax credits among a syndicate of capital investors who support the development of affordable housing. You state that this is a common structure and mechanism for utilizing Low Income Housing Tax Credits under the Internal Revenue Code.

II. RULINGS REQUESTED

1. Are the building materials and supplies used in the construction of the Project *prior* to the conversion of ownership of the Project on ***** exempt from the sales tax imposed under G.L. c. 64H, § 2?
2. Are the building materials and supplies used in the construction of the Project exempt from the sales tax imposed under G.L. c. 64H, § 2 where subcontracts and purchase orders were executed together with consideration *prior* to the ***** ownership conversion but were paid for in full after (the conversion date)?
3. Are the building materials and supplies used in the construction of the Project *after* the conversion of ownership of the Project on ***** exempt from the sales tax imposed under G.L. c. 64H, § 2?
4. For periods to which the sales tax exemption applies, does the exemption extend to use taxes due on building materials and supplies brought into the Commonwealth?

III. RULINGS

1. The building materials and supplies used in the construction of the Project are exempt from the sales tax imposed under G.L. c. 64H, § 2 prior to the conversion of the ownership of the Project on *****.
2. The building materials and supplies purchased under subcontracts and purchase orders that were executed together with consideration prior to (the conversion date), but paid for in full after (the conversion date), are subject to the sales tax imposed under G.L. c. 64H, § 2.
3. After the conversion of ownership on ***** , the building materials and supplies used in the construction of the Project are subject to the sales tax imposed under G.L. c. 64H, § 2 and the exemption in G.L. c. 64H, § 6(f) does not apply.
4. Where applicable, the G.L. c. 64H, § 6(f) sales tax exemption extends to use taxes due on building materials and supplies purchased outside of the Commonwealth and brought into the state.

IV. DISCUSSION

Generally, sales of tangible personal property and certain services are subject to the sales tax under G.L. c. 64H, § 2. However, purchases of building materials and supplies may be exempt from the sales tax if they are to be used in the construction, reconstruction, alteration, remodeling or repair of any building or structure owned by or held in trust for the benefit of any corporation, foundation, organization or institution described in chapter 64H, § 6(e) and used exclusively in the conduct of its religious, scientific, charitable or educational purposes. G.L. c. 64H, § 6(f).

For the exemption to apply, the statute requires that the building or structure be “owned by or held in trust for a non-profit § 501(c)(3) entity as described in G.L. c. 64H, § 6(e).” In Letter Ruling 87-16, the Department ruled that sales tax was due on materials and supplies used in the rehabilitation of two public housing developments for a local housing authority under a so-called “turnkey project.”

The exemption provided under G.L. c. 64H, § 6(f) did not apply to the materials and supplies purchased by the contractor because the property being rehabilitated was not owned by or held in trust for the public entity during the construction period. *Also see Northgate Construction Co., Inc. v. State Tax Commission*, 377 Mass. 205 (1979).

However, in a differently structured transaction, the Department ruled that the G.L. c. 64H, § 6(f) exemption applied in Letter Ruling 01-13.^[2] That case involved a non-profit § 501(c)(3) corporation that was formed for the construction, development, operation and sale of affordable housing within the Commonwealth of Massachusetts. The non-profit formed several entities for the purpose of acquiring and constructing the project. The result was that an LLC and Limited Partnership were tenants in common as to the project through the vehicle of a nominee trust. The non-profit § 501(c)(3) corporation was the sole member of the LLC, which was a disregarded entity for federal and state income tax purposes. The Limited Partnership was a Massachusetts Limited Partnership with a corporate general partner and a corporate limited partner, both wholly owned by the non-profit § 501(c)(3) corporation. The Realty Trust was formed as a “nominee trust” and did not pay tax. The beneficial interests in the trust were owned solely by the LLC and the Limited Partnership, which were solely owned by the non-profit § 501(c)(3) corporation. The Commissioner ruled that since the building materials and supplies were used exclusively in the conduct of the non-profit § 501(c)(3) corporation’s charitable purposes, and since during the entire construction project the property was “owned by or held in trust for” that non-profit, the purchase of building materials and supplies was exempt from the sales tax under G.L. c. 64H, § 6(f).

In the present case, the charitable purpose of the Project is to provide affordable housing and supportive services to low income senior citizens. The Department rules that the G.L. c. 64H, § 6(f) exemption applied to “A”’s purchases made between ***** and ***** because each entity with an ownership interest in the Project during this time period was a non-profit as defined under § 501(c)(3) of the Code except for “C,” which was a chapter 180 non-profit corporation whose sole member was “E,” a § 501(c)(3) corporation. The purpose of the chapter 180 corporation was to involve a non-tax exempt entity in accordance with the requirements for a mixed-finance project under the HUD 202 program. The chapter 180 corporation was formed to facilitate the § 501(c)(3)’s charitable mission and served no other purpose.

The second ruling request raises the issue as to when the sale took place for certain contracts and subcontracts that were executed with consideration prior to the conversion, but paid in full with actual delivery of the building materials after the date of conversion. You state that the contracts contain a conditional transfer of title provision, and thus the date of the sale is the date the contracts were signed. Although you have not supplied the contracts themselves, based on these facts, there was not an actual transfer of title or possession prior to the conversion. The situation you describe is not a “conditional sale contract,” defined in *Black’s Law Dictionary* as a “(f)orm of sales contract in which seller reserves title until buyer pays for goods, at which time, the condition being fulfilled, title passes to buyer. Such contract under Uniform Commercial Code is a purchase money security agreement.” *Also see* LR 83-18 discussing conditional sales in general and LR 80-31, distinguishing a conditional sale from a lease (note that in both rulings actual possession had passed to the purchaser/lessee.) Your reliance on *Continental-Hyannis Furniture Co., Inc. v. State Tax Commission* is also misplaced. That case involved a credit sale of furniture, which was in the purchaser’s possession when the purchaser later defaulted on the payments, and the vendor’s duty to report credit sales on an accrual rather than cash basis.

After the ownership conversion on ***** , the Project owners include non-qualifying entities that are either for profit or are not tax-exempt under § 501(c)(3) of the Code. General Laws c. 64H, § 6(f)(2) specifically states that the sales tax exemption applies to sales of building materials and supplies to be used in the construction of any building or structure owned by or held in trust for the benefit of any corporation, foundation, organization or institution, which is exempt from taxation under § 501(c)(3) of the Code, as described in G.L. c. 64H, § 6(e). After the conversion of ownership, "F," its assigns^[3] and its sole owner "G," a § 501(c)(4) entity, became part owners of the Project. Therefore, the Department rules that upon conversion of ownership of the Project, purchases of materials and supplies for its construction were no longer exempt from sales tax under G.L. c. 64H, § 6(f)(2). Accordingly, "A"'s Form ST-5C which was obtained under the prior ownership arrangement is no longer valid for purchases of materials and supplies for construction of the Project.

G.L. c. 64I, § 2 provides that the use tax applies to tangible personal property or services purchased from any vendor "or manufactured, fabricated or assembled from materials acquired either within or outside the commonwealth" for storage, use, or other consumption within the Commonwealth." See TIR 04-26, Section V. G.L. c. 64I, § 7(b) exempts from the use tax sales exempt from the taxes imposed under the sales tax, c. 64H. The use tax, therefore, would only apply to materials and supplies brought into Massachusetts during periods when the sales tax exemption was not available, *i.e.*, after the date of the ownership conversion.

IV. CONCLUSION

The Department rules that the sales tax exemption afforded under G.L. c. 64H, § 6(f) applies to the purchases of materials and supplies for the Project prior to the ownership conversion on ***** , as well as to materials and supplies brought into Massachusetts before (the conversion date) on which use tax was due. The statutory requirements in G.L. c. 64H, § 6(f) must be met at the time of the actual transfer of title or possession of the construction materials in order to obtain the sales tax exemption. Finally, the Department rules that after the ownership conversion took place, the Project failed to qualify for the sales tax exemption under G.L. c. 64H, § 6(f) because, as part of the tax credit syndication process, ownership interests were sold to tax credit limited partners and, at that point, the Project was no longer wholly owned by or held in trust for 501(c)(3) organizations as required by statute.

Very truly yours,

/s/Navjeet K. Bal

Navjeet K. Bal
Commissioner of Revenue

NKB:MTF:wm

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^[1]A § 501(c)(4) organization is a civic league or organization exempt from federal income taxes if it is not organized or operated for profit, it is operated exclusively for the promotion of social welfare and its net earnings are devoted exclusively to charitable, educational, or recreational purposes. IRC § 501(c)(4). An organization will be considered to be operated exclusively for the promotion of social welfare if it is primarily engaged in promoting the common good and general welfare of the community.

^[2] Also see Letter Ruling 08-9 where the Department allowed the sales tax exemption afforded under G.L. c. 64H, § 6(f) with respect to materials and supplies purchased for the construction of a hospital building that was held in the form of a Business Trust for the benefit of two § 501(c)(3) entities.

[3] "G" designated its subsidiary "F" as the tax credit limited partner and syndicating entity. "F" assigns and allocates the tax credits among a syndicate of capital investors that support the development of affordable housing. Tax credit limited partners are taxpayers who invest equity capital in the Project in exchange for an allocation of tax credits that they use to reduce their tax liability.