

Under 26 U.S.C. § 42(h)(6)(E)(i)(I), unlike a Foreclosure, Tax Forfeiture Does Not Allow a Low-Income-Housing-Tax-Credit Landlord to Avoid the Extended Use Period

Introduction

The Low Income Housing Tax Credit subsidized-housing program, often called “LIHTC” or “Section 42” housing, is a program created under the Internal Revenue Code, specifically IRC Section 42 (26 U.S.C. § 42).

A good summary of the program is set out in a law review by Jeanne Peterson.¹ Briefly, in return for tax credits, the developer/landlord of a LIHTC building agrees to rent to low-income occupants at rents below certain caps. The tax credits are paid out during the 15 years after the building opens to tenants. This period is the “compliance period”, during which the landlord must obey a host of section-42 rules. After the end of the 15 years, for another 15 years – the “extended use period” – the landlord must still obey many of the rules, including the most important ones -- the rent caps, no eviction except for good cause, and no discrimination against voucher-holding applicants and tenants. [26 U.S.C. § 42\(h\)\(6\)\(B\)](#); [26 U.S.C. § 42\(h\)\(6\)\(E\)\(i\)\(I\)](#); [IRS Revenue Ruling 2004-82, Q&A #5 \(Aug. 30, 2004\)](#).

In two situations, a landlord is excused from the extended-use period:

[1] No buyer is available and willing to continue to operate the building under the low-income rules as of the last day of the compliance period;² or

[2] the building is foreclosed on in good faith. Specifically, [26 U.S.C. § 42\(h\)\(6\)\(E\)\(i\)\(I\)](#) states:

¹ [Jeanne L Peterson, *The Low-Income Housing Tax Credit*, 73 MICH. BAR J. 1154 \(1994\)](#)

² [26 U.S.C. § 42\(h\)\(6\)\(E\)\(i\)\(I\)](#) states that the extended use period ends “on the last day of the [compliance] period ... the housing credit agency is unable to present during such period a qualified contract for the acquisition of the low-income portion of the building by any person who will continue to operate such portion as a qualified low-income building.”

The extended use period building shall terminate **(I)** on the date the building is acquired by foreclosure (or instrument in lieu of foreclosure) unless the Secretary determines that such acquisition is part of an arrangement with the taxpayer a purpose of which is to terminate such period

(emphasis added).

Issue

Obviously, “foreclosure” is a concern to the tenants since they will lose rent-cap, good-cause and other protections.³ An issue came up in a Virginia colleague’s practice regarding how broad is the meaning of “foreclosure”? Specifically, did it apply to a tax forfeiture under which a local government took over the building because the property taxes were delinquent?⁴

The Virginia case eventually resolved on other grounds, but in the meantime, I’d done a fair amount of research into the issue, especially looking into the legislative history of the foreclosure provision. Since this issue is likely to recur, albeit rarely, I decide to write this essay setting out my thinking and research.

Plain Meaning

IRC Section 42 includes no definition of “foreclosure” nor does the code’s definitional section, 26 U.S.C. § 7701. The Public Law that included the foreclosure provision, [P.L. 101-239](#), included no definition. None of the Treasury Regulations, Revenue Rulings or Private Letter Rulings have a definition.⁵

Thus, one must turn to dictionaries. Given the technical nature of the tax code, I think law dictionaries are a better choice than law dictionaries, but

³ Incumbent tenants do get a three-year grace period to retain their good-cause and rent-cap protections (three-year vacancy decontrol). [26 U.S.C. § 42\(h\)\(6\)\(E\)\(ii\)](#).

⁴ Examples of forfeiture of real estate for not paying property taxes include [Minn. Stat. Chapters 279-282](#) and [Code of Virginia, Title 58, Chapter 39, Article 4](#).

⁵The website <https://www.novoco.com/resource-centers/affordable-housing-tax-credits/lihtc-irs-guidance> includes an excellent compilation of these documents as well as many other LIHTC resources.

the US Supreme Court seems to have a preference for lay dictionaries when construing federal statutes. The Minnesota Supreme Court takes a more even-handed approach.⁶ In this particular case, both types of dictionaries provide the same answer.

All the Internet law dictionaries I consulted define “foreclosure” as referring only to mortgages and not to non-mortgage-related events. For example, [Merriam Webster Dictionary](#) states:

Foreclosure [means] a legal proceeding that bars or extinguishes a mortgagor's right of redeeming a mortgaged estate.

A variety of other Internet law dictionaries are all in accord.⁷

The [IRS Real Estate Property Foreclosure and Cancellation of Debt Audit Technique Guide](#), albeit a publication not related to IRC Section 42, agrees. Its Relevant Terms section states:

C.... (5) Foreclosure – A legal procedure by which mortgaged real estate property is sold by the lender in full or partial satisfaction of

⁶[United States v. Rodgers](#), 466 U.S. 475, 479 (1984) (when a word is not defined in the statute, we start with the assumption that the legislative purpose is expressed by the ordinary meaning of the words used.”); [Van Buren v. United States](#), 593 U.S. 374, 141 S. Ct. 1648, 210 L.Ed.2d 26 (2021) (“when a statute, like this one, is addressing a technical subject, a specialized meaning is to be expected” [cleaned up]”; [Cocchiarella v. Driggs](#), 884 N.W.2d 621, 624 (Minn. 2016) (“we construe technical words and phrases according to their special meaning, and other words and phrases according to their common and approved usage”)

⁷ <https://dictionary.cambridge.org/us/dictionary/english/foreclosure>

The action of taking back property that was bought with borrowed money because the money was not being paid back as formally agreed, or an example of this:

<https://www.collinsdictionary.com/us/dictionary/english/foreclosure>

Foreclosure s when someone who has lent money to a person or organization so that they can buy property takes possession of the property because the money has not been repaid.

<https://corporatefinanceinstitute.com/resources/commercial-real-estate/foreclosure/>

The process of transferring back the ownership of a home to the bank or lender after the borrower's failure to repay the home loan

the mortgage debt. For example, if the borrower fails to pay the monthly mortgage payments, the lender takes the property back and sells it to recover some or all of the debt. If proceeds from the sale fail to pay recourse debt in full, the lender may obtain a deficiency judgment in court to recover the outstanding balance. The foreclosure proceeding and whether the lender is able to obtain a deficiency judgment is determined by the law of the state where the property is located.

As to law dictionaries, Black's Law Dictionary 331 (5th ed. 1983) -- the current edition of Black's in 1989 when the foreclosure provision was added to IRC Section 42 -- gave this definition:

Foreclosure [means] To shut out, to bar, to destroy an equity of redemption. A termination of all rights of the mortgagor or his grantee in the property covered by the mortgage. The process by which a mortgagor of real or personal property, or other owner of property subject to a lien, is deprived of his interest therein. Procedure by which mortgaged property is sold on default of mortgagor in satisfaction or mortgage debt.

In common usage, refers to enforcement of lien, trust deed, or mortgage in any method provided by law.

The [Cornell law website](#) gives this definition:

Foreclosure is a catch-all term for the processes used by mortgage-holders (mortgagees) to take mortgaged property from borrowers (mortgagors who default on their mortgages). Foreclosure, like mortgages generally, is governed by the law of the place where the mortgaged item is located.

A variety of other Internet legal dictionaries agree that foreclosure involves the mortgage taking back a property from a delinquent mortgagor.⁸ Only

⁸ <https://www.usa.gov/foreclosure>

Foreclosure happens when a lender seizes and sells a property because the homeowner has not been making the required mortgage payments. Learn how you might be able to prevent it.

Black's Law Dictionary even mentions non-mortgage situations and its reference to "common usage" as including non-mortgage liens and deeds of trust is not reflected in the lay dictionaries I consulted.

In summary, dictionary definitions of "foreclosure" foreclose the idea that the word means anything other than a mortgagee taking back a property because the mortgagor is delinquent on its payments (pun intended).

Context

Sometimes, the meaning of a word can be deduced from how it appears in the same statutory section or session law. Here that approach is of no help. As stated above, outside the provision at issue, IRC Section 42 does not use

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<https://www.nolo.com/legal-encyclopedia/foreclosure-basics-terms-parties-steps-and-defenses.html>

"Foreclosure" is the legal process that allows a lender, or the subsequent loan owner, to sell your home to satisfy a mortgage debt.

<https://legal-dictionary.thefreedictionary.com/foreclosure>

Foreclosure [is] A procedure by which the holder of a mortgage—an interest in land providing security for the performance of a duty or the payment of a debt—sells the property upon the failure of the debtor to pay the mortgage debt and, thereby, terminates his or her rights in the property.

<https://dictionary.law.com/Default.aspx?selected=763>

foreclosure [is] n. the system by which a party who has loaned money secured by a mortgage or deed of trust on real property (or has an unpaid judgment), requires sale of the real property to recover the money due, unpaid interest, plus the costs of foreclosure, when the debtor fails to make payment.

the word “foreclosure” in any helpful way.⁹ Neither does the use of the word “foreclosure” elsewhere in the session law shed any light?¹⁰

Legislative History

Mitchell-Danforth Report

The legislative history of the foreclosure clause starts outside the halls of Congress. The LIHTC was created out of whole cloth as part of the 1986 Tax Reform Act. It was the first tax program directly aimed at creating subsidized housing. Unsurprisingly the program had some flaws. In response, the Democratic Majority Leader of the Senate, George Mitchell, and Republican Senator John Danforth convened a 13-member task force in May 1988 to suggest improvements. The task force had representatives of all or nearly all the stakeholders. [Tracy A. Kaye, *Sheltering Social Policy in the Tax Code: The Low-Income Housing Credit*, 38 VILL. L. REV. 871, fn.67 \(1993\)](#) (hereafter “*Sheltering Social Policy in the Tax Code*”). In January 1989, the task force released the [Report of the Mitchell-Danforth Task Force on the Low-Income Housing Tax Credit \(Jan. 1989\)](#) (hereafter “Mitchell Danforth Report”).

Most of the recommendations of the [Mitchell Danforth Report](#) were incorporated into S.980 and subsequently into the LIHTC part of P.L. 101-239. [Sheltering Social Policy in the Tax Code, fn. 71; Congressional Record, May 11, 1989, page 8977](#) (Senator Mitchell stating, “This legislation [S.980] is largely based on recommendations made by a low income housing industry task force organized by Senator DANFORTH and myself last

⁹ [26 U.S.C. §42\(d\)\(2\)\(i\)\(IV\)](#) does use the word foreclosure. It reads:

For purposes of determining under subparagraph (B)(ii) when a building was last placed in service, there shall not be taken into account any placement in service

....

(IV) by any person who acquired such building by foreclosure (or by instrument in lieu of foreclosure) of any purchase-money security interest held by such person if the requirements of subparagraph (B)(ii) are met with respect to the placement in service by such person and such building is resold within 12 months after the date such building is placed in service by such person after such foreclosure

¹⁰“Foreclosure” appears only two other places in the huge public law, [P.L. 101-239](#), and only in almost offhand and certainly irrelevant ways.

year.”); [Congressional Record, May 11, 1989, pages 9011-9012](#) (Congressman Rangel, chief sponsor of the companion bill to S.980, summarizing the bill and stating, “The bill also makes several changes in the credit program designed to improve its effectiveness. These changes are being proposed as a result of a task force of housing experts convened by Senator GEORGE MITCHELL of Maine and Senator JOHN DANFORTH of Missouri.”); [Congressional Record, May 11, 1989, pages 8985-8986](#) (Senator Danforth stating, “[T]oday Senator MITCHELL and I are introducing a bill to extend permanently and modify the low-income housing tax credit....These modifications to the low income housing tax credit are primarily based on the recommendations made by the Mitchell Danforth Task Force on the Low-Income Housing Tax Credit.”)

The foreclosure provision was a minor part of the Mitchell Danforth Report. However, the report did explain the provision as follows:

In the event the property is taken by a lender through foreclosure, the lender should be provided a means for re-negotiating the terms of the Regulatory Agreement if continued compliance is not financially viable.

[Mitchell Danforth Report at 18](#) (emphasis added).

In order to get a fuller understanding of this point, I contacted Tracy Kaye, the author of [Sheltering Social Policy in the Tax Code](#). Professor Kaye was the Tax Legislative Assistant to Senator Danforth during the relevant period. [Id. fn.*](#). I asked her about the thinking behind the foreclosure provision. She contacted a colleague and this was the reply:

Since the statute speaks of “foreclosure (or instrument in lieu of foreclosure)”, I would say the answer is no, a tax-forfeiture sale would not cause the rent and income restrictions to be terminated. This provision was included in section 42 to give lenders security for their loans and thus facilitate the ability of developers to obtain long term financing. The rationale for this exception to the 30 year use restrictions would not seem to me to apply to tax-forfeitures.

The email string is available from me upon request.

As set out above, the [Mitchell Danforth Report](#) actually did “discuss this rather obscure issue”, although not in as full a fashion as did the professors.

That said, the professors' explanation is more complete. The foreclosure provision was designed to help lenders "to give lenders security for their loans and thus facilitate the ability of developers to obtain long term financing." I.e., lenders, not property-taxing governments, were meant to be protected by the provision.

Congressional Statements

As it turned out, the foreclosure provision in S.980 remained intact during the Senate committee process. <https://www.congress.gov/bill/101st-congress/senate-bill/980>. The House committee process produced a considerably different provision, which did not have an Extended Low Income Commitment and thus no foreclosure provision.¹¹ The conference committee's report, which was adopted by both chambers and included in [P.L. 101-239](#), used the Senate version. [House Conference Report 101-386 at 528, USCANN page 734.](#)

The Senate Finance Committee's report is not helpful. It only said this about the foreclosure provision:

[I]f a building for which the credit has been allocated is acquired by foreclosure, the extend use period terminates of the date of such acquisition.

[Senate Print 101-56 at page 28.](#)

When Senator Mitchell first introduced S.980 on the Senate floor, he inserted a detailed summary of the bill into the Congressional Record. The summary briefly mentioned the foreclosure provision three times as follows:

"(II) the building is owned by such Department following its acquisition (by such Department or the mortgage loan lender) by foreclosure").

and

acquired through foreclosure by a Federal, state or local agency following at least 6 months of arrears on the mortgage"

and

¹¹[House Tax Bill, LIHTC part](#); also see [House Report 101-247](#).

First, a waiver would be possible for property in financial distress: (1) to facilitate the sale of a project whose mortgage is held by HUD; and (2) to facilitate the sale of a project which is owned by FmHA or is owned by HUD following its acquisition by HUD or the lender by foreclosure or deed in lieu of foreclosure.

[Congressional Record, May 11, 1989, pages 8980,8984.](#)

These summaries are not as helpful as the professors' comments, but they are in accord that the foreclosure provision was aimed at a "mortgage".

Conclusion

There is no one absolute indicator that tax forfeitures are not within the meaning of "acquired by foreclosure". However, all the indications of congressional intent, including the plain meaning of the statute, point to tax forfeitures as not being covered by the foreclosure provision in [26 U.S.C. § 42\(h\)\(6\)\(E\)\(i\)\(I\).](#)

Appendix

Links to Documents Not Readily Available on the Internet

[1] Report of the Mitchell-Danforth Task Force on the Low-Income Housing Tax Credit (Jan. 1989)

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/mitchell-danforth-task-force-on-the-lihtc-january-1989-good-copy.pdf>

[2] Extracts from House Report 101-247

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/house-report-101-247.pdf>

[3] Extracts from Senate Print 101-56 (committee report)

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/senate-print-101-56-1.pdf>

[4] Extracts from House Conference Report 101-386

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/house-conference-report-101-386.pdf>

[5] 1989 House Tax Bill, LIHTC Part

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/1989-house-tax-bill-lihtc-part.pdf>

[6] Extract from Joint Committee on Taxation, Description of Revenue Reconciliation Proposal: Part Two, JCX-58-89, October 3, 1989

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/jcx-58-89.pdf>

[7] Serial 101-49, Hearing Before the Subcommittee on Select Revenue Measures of the House Committee on Ways and Means, May 23, 1989, GOVDOCS Y 4.W 36:101-49 (Extracts, LIHTC testimony),

<https://birnberglegalwebsite.net/wp-content/uploads/2024/08/serial-101-49.pdf>

Links to Cited Law Reviews

[8] Jeanne L Peterson, *The Low-Income Housing Tax Credit*, 73 MICH. BAR J. 1154 (1994)

<https://homelinemn.org/wp-content/uploads/The%20Low-Income%20Housing%20Tax%20Credit%20by%20Jeanne%20Peterson.pdf>

[9] Tracy A. Kaye, *Sheltering Social Policy in the Tax Code: The Low-Income Housing Credit*, 38 VILL. L. REV. 871 (1993)

<https://digitalcommons.law.villanova.edu/vlr/vol38/iss4/1/>