Transition Relief for Certain Partnerships and Other Pass-Thru Entities Under Section 470

Notice 2005–29

PURPOSE

This notice provides transition relief under § 470 of the Internal Revenue Code to partnerships and other pass-thru entities that are treated as holding tax-exempt use property as a result of the application of § 168(h)(6).

BACKGROUND

Section 848 of the American Jobs Creation Act of 2004, Pub. L. No. 108–357, 118 Stat. 1418, 1602 (the Act), which was enacted on October 22, 2004, creates new limitations on the deductibility of losses relating to tax-exempt use property through the enactment of § 470.

With limited exceptions, § 470(a) provides that a "tax-exempt use loss" for any taxable year is not allowed. Under § 470(c)(1), the term "tax exempt use loss" means, with respect to any taxable year, the amount (if any) by which the sum of the aggregate deductions (other than interest) directly allocable to tax-exempt use property, plus the aggregate deductions for interest properly allocable to the property, exceed the aggregate income from the property. Under § 470(b), any disallowed loss is treated as a deduction with respect to the property in the next taxable year.

Under § 470(c)(2), "tax-exempt use property" has the meaning provided under § 168(h) (with certain modifications). As a general rule, under § 168(h), property is treated as "tax-exempt use property" if it is leased to a "tax-exempt entity."

Under § 168(h)(2), "tax-exempt entity" includes organizations exempt from income tax under the Code and certain foreign persons and entities that are not subject to income tax under the Code with respect to the property.

Under § 168(h)(6), if any property that is not otherwise "tax-exempt use property" under § 168(h) is owned by a partnership that has both a tax-exempt entity and a person who is not a tax-exempt entity as partners, and any allocation to the tax-exempt entity of partnership items is not a qualified allocation, an amount equal to the tax-exempt entity's proportionate share of the property generally is treated as tax-exempt use property.

Under § 168(h)(6)(B), an allocation to a tax-exempt entity is a qualified allocation if the allocation (1) is consistent with the allocation to the entity of the same distributive share of each item of income, gain, loss, deduction, credit and basis throughout the entire period that the entity is a partner in the partnership and (2) has substantial economic effect within the meaning of § 704(b)(2).

Section 168(h)(6)(E) provides that rules similar to those applicable to partnerships in determining whether property is tax-exempt use property apply to other pass-thru entities.

Under § 470(c)(2), "tax-exempt use property" does not include property otherwise subject to § 168(h)(6) if any credit is allowable under § 42 or § 47 with respect to the property.

Section 470 generally applies to leases entered into after March 12, 2004.

It has come to the attention of the Internal Revenue Service and the Treasury Department that, with respect to partnerships and other pass-thru entities that are subject to § 470 because of § 168(h)(6), difficulties may exist in applying the provisions of § 470 with respect to taxable years beginning before January 1, 2005.

Section 470(g) provides that the Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of § 470.

TRANSITION RELIEF

In the case of partnerships and pass-thru entities described in § 168(h)(6)(E), for taxable years that begin before January 1, 2005, the Service will not apply § 470 to disallow losses associated with property that is treated as tax-exempt use property solely as a result of the application of § 168(h)(6).

REQUEST FOR COMMENTS

The Service and the Treasury Department request comments with respect to the application of § 470 when a partnership or other pass-thru entity is treated as holding tax-exempt use property because of the application of § 168(h)(6). Specifically, comments are requested regarding (1) the extent to which property held by these entities should be aggregated in determining tax-exempt use losses under § 470(a), (2) the manner in which deductions and income are allocated to a specific "property" for purposes of determining tax-exempt use loss, (3) whether tax-exempt use losses arising from property held by these entities are determined at the entity level or at the owner level, and (4) what types of entities other than partnerships should be considered pass-thru entities subject to § 470.

Comments should be submitted in writing on or before May 2, 2005, and should include a reference to Notice 2005–29. Comments may be submitted to CC:PA:LPD:PR (Notice 2005–29), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Alternatively, comments may be submitted electronically via the following e-mail address: *Notice.Comments@irscounsel.treas.gov*. Please include "Notice 2005–29" in the subject line of any electronic communications.

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 2005–29), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC 20224. All comments are available for public inspection and copying.

DRAFTING INFORMATION

For further information regarding this notice, contact John Aramburu of the Office of Associate Chief Counsel (Income Tax & Accounting) at (202) 622–4960 (not a toll-free call).