DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

200311042

Date: DEC 19 2002

Contact Person:

ID Number:

UIL: 501.03-11

Telephone Number:

T:EO:B1

Employer Identification Number:

Legend:

A =
B =

Dear Sir or Madam:

This is in response to a letter from your authorized representative requesting a series of rulings on your behalf regarding the tax consequences associated with the purchase from and subsequent lease of certain real and personal property to B.

A and B are exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code and are classified as nonprivate foundations under section 509(a)(1). A and B operate hospitals.

You have stated that to improve access and better serve the needs of their respective communities, B has agreed to sell its hospital facilities and related equipment to A in order to construct a new hospital. The parties have agreed that after the sale, B will lease back its hospital facilities until the new hospital is built.

You have stated that the transaction is expected to occur in two phases. At the phase one closing, A will pay the purchase price for the transfer by B of title to the real estate, buildings and equipment (other then the delivery rooms) and will lease the property and equipment back to B pursuant to a lease. At the phase two closing, which is expected to occur no more than 5 years later, the delivery rooms, inventory, supplies and certain contracts will be assigned to A, the lease with B will be terminated and A will take operational control of the hospital facilities and equipment. Under the acquisition documents, B is required to use the leased property for the same purposes as B is currently using the property, to operate a hospital.

You have requested the following rulings in connection with the affiliations and subsequent activities and transactions described above:

1. The transactions described herein will not jeopardize the tax-exempt status of A or any of its tax-exempt affiliates under section 501(c)(3) of the Code.

2. The lease of the hospital facilities and equipment to B will not constitute the operation of an unrelated trade or business by A pursuant to sections 511 through 514 of the Code.

3. The lease of hospital facilities by A to B, pursuant to the terms of the lease, will not cause the receipt by A of unrelated debt-financed income within the meaning of section 514 of the Code.

Section 501(a) of the Code provides an exemption from federal income tax for organizations described in section 501(c)(3), including organizations that are organized and operated exclusively for charitable, educational or scientific purposes.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense.

Revenue Ruling 69-545, 1969-2 C.B. 117, acknowledges that the promotion of health is a charitable purpose within the meaning of section 501(c)(3) of the Code.

Section 511(a) of the Code imposes a tax on the unrelated business income of organizations described in section 501(c).

Section 512(a)(1) of the Code defines unrelated business taxable income as the gross income derived by an organization from any unrelated trade or business regularly carried on by it, less the allowable deductions which are directly connected with the carrying on of the trade or business, with certain modifications.

Section 513(a) of the Code defines unrelated trade or business as any trade or business the conduct of which is not substantially related (aside from the need of the organization for funds or the use it makes of the profits derived) to the exercise of the organization's exempt purposes or functions.

Section 1.513-1(d)(2) of the regulations provides, in part, that a trade or business is related to exempt purposes only where the conduct of the business activities has a causal relationship to the achievement of exempt purposes; and it is substantially

related for purposes of section 513 of the Code only if the causal relationship is a substantial one. Thus, for the conduct of trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of exempt purposes.

Section 514(a) requires unrelated business income attributable to debt-financed property to be included within the calculation of an organization's unrelated business taxable income.

The transactions described herein will not adversely affect the tax exempt status of A or any of its affiliates under section 501(c)(3) of the Code as they will continue to promote health within the meaning of Revenue Ruling 69-545. In addition, the transactions described in this letter will not result in the receipt by A of unrelated business taxable income under sections 511 through 514 of the Code because these activities will be substantially related to the accomplishment of A's exempt purposes by assuring that the community will continue to have access to critical hospital facilities while new hospital facilities are being built. The limited five year duration of the lease is consistent with the amount of time needed to construct the new hospital. Therefore, the end result will be that the community will have an additional hospital in the area with no lapse in hospital services.

Accordingly, based on all the facts and circumstances described above, we rule:

1. The transactions described herein will not jeopardize the tax-exempt status of A or any of its tax-exempt affiliates under section 501(c)(3) of the Code.

2. The lease of the hospital facilities and equipment to B will not constitute the operation of an unrelated trade or business by A pursuant to sections 511 through 514 of the Code.

3. The lease of hospital facilities by A to B, pursuant to the terms of the lease, will not cause the receipt by A of unrelated debt-financed income within the meaning of section 514 of the Code.

These rulings are based on the understanding that there will be no material changes in the facts upon which they are based.

These rulings are directed only to the organization that requested them. Section 6110(k)(3) of the Code provides that they may not be used or cited by others as precedent.

These rulings do not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described.

Please keep a copy of these rulings in your permanent records.

Sincerely,

(signed) Marvin Friedlander

Marvin Friedlander
Manager, Exempt Organizations
Technical Group 1