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Person To Contact:
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Date:
March 17, 2011

Legend

Taxpayer =

Targets =

Manager =
State A =
State B =
State C =
Date 1 =
Date 2 =
t =
u =
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Dear :

This is in response to your letter dated November 10, 2010, and supplemental submission dated February 7, 2011, regarding the definition of the term “qualified health care property” under section 856(e)(6)(D)(i) of the Internal Revenue Code of 1986, as amended (the “Code”) for purposes of section 856(d)(8)(B) and the qualification of Manager (defined below) as an “eligible independent contractor” under section 856(d)(9)(A). Specifically, you have requested the following rulings:

1) The Mixed-Use Communities (defined below) constitute qualified health care properties within the meaning of section 856(e)(6)(D)(i) of the Code. Thus, Taxpayer may lease the Mixed-Use Communities to a taxable REIT subsidiary (TRS) pursuant to the rules of section 856(d)(8)(B).

2) Manager will be deemed to be actively engaged in the trade or business of operating qualified health care properties within the meaning of section 856(d)(9)(A) and, therefore, will qualify as an eligible independent contactor under section 856(d)(9)(A) with respect to the health care facilities it manages or operates for the TRS.

FACTS

Taxpayer is domestic corporation that elected to be taxed as a real estate investment trust (REIT) beginning on Date 1. Taxpayer is engaged in the acquisition and ownership of hospital, skilled nursing, medical office building, and senior housing projects. Taxpayer uses an overall accrual method of accounting and the calendar year as its taxable year.

Taxpayer entered into a merger agreement with Targets whereby Taxpayer will acquire from Targets the ownership or leasehold interests in t senior housing communities. Targets currently own, lease, operate, and manage the real estate.

Taxpayer will lease properties meeting the definition of qualified health care properties under section 856(e)(6)(D)(i) to a wholly-owned TRS. In turn, the TRS will engage an eligible independent contractor to operate and manage the health care facilities. Taxpayer (and/or its wholly-owned disregarded entities) will directly engage an independent contractor to operate and manage the properties considered to be independent living facilities. The eligible independent contractor providing services to the TRS's properties and the independent contractor (Manager) providing services to Taxpayer's properties will be the same company. Taxpayer will not derive any income from nor will it have any ownership interest in the eligible independent contractor or any of its subsidiaries.

The Properties

The majority of the t senior housing communities are comprised of both independent living (IL) and assisted living (AL) residents (together, "Mixed-Use Communities"). Many of the communities also have Alzheimer (ALZ) residents who reside in separate, secure wings within the respective communities. As of Date 2, the communities to be acquired from Targets can be summarized as the following: (1) u Mixed-Use Communities comprised mostly of fully-licensed AL/ALZ communities (including both IL residents and AL/ALZ residents), some partially licensed AL/ALZ communities, and some unlicensed communities with AL/ALZ licenses pending or

licenses not required; and (2) v unlicensed IL communities (without any AL/ALZ residents) with plans for some of these communities to be licensed in the future so that they can be operated as Mixed-Use Communities.

Each Mixed-Use Community is and will continue to be operated and marketed as one integrated community with different service options and units available for AL/ALZ and IL residents. Generally, each property has an executive director, community business director, activity director, maintenance director, food service director, and numerous other employees that serve the entire community. The same activities, housekeeping, maintenance, food service, and administrative staff provide services for both IL and AL/ALZ residents and are trained to handle all residents' needs.

There are a significant number of AL residents in each Mixed-Use Community, and a significant portion of the gross income is from the AL residents. In Mixed-Use Communities with ALZ residents, the ALZ residents are assigned to separate, secure wings within each community.

Taxpayer represents that transitioning a resident from IL to AL within a Mixed-Use Community is generally a simple process. With the exception of w partially licensed Mixed-Use Communities and y fully-licensed Mixed-Use Community, each property is able to accommodate either an IL or an AL living situation in every unit. A resident previously not receiving assistance with activities of daily living (ADLs) or medication management does not need to relocate to another unit in order to begin receiving these services. Switching the resident from IL to AL is accomplished by updating the resident's service plan, providing the services outlined in the service plan and adding a monthly care charge. Despite the transition to AL, all other aspects of the resident's life remain the same, such as social activities, meal plans, and the individuals with whom the resident interacts at the community.

For the w partially licensed Mixed-Use Communities and y fully-licensed Mixed-Use Community properties, the IL and AL residents are in different buildings, units, or sections of units, but they are located on the same real estate parcel. For these communities, AL residents typically eat in dining areas separate from IL residents. However, consistent with all the other Mixed-Use Communities, these IL and AL communities are operated and marketed as one integrated community. IL and AL residents share common area facilities for front desk reception, social activities, and fitness activities. During social activities and outings, the same events are offered for both IL and AL residents.

IL residents in all Mixed-Use Communities are provided with services that are customarily provided to residents of rental housing units and are provided with additional supportive services including the following: three meals a day in a central dining location, generally shared with AL residents; housekeeping and linen services; transportation to doctors' offices, banks, and retail stores; social and recreational

activities; assistance with diet; assistance in obtaining prescription medication; and assistance with arranging physical therapy services. AL residents are provided with the same services as IL residents as well as assistance with ADLs such as bathing, dressing, toileting, ambulating, eating and continence care. Depending on specific state regulations, caregivers also assist AL residents with medical administration. AL residents receive different levels of care depending on their needs. All units have emergency call systems, and staff members are available at the facilities on a 24-hour schedule.

Mixed-Use Communities are generally licensed under the laws of the state in which the community is located. Targets have x communities with AL/ALZ residents in states where a license is not required (State A and State B). Other than these x exceptions, each state regulates items such as the scope of services that may be rendered at the community; the types of individuals that may be admitted as residents (depending on the medical/physical condition of the individual); resident policies; training required of the staff; whether nursing staff is required; and building and construction standards.

Independent Contractor

The following steps will take place prior to Taxpayer's merger with Targets:

1) The management entities (Manager) and their net assets and at least y unrelated management contract for a Mixed-Use Community will be distributed to Targets' shareholders in taxable transactions.
2) The operations of the health care facilities will be transferred to separate entities disregarded for Federal income tax purposes (Opcos). These separate entities will then be transferred to a corporation which will be owned by Taxpayer immediately after the merger. The corporation and Taxpayer will jointly elect for the corporation to be treated as a TRS of Taxpayer.
3) Opcos will enter into new management contracts with Manager. Taxpayer's property owning/leasing entities (Propcos) will enter into lease or sublease agreements with Opcos. Propcos will be disregarded entities wholly owned by Taxpayer immediately after the merger.

At the time of the merger, Manager will operate and manage the t communities to be acquired by Taxpayer and at least y unrelated Mixed-Use Community through a management contract with a third party (as described below). Furthermore, Manager will be operating qualified health care properties either (1) pursuant to x management contracts for x separate qualified health properties or (2) pursuant to y management contract for an unrelated third party and a self-managed property that Manager may lease from an unrelated third party or that Manager may own prior to closing and retain. The t communities acquired by Taxpayer will be operated and managed by Manager through new management contracts after the merger.

Pursuant to these management contracts, Manager maintains all licenses and will obtain any additional licenses to be held in the name of the applicable Opco entity that are required in connection with the services that Manager provides at the communities. Manager is also required to provide the management services in compliance with Federal, state, county, municipal and other statutes, laws, orders, regulations and ordinances affecting communities. Manager will supervise the assignment of all management and community employees among the communities.

Taxpayer and Manager will enter into a management agreement on the merger date for each of the t communities. On the merger date and the date of the management contracts with the TRS subsidiary, Opcos, Manager will be under contract to manage a third-party-owned community. Manager (through its wholly-owned disregarded and regarded subsidiaries) is and should continue to be responsible after the proposed transaction for all of the operational and management functions at this third-party-owned community. The management agreement with the third party is a contract with respect to a Mixed-Use Community in which Manager has an ownership interest.

For each of the Mixed-Use Communities (e.g., the t Mixed-Use Communities acquired by Taxpayer along with the unrelated third-party leased and managed communities), Manager provides administrative personnel (including the executive director and community business director) and supervisors who oversee the staff. Manager advises and assists in the development of policies and procedures, the preparation and submission of applications and other materials necessary to obtain the required approvals, the development and implementation of staffing partners, and the administration of all billing and collections matters. Manager recruits key administrative personnel, evaluates staffing standards, provides staff training, screens management staff, provides charting, conducts routine site visits, monitors resident mix and admissions compliance, assists residents with insurance filings and ensures compliance with all standards and legal requirements. Pursuant to agreements between Manager and the property owners, Manager assists owners in establishing policies and responsibilities and ensures compliance with patient rights, provides financial oversight, maintains and repairs the physical properties of the communities, and serves as a liaison between the communities and residents, visitors, staff, and physicians.

For the third-party leased community, Manager operates the entire community, providing all resident care, equipment and supplies, maintaining and repairing the community, ensuring compliance with regulatory and other requirements, admitting patients, collecting all resident fees and providing personnel to operate the community.

Manager is in negotiations to finalize the terms of a management contract with another unrelated party owner to manage a fully-licensed Mixed-Use Community. Manager intends to successfully close this management contract before the merger

date. Furthermore, Manager is pursuing consent to continue to lease certain Mixed-Use Communities for its own benefit and is pursuing other unrelated third party contracts and the retention of self-managed properties (owned or leased).

LAW AND ANALYSIS

Section 856(c) provides that to qualify as a REIT, a corporation must: (1) derive at least 95 percent of its gross income (excluding gross income from prohibited transactions) from sources listed in section 856(c)(2), which includes dividends, interest, rents from real property, and certain other items; and (2) derive at least 75 percent of its gross income (excluding gross income from prohibited transactions) from sources listed in section 856(c)(3), which includes rents from real property and certain other items.

Section 856(d)(2)(B) provides that the term "rents from real property" does not include, except as provided in section 856(d)(8), 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 which 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 which is not a corporation, an interest of 10 percent or more in the assets or net profits of such person.

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 or a qualified health care property to a TRS of the REIT and the property is operated on behalf of such TRS by a person who is an eligible independent contractor.

Section 856(e)(6)(D)(i) provides that the term "qualified health care property" means any real property (including interests therein), and any personal property incident to such real property, which is a health care facility, or is necessary or incidental to the use of a health care facility.

Section 856(e)(6)(D)(ii) provides that the term "health care facility" means a hospital, nursing facility, assisted living facility, congregate care facility, qualified continuing care facility (as defined in section 7872(g)(4)), or other licensed facility which extends medical or nursing or ancillary services to patients and which, immediately before the termination, expiration, default, or breach of the lease or of the mortgage secured by such facility, was operated by a provider of such services which was eligible for participation in the medicare program under title XVIII of the Social Security Act with respect to such facility.

Section 856(d)(9)(A) provides that the term "eligible independent contractor" with respect to any qualified lodging facility or qualified health care property (as defined in

section 856(e)(6)(D)(i)) means any independent contractor if, at the time such contractor enters into a management agreement or other similar service contract with the TRS to operate such qualified lodging facility or qualified health care property, such contractor (or any related person) is actively engaged in the trade or business of operating qualified lodging facilities or qualified health care properties, respectively, for any person who is not a related person with respect to the real estate investment trust or the TRS.

Section 856(d)(3)(A) provides that the term "independent contractor" means any person who does not own, directly or indirectly, more than 35 percent of the shares, or certificates of beneficial interest, in the real estate investment trust; and if such person is a corporation, not more than 35 percent of the total combined voting power of whose stock (or 35 percent of the total shares of all classes of whose stock), or, if such person is not a corporation, not more than 35 percent of the interest in whose assets or net profits is owned, directly, or indirectly, by one or more persons owning 35 percent or more of the shares or certificates of beneficial interest in the trust.

In the present case, the AL/ALZ and IL residents are located in the same building or on the same real estate parcel. All the AL units are licensed by the state in which they are located (to the extent licensing is required). When a resident requires ADLs, the resident may transition from an IL unit to an AL unit (depending on availability), which may or may not require the resident to physically move units (depending on the facility's licensing). While not all of the residents of the Mixed-Use Communities receive AL services, a significant number of units in each of the Mixed-Use Communities will be occupied as AL units. Manager (directly or indirectly through its wholly-owned subsidiaries) will be actively engaged in operating these Mixed-Use Communities for the TRS. Manager will be engaged in the operation of at least y health care property for a third party pursuant to a management contract and will pursue other management contracts. Additionally, Manager has a history of operating AL and other senior living facilities.

CONCLUSION

On the basis of the facts presented and the representations made, we conclude that the Mixed-Use Communities, as described above, will qualify as "qualified health care properties" under section 856(e)(6)(D)(i). Additionally, we conclude that Manager will be considered to be actively engaged in the trade or business of operating health care properties within the meaning of section 856(d)(9)(A) and will qualify as an "eligible independent contractor" under section 856(d)(9)(A) with respect to the health care facilities it manages or operates for the TRS.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed whether Taxpayer otherwise qualifies as a REIT under part II of subchapter M of Chapter 1 of the Code.

Furthermore, no opinion is expressed regarding the tax treatment of the merger between Taxpayer and Targets.

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.

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

Sincerely,

Jonathan D. Silver
Jonathan D. Silver
Assistant to Branch Chief, Branch 2
Office of Associate Chief Counsel
(Financial Institutions & Products)