Internal Revenue Service

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LEGEND:
$A =
$B =
Corporation =
Date 1 =
Month 1 =
Month 2 =
Partnership =
Plan 1 =
Plan 2 =
Target = .
X percent =
Y percent =
Year 1 =

Dear :

This letter is in response to the letter dated October 25, 2006, submitted by your authorized representative, requesting certain rulings under section 424 of the Internal Revenue Code (Code) regarding the adjustment, as the result of a particular transaction, of outstanding stock options intended to satisfy the requirements under section 422 of the Code concerning incentive stock options. The facts, as represented, are as follows.

Corporation owns approximately X percent of the common limited partnership units of Partnership. Corporation also owns preferred units of Partnership. Corporation's overall ownership interest in Partnership (both common and preferred units) is Y percent. Corporation elected to be taxed as a real estate investment trust (REIT) as defined under section 856 of the Code. Virtually all of Corporation's interests in properties and

other assets are held through Partnership. Both Corporation and Partnership have common equity securities that are required to be registered under section 12 of the Securities Exchange Act of 1934 (Exchange Act).

Options intended to qualify as incentive stock options under section 422 of the Code have been granted to employees of Corporation under Plan 1 and Plan 2. Plan 1 includes an adjustment provision under which the compensation committee of Corporation "may make such substitution or adjustment, if any, as it deems to be equitable" with respect to the number or kind of shares or other securities issued or reserved for issuance pursuant to Plan 1 and to outstanding awards in the event of any change in the outstanding shares of Corporation by reason of any share dividend or split, recapitalization, merger, consolidation, spinoff, combination or exchange of shares or other corporate change, or any distributions to common shareholders other than regular cash dividends.

Plan 2 contains a substantially identical adjustment provision except that either the compensation committee or the board of trustees of Corporation may make such substitutions or adjustments as it deems equitable in such circumstances.

For financial accounting reasons, Corporation's board of trustees approved an amendment to the adjustment provision under both Plan 1 and Plan 2. The amendment to each of the stock plans revised the language "may make such substitution or adjustment, if any, as it deems to be equitable" to read "shall make such substitution or adjustment, if any, as it deems to be equitable." Prior to the amendment, only the compensation committee had authority to make substitutions or adjustments under Plan 1. As part of the amendment of Plan 1, the adjustment provision was amended to provide that either the compensation committee or the board of trustees of Corporation has the authority to make substitutions or adjustments as it deems equitable.

During Year 1, Corporation made an investment in Target. In Month 1 of Year 1, Target sold one of its businesses and in Month 3 of Year 1 paid most of the net after-tax proceeds of the sale to Target shareholders as an extraordinary dividend. As a shareholder of Target, Corporation's share of the extraordinary dividend was $A. Corporation shared this extraordinary dividend with its own shareholders and unit holders by paying them a special dividend (the "Special Distribution") of $B per share on Date 1.

Corporation distributes a portion of its earnings to shareholders by paying four equal quarterly dividends each year. The Special Distribution is unlike the quarterly dividends because it is nonrecurring, not a part of a pattern of dividends or distributions and could not reasonably have been predicted until shortly before the Special Distribution was made. The Special Distribution is more in the nature of a return of corporate capital (through the one-time sale of a corporate asset by Target) than a payout of normal

corporate earnings (as is the case with regular quarterly dividends). Further, the Special Distribution potentially reduced or diluted the value of the option holders' interests relative to those of the shareholders who received the Special Distribution.

As a result of the Special Distribution, Corporation intends to make a proportional adjustment of outstanding options, including options intended to qualify as incentive stock options under section 422 of the Code, under both Plan 1 and Plan 2 as soon as practicable following receipt of a favorable response to its ruling request. The adjustment would apply to all options that were outstanding when the Special Distribution was paid. The options would cover the same stock before and after the contemplated adjustments.

Section 424(h)(1) of the Code provides that if the terms of any option to purchase stock are modified, extended or renewed, such modification, extension or renewal shall be considered the granting of a new option.

Section 1.424-1(e)(2) of the Income Tax Regulations (Regulations) provides that any modification, extension or renewal of the terms of an option to purchase shares is considered the granting of a new option.

Section 424(h)(3) of the Code provides that the term "modification" means any change in the terms of the option that gives the employee additional benefits under the option, but such terms shall not include a change in the terms of the option attributable to the issuance or assumption of an option under section 424(a).

Section 1.424-1(e)(4)(i) of the Regulations provides that for purposes of section 1.424-1 the term modification means any change in the terms of the option (or change in the terms of the plan pursuant to which the option was granted or in the terms of any other agreement governing the arrangement) that gives the optionee additional benefits under the option regardless of whether the optionee in fact benefits from the change in terms.

Section 424(a) of the Code provides that the term "issuing or assuming a stock option in a transaction to which section 424**(**a) applies" means a substitution of a new option for the old option, or an assumption of the old option, by an employer corporation, or a parent or subsidiary of such corporation, by reason of a corporate merger, consolidation, acquisition of property or stock, separation, reorganization or liquidation, if (1) the excess of the aggregate fair market value of the shares subject to the option immediately after the substitution or assumption over the aggregate option price of such shares is not more than the excess of the aggregate fair market value of all shares subject to the option immediately before such substitution or assumption over the aggregate option price of such shares, and (2) the new option or the assumption of the old option does not give the employee additional benefits which he did not have under the old option.

Section 1.424-1(a)(4)(i) of the Regulations provides that in order for a change in an option or issuance of a new option to qualify as a substitution or assumption, the change must occur by reason of a “corporate transaction” as defined in section 1.424-1(a)(3).

Section 1.424-1(a)(4)(ii) of the Regulations provides that generally a change in an option or issuance of a new option is considered to be by reason of a corporate transaction unless the relevant facts and circumstances demonstrate that such change or issuance is made for reasons unrelated to such corporate transaction. A change in an option or issuance of a new option will be considered to be made for reasons unrelated to a corporate transaction if there is an unreasonable delay between the corporate transaction and such change in the option or issuance of a new option or if the corporate transaction serves no substantial corporate business purpose independent of the change in options.

Section 1.424-1(a)(4)(iii) of the Regulations provides that a change in an option or issuance of a new option is by reason of a distribution or change in the terms or number of the outstanding shares of a corporation only if the option as changed, or the new option issued, is an option on the same stock as under the old option.

Section 1.424-1(a)(3)(ii) of the Regulations provides that the term corporate transaction includes a distribution (excluding an ordinary dividend or a stock split or stock dividend described in section 1.424-1(e)(4)(v)) or change in the terms of number of outstanding shares of a corporation.

Section 1.424-1(a)(5)(v) of the Regulations provides that in order for a change in an option or issuance of a new option to qualify as a substitution or assumption, the new option or assumed option must not give the optionee additional benefits that the optionee did not have under the old option.

In Rev. Rul. 71-217, 1971-1 CB 136, the terms of outstanding qualified stock options provided that the options would terminate if the granting corporation was not the survivor in any corporate merger, consolidation, reorganization or similar transaction, unless otherwise provided for in writing in connection with the transaction. The corporation later deleted this termination provision and substituted a provision providing assurances that, in the event of a designated corporate transaction, the options would be replaced by new options of comparable value or would be assumed by a successor corporation. The Service ruled that a modification occurred because the deletion of the termination provision and the addition of the favorable provision conferred upon the employee an additional benefit he did not previously have.

Unlike the options described in the ruling, the options issued under Plan 1 and Plan 2 do not terminate in the event of a corporate transaction and the amended adjustment provision does not require the continuation of options that would otherwise terminate. The compensation committee or board of trustees of Corporation retains the discretion to determine which adjustments or substitutions are equitable and is not required to make any particular adjustment or substitution. Therefore, Rev. Rul. 71-217 is distinguishable from the facts in the ruling request and the amended adjustment provision does not confer an additional benefit on employees holding options previously issued pursuant to Plan 1 or Plan 2.

Based solely on the facts presented, we rule as follows:

1. The amendment of the adjustment provisions in both Plan 1 and Plan 2 as described in this ruling will not constitute a modification, extension or renewal under section 424(h) of the Code or section 1.424-1(e) of the Regulations of outstanding options intended to qualify as incentive stock options that were granted pursuant to Plan 1 and Plan 2.

2. The adjustment of outstanding options intended to qualify as incentive stock options that were granted pursuant to Plan 1 and Plan 2 “by reason of” a “corporate transaction” (within the meaning of those terms as used in section 1.424-1(a)(3) and (4) of the Regulations) will not give optionees additional benefits under section 1.424-1(a)(5)(v) and will not otherwise constitute a modification, extension or renewal of those options under section 424(h) of the Code or section 1.424-1(e) merely because (a) the adjustment is made pursuant to the amended adjustment provision in Plan 1 or Plan 2, as applicable or (b) the original adjustment provision in each of Plan 1 and Plan 2 has been amended as described in this ruling.

3. The Special Distribution was a “corporate transaction” within the meaning of that term as used in section 1.424-1(a)(3) of the Regulations.

4. The contemplated adjustment of outstanding options intended to qualify as incentive stock options that were granted pursuant to Plan 1 and Plan 2 to reflect the Special Distribution will be treated as occurring “by reason of” a “corporate transaction” (within the meaning of those terms as used in section 1.424-1(a)(3) and (4) of the Regulations).

No opinion is expressed or implied regarding whether options granted under Plan 1 or Plan 2 satisfy the requirements of section 422 of the Code. No opinion is expressed or implied concerning the tax consequences of the proposed transactions under any other provision of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the proposed transactions that are not specifically covered by the above rulings. In particular, no opinion is expressed or implied concerning the application of section 409A of the Code to the proposed transactions.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

WILLIAM C. SCHMIDT
Senior Counsel, Executive Compensation Branch
(Employee Benefits)
(Tax Exempt & Government Entities)