Internal Revenue Service

Number: **201214009**
Release Date: 4/6/2012

Index Number: 856.00-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:FIP:B02
PLR-128509-11
Date:
January 03, 2012

Legend:

Taxpayer =

State A =

State B =

Year 1 =

Date 1 =

Properties =

Facilities =

Services Businesses =

Company A =

Company B =

Company C =

Lessor =

Lessee =

Nominee =

a =

b =

c =

d =

e =

Dear :

This is in reply to a letter dated July 6, 2011, and a subsequent submission, requesting rulings on behalf of Taxpayer. The requested rulings concern the treatment of a REIT and its taxable REIT subsidiary (TRS) under section 856 of the Internal Revenue Code in the circumstances described below.

Facts:

Taxpayer is a publicly held State A corporation that elected to be taxed as a real estate investment trust (REIT) for its tax year beginning Year 1. Taxpayer invests in Properties through the acquisition and development of primarily single tenant properties. In general, Taxpayer's Properties are leased under absolute-net lease terms to third party lessee/operators, and Taxpayer is not involved in the management of the properties.

On Date 1, Taxpayer acquired all of the stock of Company A as part of a merger transaction (the Merger). Prior to the Merger, Taxpayer had an approximately b% interest in Company A. As part of the Merger, Company A was merged with a transitory subsidiary of Taxpayer with Company A surviving as a wholly-owned subsidiary of Taxpayer. After the Merger, Company A is a qualified REIT subsidiary (QRS) of Taxpayer. The Merger included the acquisition by Taxpayer of Company A's Facilities. Facilities were leased to TRS in a RIDEA[1] structured transaction by Taxpayer and Company B, which was formed by nine senior executives of Company A (Management

[1] REIT Investment Diversification and Empowerment Act of 2007 which permits a REIT to lease qualified health care facilities to a TRS.

Team). Prior to the merger, Company A had spun off its Services Businesses into a new company, Company C.

Taxpayer and Management Team established a limited liability company, Lessor, to own Facilities and, through TRS, established a separate limited liability company, Lessee, to own the operations portion of the business. Company A owns approximately d percent of Lessor and TRS owns approximately d percent of Lessee. Management Team owns approximately a percent of each entity. Lessor leases Facilities to Lessee under three separate master leases. A wholly-owned subsidiary of Company C manages the Facilities as an eligible independent contractor (EIK).

TRS Investment in EIK

As part of this transaction, TRS made an equity investment in exchange for a c percent interest in Company C, the parent company of the EIK. This investment will not cause the TRS to own, directly or indirectly, securities possessing more than 35 percent of the total voting power or value of the outstanding securities of the EIK or any parent or affiliate of the EIK.

Taxpayer represents that all of the agreements between Taxpayer and the TRS and Company C and the EIK will reflect market terms and will be negotiated by the parties at arm's length. Taxpayer further represents that Company C and the EIK are separate legal entities for state law purposes and they maintain their own bank accounts, books and records. Also, Company C and the EIK have their own employees under separate control.

Interim Licensing Agreements

Immediately prior to the Merger, the license to operate a Facility was held by Nominee, a wholly-owned entity of Company A. After the Merger, Nominee became a wholly-owned entity of Taxpayer. Due to the need to process certain regulatory licenses in State B, it was not possible to immediately transfer the operating license from Nominee to the tenant that would hold the operating license for the Facility after the Merger. Therefore, Taxpayer established an interim leasing arrangement (Interim Arrangement) that will terminate once the license can be transferred to the Subtenant. The Interim Arrangement will be effective for the limited time period required to process the licenses. Under the Interim Arrangement, Lessee subleases the Facility to an entity wholly-owned by Lessee (and disregarded for federal income tax purposes) (the Subtenant). The Subtenant then sub-subleases the property (on an interim basis only) (the Sub-Sublease) to Nominee, who then enters into an interim management agreement with the EIK.

Taxpayer represents that the Interim Arrangement was entered into for the limited purpose of allowing the Facility to operate pending the issuance of a license to the Subtenant. Taxpayer expects the license to be transferred to Subtenant within e,

and represents that it will effectuate this transfer expeditiously once the required regulatory clearances are obtained. Under the terms of the Sub-Sublease, Nominee is obligated to pay over the positive net operating income received by it to the Subtenant and the Subtenant is solely responsible for any net operating losses and for maintaining insurance on the Facility and bearing any uninsured losses. Although funds flow through the Nominee to the Subtenant, the Nominee, as an economic matter, pays no rent on its own behalf and receives no payments from Taxpayer to pay rent under the Sub-Sublease.

Law and Analysis:

Section 856(c)(2) provides that at least 95 percent of a REIT's gross income must be derived from, among other sources, rents from real property.

Section 856(c)(3) provides that at least 75 percent of a REIT's gross income must be derived from, among other sources, rents from real property.

Section 856(d)(1) provides that rents from real property include (subject to exclusions provided in section 856(d)(2)): (A) rents from interests in real property; (B) charges for services customarily furnished or rendered in connection with the rental of real property, whether or not such charges are separately stated; and (C) rent attributable to personal property leased under, or in connection with, a lease of real property, but only if the rent attributable to the personal property for the taxable year does not exceed 15 percent of the total rent for the tax year attributable to both the real and personal property leased under, or in connection with, the lease.

Section 856(d)(2)(B) provides that 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: (1) in the case of a corporation, stock 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 the corporation; or (2) 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 the person.

Section 856(d)(2)(C) provides that any impermissible tenant service income is excluded from the definition of rents from real property. Section 856(d)(7)(A) defines impermissible tenant service income to mean, with respect to any real or personal property, any amount received or accrued directly or indirectly by the REIT for services furnished or rendered by the REIT to tenants at the property, or for managing or operating the property.

Section 856(d)(7)(C) provides certain exclusions from impermissible tenant service income. Section 856(d)(7)(C) provides that for purposes of section 856(d)(7)(A), services furnished or rendered, or management or operation provided, through an independent contractor from whom the REIT does not derive or receive any

income shall not be treated as furnished, rendered, or provided by the REIT, and there shall not be taken into account any amount which would be excluded from unrelated business taxable income under section 512(b)(3) if received by an organization described in section 511(a)(2).

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 qualified health care facility to a TRS, and the facility or property is operated on behalf of the TRS by a person who is an eligible independent contractor. A TRS is not considered to be operating or managing a qualified health care property solely because it possesses a license to do so.

Section 856(d)(3) defines an independent contractor as any person who does not own, directly or indirectly, more than 35 percent of the REIT's shares 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) is owned directly or indirectly, by one or more persons owning 35 percent or more of the shares of the REIT.

Section 856(d)(9)(A) provides that the term eligible independent contractor means, with respect to any qualified lodging facility or qualified health care property, 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 or property, the contractor (or any related person) is actively engaged in the trade or business of operating qualified lodging facilities or qualified health care properties for any person who is not a related person with respect to the REIT or the TRS.

Section 856(l) provides that a REIT and a corporation (other than a REIT) may treat such corporation as a TRS if the REIT directly or indirectly owns stock in the corporation, and the REIT and the corporation jointly elect such treatment.

Section 856(l)(2) provides that any corporation in which a TRS owns directly or indirectly more than 35 percent of the total voting power or value of the outstanding securities shall be treated as a TRS. Section 856(l)(3)(A) provides that a TRS cannot directly or indirectly operate or manage a lodging facility or a health care facility.

Rev. Rul. 75-136, 1975-1 C.B. 195 concerns whether a wholly-owned subsidiary of a REIT's corporate investment adviser that manages the REIT's property can qualify as an independent contractor under section 856(d)(3). In determining that the subsidiary may qualify as an independent contractor, the ruling states that it is the relationship of the entity or individual (such as an employee or trustee) to the trust itself that precludes the entity from qualifying as an independent contractor for the management of the property. A relationship between the entity or individual and the trustee, or employee, or investment adviser of the REIT would not in itself disqualify the entity, assuming the other requirements for qualification as an independent contractor

are met. Accordingly, the ruling holds that the wholly-owned subsidiary of the investment adviser is not precluded from qualifying as an independent contractor if it operates as a separate entity with its own separate officers and employees and keeps its own separate books and records that clearly reflect its activities in the management of the property.

In Rev. Rul. 73-194, 1973-1 C.B. 335, a REIT entered into a partnership with X corporation to construct and hold apartment buildings for investment. The partnership agreement provided that the partners would engage a management company to manage an apartment building. The management company was employed in an arm's length transaction and was paid a market rate for its services. X corporation was a wholly-owned subsidiary of Y corporation, which owned a substantial percentage of the stock of the management company. In concluding that the income received by the REIT from the partnership will not be disqualified as rents from real property due to the relationship between X, Y, and the management company, the ruling cites the legislative history underlying section 856(d), which states that the restrictions imposed by that section were intended to prevent income from active business operations from being included in a REIT's income. The legislative history indicates that for this requirement to be satisfied, the REIT and the independent contractor must have an arm's length relationship. See H.R. No. 2020, 86th Cong., 2d Sess.6, 1960-2 C.B. 819, 825.

In Rev. Rul. 2003-86, 2003 C.B. 290, a REIT owned all of the stock of a TRS that owned an interest in a partnership. The partnership was an independent contractor under section 856(d). The partnership provided certain noncustomary services to the REIT's tenants. Although the REIT did not directly receive payments from the independent contractor, the REIT indirectly held an equity interest in the independent contractor through its ownership of the TRS. The revenue ruling states that section 856(d)(7)(C)(i) provides an exception for services furnished or rendered through a TRS. Noting that the REIT's only interest in the independent contractor is through the TRS, the ruling states that the services provided by the independent contractor are provided by the TRS to the extent of the TRS's interest in the independent contractor. Accordingly, the ruling concludes that the REIT will not be treated as providing impermissible tenant services.

In the present case, Taxpayer's wholly-owned TRS holds an equity interest in Company C, the parent company of the EIK. Taxpayer may therefore be considered as indirectly receiving income from that equity interest. However, the income received is not derived from or dependent upon Taxpayer's relationship with the EIK. Furthermore, all of the agreements entered into by the TRS for the management or operation of the Properties are represented to be arm's length and to reflect market terms.

Taxpayer, through Nominee, holds the license to operate Facilities. However, Taxpayer merely holds the license as a nominee for the benefit of the Subtenant, an unrelated party, who acts as the lessee and who will later hold the operating license for

the Facilities. The obligations of operating the Facility and the obligations under the Sublease remain with the Subtenant. Section 856(d)(8)(B)(i) indicates that mere possession of a license should not lead to a conclusion that the REIT is operating a property. Furthermore, the foreclosure property rules with respect to health care facilities demonstrate Congress's awareness of a health care facility's need for continuity of operation. The Interim Arrangement allows the Facilities to continuously operate until the license is transferred to the Subtenant.

Accordingly, based on the information received and representations made, we conclude that: (1)TRS will not be treated as directly or indirectly operating or managing health care facilities under section 856(l)(3)(A) and, (2) rents from the health care facilities received by Taxpayer from TRS will not be treated as other than rents from real property under section 856(d) solely because TRS, directly or through Company C, acquires an equity interest in EIK, provided that such equity interest in the aggregate represents less than 35 percent of the total voting power and value of the outstanding securities of EIK or any of its affiliates.

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 Taxpayer otherwise qualifies as a REIT under part II of subchapter M of Chapter 1 of the Code. No opinion is expressed concerning the treatment of payments between Taxpayer's TRS and Taxpayer for purposes of section 857(b)(7). Also, no opinion is expressed concerning the treatment of any payment made by Nominee to the Subtenant for purposes of section 857. Furthermore, no opinion is expressed concerning whether the party represented to be an EIK satisfies the requirements under section 856(d)(9) to be treated as an EIK.

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,

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