Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200825034**
Release Date: 6/20/2008

Index Number: 856.04-00

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Refer Reply To:
CC:FIP:B02
PLR-150591-07
Date:
March 17, 2008

Legend:

Taxpayer =

Date 1 =

OP =

TRS =

Month 1 =

Management =

Month 2 =

Date 2 =

a =

b =

c =

Hotel A =

Hotel B =

Hotel C =

Year 1 =
d =

Hotel D =

e =

f =

Corporation A =

Date 3 =

Dear :

This is in reply to a letter dated November 6, 2007, requesting a private letter ruling on behalf of Taxpayer. Specifically, you have requested a ruling that Management qualifies as an eligible independent contractor under section 856(d)(9)(A) of the Internal Revenue Code, with respect to certain hotels owned by Taxpayer, so long as Management qualifies as an independent contractor.

Facts:

Taxpayer is a self-advised, publicly traded real estate investment trust (REIT) that elected to be treated as a REIT for its tax year ended Date 1. Taxpayer owns substantially all of its assets and conducts most of its operations through OP, a limited partnership in which Taxpayer owns substantially all of the interests. OP owns all of the stock of TRS, a taxable REIT subsidiary of Taxpayer. TRS has certain wholly-owned subsidiaries.

As of Date 2, Taxpayer and its affiliates owned approximately a hotels, which are primarily leased to TRS. TRS contracts with hotel management companies to operate the hotels under management contracts. Most of the hotels are operated by the management companies under franchise licenses or brand management agreements with national brand hotel companies. The number of hotels under management contacts with each company varies depending on factors such as the sale of hotels and the purchase of other hotels.

In Month 1, TRS entered into management agreements with Management, a hotel management company wholly-owned by Taxpayer's Chairman and Taxpayer's

President and Chief Executive Officer, to operate four hotels. In Month 2, TRS entered into management agreements with Management to operate six additional hotels. As of Date 2, Taxpayer's Chairman owned approximately b percent of Taxpayer's common stock and approximately c percent of OP. At the same time, Taxpayer's President and Chief Executive Officer also owned approximately b percent of Taxpayer's common stock and approximately c percent of OP. Taxpayer has represented that the terms of the management agreements with Management were approved by Taxpayer's independent directors and were based on customary arrangements.

In Month 1, when TRS entered into the management agreement with Management to operate the four hotels, Management and persons related to Management within the meaning of section 856(d)(9)(F) (the "Management Group") operated Hotels A, B, and C (the "Hotels") for persons unrelated to Taxpayer and TRS. Taxpayer represents that the Hotels are qualified lodging facilities within the meaning of section 856(d)(9)(D)(i) of the Code. In Month 2, when TRS entered into management agreements with Management to operate the other six hotels, the Management Group no longer operated Hotel C. The Management Group provides substantially all the management and operational functions in connection with the operation of the Hotels with its own employees. As of Date 2, the Management Group manages e hotels for Taxpayer.

The Management Group and its predecessor entities have been in the hotel management business for more than d years. Through Year 1, Management Group operated approximately d hotels for persons unrelated to Taxpayer or TRS. The decline in the number of hotels operated by the Management Group is due primarily to sales of hotel properties that were managed by the Management Group, including some acquired by Taxpayer. Management Group has continued to actively pursue hotel management contracts with parties unrelated to Taxpayer and TRS. The Management Group has recently agreed to manage Hotel D, at which it employs approximately d employees and contractors.

Law and Analysis:

To qualify as a REIT, an entity must derive at least 95 percent of its gross income from sources listed in section 856(c)(2) and at least 75 percent of its gross income from sources listed in section 856(c)(3). "Rents from real property" are among the sources listed in both of those sections.

Section 856(d)(1) defines rents from real property to include rents from interests in real property, charges for services customarily rendered in connection with the rental of real property, and rent attributable to certain leased personal property. However, section 856(d)(2)(C) excludes "impermissible tenant service income" from the definition of rents from real property. Section 1.856-4(a) of the Income Tax Regulations provides

that “rents from real property” means, generally, the gross amounts received for the use of, or the right to use, real property of the REIT.

Under section 1.856-3(g), a REIT that is a partner in a partnership is deemed to own its proportionate share of each of the assets of the partnership and to be entitled to the income of the partnership attributable to that share. For purposes of § 856, the interest of a partner in the partnership's assets is determined in accordance with the partner's capital interest in the partnership. The character of the various assets in the hands of the partnership and items of gross income of the partnership retain the same character in the hands of the partners for all purposes of section 856.

Section 856(d)(2)(B) provides, in part, that except as provided in section 856(d)(8), the term “rents from real property” does not include any amount received or accrued directly or indirectly from any person if the REIT owns, directly or indirectly - (i) in the case of any person that is a corporation, stock of such person possessing 10 percent or more of the total combined voting power of all classes of stock entitled to vote, or 10 percent or more of the total value of shares of all classes of stock of such person; or (ii) in the case of any person that is not a corporation, an interest of 10 percent or more in the assets or net profits of such person. Section 856(d)(5) provides that for purposes of section 856(d), the rules prescribed in section 318(a) apply for determining the ownership of stock, assets, or net profits of any person, except as modified by subparagraphs (A) and (B) of section 856(d)(5).

Section 856(d)(8)(B) provides that amounts paid to a REIT by a TRS shall not be excluded from “rents from real property” by reason of section 856(d)(2)(B) when a REIT leases a qualified lodging facility to a TRS, and the property is operated on behalf of the TRS by a person who is an eligible independent contractor.

Section 856(d)(9)(A) provides that the term “eligible independent contractor” means, with respect to any qualified lodging facility, any independent contractor if, at the time such contractor enters into a management agreement or similar service contract with the TRS to operate the facility, the contractor (or any related person) is actively engaged in the trade or business of operating qualified lodging facilities for any person who is not a related person with respect to the REIT or the TRS.

Section 856(d)(9)(F) provides that persons shall be treated as related to each other if such persons are treated as a single employer under subsection (a) or (b) of section 52.

Section 856(d)(9)(D)(i) generally provides that the term “qualified lodging facility” means any lodging facility unless wagering activities are conducted at or in connection with such facility by any person who is engaged in the business of accepting wagers and who is legally authorized to engage in the business at or in connection with such facility.

Although not definitive with respect to determining whether an independent contractor is “actively engaged” in the trade or business of operating qualified lodging facilities under section 856(d)(9)(A), section 1.355-3(b)(2)(iii) of the regulations is instructive in determining if that requirement is satisfied. The regulation provides that the determination of whether a trade or business is actively conducted will be made from all of the facts and circumstances. In defining “active conduct “ of a trade or business, section 1.355-3(b)(2)(iii) indicates that for a trade or business to be actively conducted, substantial management and operational activities generally must be directly carried on by the corporation itself, and such activities generally do not include the activities of others outside the corporation, including independent contractors. However, the fact that a portion of a corporation’s business activities is performed by others will not preclude the corporation from being engaged in the active conduct of a trade or business if the corporation itself directly performs active and substantial management and operational functions.

In Rev. Rul. 2001-29, 2001-1 C.B. 1348, the Service addressed the issue of whether the rental activities of a REIT satisfy the active trade or business requirement of section 355(b). In concluding that a REIT satisfies this active trade or business requirement, the ruling points to the fact that REITs may provide active and substantial management functions with respect to their properties that produce qualifying rents from real property under section 856(d).

In this case, it is represented that Management is an independent contractor within the meaning of section 856(d)(3), so the issue presented is whether it is actively engaged in the trade or business of operating qualified lodging facilities. At the time that Management and TRS entered into management contracts for Management to operate the Hotels, Management operated f lodging facilities for parties other than Taxpayer or TRS. The facts indicate that the Management Group has a history of managing or operating many hotels throughout the United States. Substantially all of the management and operational activities provided by the Management Group are conducted through employees. An attachment to the ruling request, Exhibit D, dated Date 3, includes an article that indicates Management was designated by Corporation A, a leading international hotel company, as a “Preferred Management Company” for Corporation A’s properties. Exhibit D also includes an article in which Management’s Chief Operating Officer states the company’s intent to manage several new properties in the near future.

Based upon the information submitted and representations made, the facts and circumstances indicate that the activities and business conduct of Management are sufficient for Management to be treated as being actively engaged in the trade or business of operating qualified lodging facilities. Accordingly, we conclude that Management qualifies as an eligible independent contractor under section 856(d)(9)(A) with respect to hotels it manages or operates for TRS, provided that Management

continues to qualify as an independent contractor within the meaning of section 856(d)(3).

Except as specifically ruled upon above, no opinion is expressed concerning any federal income tax consequences relating to the facts herein under any other provision of the Code. Specifically, we do not rule whether Management qualifies as an independent contractor under section 856(d)(3), whether the Hotels are qualified lodging facilities within the meaning of section 856(d)(9)(D)(i) of the Code, or whether Taxpayer otherwise qualifies as a REIT under part II of subchapter M of Chapter 1 of the Code.

This ruling is directed only to the taxpayer requesting it. Taxpayer should attach a copy of this ruling to each tax return to which it applies. Section 6110(k)(3) of the Code provides that this ruling may not be used or cited as precedent.

Sincerely,

David B.Silber
David B. Silber
Chief, Branch 2
Office of Associate Chief Counsel
(Financial Institutions & Products)