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Date:
June 12, 2013

Legend:

Taxpayer	=
LP	=
State A	=
Year 1	=
Y Percent	=
State B	=

Dear :

This is in reply to a letter dated February 14, 2013 requesting a ruling that, pursuant to section 857(b)(6) of the Internal Revenue Code, the gain Taxpayer realizes from the sale of its assets pursuant to a plan of liquidation will not be net income derived from a prohibited transaction as defined in section 857(b)(6).

FACTS:

Taxpayer is a State A corporation that has elected to be taxed as a real estate investment trust ("REIT") under section 856(c)(1) beginning in Year 1 and for each taxable year thereafter. Through subsidiary entities that are generally taxed as disregarded entities for federal income tax purposes, Taxpayer primarily owns and leases residential real estate to third parties.

LP, a State B limited partnership, owns a Y percent interest in Taxpayer. In order to facilitate the winding down and dissolution of LP, Taxpayer intends to adopt a plan of liquidation pursuant to which it will dispose of all of its assets and liquidate.

LAW AND ANALYSIS:

Section 857(b)(6)(A) imposes a 100 percent tax on a REIT's net income from prohibited transactions. Section 857(b)(6)(B)(iii) defines the term "prohibited transaction" as the sale or other disposition of property described in section 1221(a)(1) that is not foreclosure property. Section 1221(a)(1) property, in turn, consists of "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." Section 857(b)(6)(B)(ii) provides that losses attributable to prohibited transactions are not taken into account in determining the amount of net income derived from prohibited transactions.

Section 857(b)(6)(C) excludes certain sales from the definition of a prohibited transaction. Under section 857(b)(6)(C), the term "prohibited transaction" does not include the sale of property which is a real estate asset (as defined in section 856(c)(5)(B) and which is described in section 1221(a)(1)) if --

(i) the REIT has held the property for not less than 2 years;

(ii) the aggregate expenditures made by the REIT, or any partner of the REIT, during the 2-year period preceding the date of sale that are includible in the basis of the property do not exceed 30 percent of the net selling price of the property;

(iii) (I) during the taxable year the REIT does not make more than 7 sales of property (other than sales of foreclosure property or sales to which section 1033 applies), or (II) the aggregate bases (as determined for computing earnings and profits) of property (other than sales of foreclosure property or sales to which section 1033 applies) sold during the taxable year does not exceed 10 percent of the aggregate bases of all the assets of the REIT as of the beginning of the taxable year, or (III) the fair market value of property (other than sales of foreclosure property or sales to which section 1033 applies) sold during the taxable year does not exceed 10 percent of the fair market value of all the assets of the REIT as of the beginning of the taxable year;

(iv) In the case of property, which consists of land or improvements, not acquired through foreclosure (or deed in lieu of foreclosure), or lease termination, the REIT has held the property for not less than 2 years for production of rental income; and

(v) If the requirement of clause (iii)(I) is not satisfied, substantially all of the marketing and development expenditures with respect to the property were made through an independent contractor (as defined in section 856(d)(3)) from whom the REIT itself does not derive or receive any income.

The legislative history underlying section 857(b)(6), which was added to the Code by the Tax Reform Act of 1976, indicates that the purpose of that section was to "prevent a REIT from retaining any profit from ordinary retailing activities such as sales to

customers of condominium units or subdivided lots in a development project." S. Rep. No. 938, 84th Cong., 2d Sess. 470 (1976, 1976-3 (Vol. 4) C.B. 508).

To determine whether a taxpayer holds property "primarily for sale to customers in the ordinary course of its trade or business", the Tax Court has held that several factors must be considered, none of which is dispositive. Among those factors are: (1) the nature and purpose of the acquisition of the property and the duration of the ownership; (2) the extent and nature of the taxpayer's efforts to sell the property; (3) the number, extent, continuity, and substantiality of the sales; (4) the extent of subdividing, developing, and advertising to increase sales; and (5) the time and effort the taxpayer habitually devoted to the sales. Generally, it is the purpose for which property is held at the time of the sale that is determinative, although earlier events may be considered to decide the taxpayer's purpose at the time of the sale. See Cottle v. Commissioner, 89 T.C. 467, 487 (1987).

Taxpayer has made the following representations that address its purposes with respect to the properties at issue. Taxpayer represents that it acquired the properties with the intent to own the properties for a long-term holding period and to derive its profits from capital appreciation and rental income from the properties. The disposition of the properties is pursuant to a plan of liquidation. No individual property to be disposed of has been owned for fewer than seven years. All the individual properties have been operated as rental properties for at least two years. Taxpayer will use one or more independent third party brokers from which Taxpayer derives no income to dispose of the properties.

CONCLUSION:

Based on the facts presented and representations made, we conclude that the gain recognized from the proposed sale of the properties pursuant to the plan of liquidation will not be treated as income derived from a prohibited transaction under section 857(b)(6)(B).[1]

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 with regard to whether Taxpayer qualifies as a REIT under subchapter M of the Code.

[1] Section 4 of Rev. Proc. 2013-3 sets forth those areas in which rulings or determination letters will not ordinarily be issued by the Service. "Not ordinarily" means that unique and compelling reasons must be demonstrated to justify the issuance of a ruling or determination letter. See Rev. Proc. 2013-3, sec. 2.01. Section 4.05 of Rev. Proc. 2013-3 provides that one of the areas in which rulings or determination letters will not ordinarily be issued is any matter dealing with the question of whether property is held primarily for sale to customers in the ordinary course of a trade or business. In this case, Taxpayer has demonstrated unique and compelling reasons to justify issuance of the ruling.

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

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

Sincerely,

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