199901002

INTERNAL REVENUE SERVICE

SEP 2 8

NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

S.I.N. 0511.00-00
S.I.N. 0512.06-00
NO THIRD PARTY CONTACT
District Director

Taxpayer's Name: XXXXXXXXXXXXXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXXX

Taxpayer's Address: XXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXXXXXXXXXXXXX

Taxpayer's EIN: XXXXXXXXXX

Conference Held: XXXXXXXXXXXXXXXX

Legend:

Y= XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX
X= XXXXXXXXXXXXXXXXXXXXXXXXXX
Z= XXXXXXXXXXXXXXXXXXXXXXXX
t= XXXXXX
u= XXXXXX
v= XXXXXX
p= XXXXX

Issue:

1. Whether the subject organization's income from the storage of cars, boats, motorhomes, trailers, etc., during the winter months constitute unrelated business income under sections 511 and 512 of the Internal Revenue Code.

2. Whether the above constitutes the rental of real property as defined in section 512(b)(3) of the Code.

Facts:

Y was incorporated on July 18, 1945, and was recognized as exempt under section 101(6) (now section 501(c)(3)) of the Code.

Y's Articles of Incorporation state that its purpose is:

> "to promote and advance the interest of agriculture, horticulture, household arts and mechanic arts and sciences, and all kindred sciences and arts of their varied branches; and to promote and conduct agricultural, industrial, educational fairs and exhibits, and to provide entertainment and amusement therewith for the purpose of drawing the attention to

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> the public thereto, and to do and perform any and all acts authorized by law to be done by a corporation ...."

The information furnished shows that Y operates X, which is an annual fair conducted over a period of 5 or 6 days approximately 3 weeks before Labor Day. It is represented that X has a variety of activities and exhibits, including carnival rides and musical entertainment. It is represented that the exhibits are open to children who are residents of Z and who are under the age of 21.

Y's primary source of income is from fair receipts, which include gate admissions, concessions, live entertainment, exhibit fees and State funds.

The information shows that X is located on a 157 acre tract of land on which there are approximately 50 buildings. Y rents these facilities to other Code section 501(c)(3) organizations and other exempt entities during those periods between Mid-April to Mid-October when the X is not operating.

The information furnished shows that from Mid-October to Early April, Y leases out some of their buildings for the storage of cars, boats, motorhomes, trailers, etc. Each lessee signs a contract for the real property space leased. It is represented that after the building is fully leased out, the building is secured until the Spring pick-up. Further, it is represented that Y performs no services for the lessees during this time period.

For the tax years ended 9409, 9509, and 9609, the gross income received from winter storage was $t, $u, $v respectively.

For 9409 the Form 990 reflects the following:

Public support	- $ 19p
Fair Income	- $732p
Interest	- $ 3p
Summer Activity	- $135p
Winter Storage	- $ 51p

For 9509 the Form 990 reflects the following:

Public support	- $ 18p
Fair Income	- $681p
Interest	- $ 3p
Summer Activity	- $190p
Winter Storage	- $ 49p
State Grant	- $ 39p

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For 9609 the Form 990 reflects the following:

Public support - $ 16p
Fair Income - $690p
Interest - $ 2p
Summer Activity- $189p
Winter Storage - $ 58p
State Grant - $ 48p

The information furnished reflects that the Agent has concluded that none of Y's income, other than the income from Winter Storage is unrelated business taxable income. The Agent states that the summer rental of the facilities is not challenged. Further the Agent states that the services provided in connection with the summer rentals are the usual and customary services provided to similar rentals.

Finally, with respect to the winter rentals, the Agent states that the rental of space for cars, motorhomes, trailers, boats, etc, is considered analogous to the rental of spaces in parking garages, warehouses, and storage facilities. Also, it is alleged Y is competing against local storage companies. For these reasons, the Agent concludes that the income from the lease of parking spaces is not rent within the meaning of section 512(b)(3) of the Code, and thus is unrelated business taxable income.

In addition, the Agent noted that nothing was uncovered that would adversely affect Y's tax exempt status under section 501(c)(3) of the Code.

Law:

Section 501(c)(3) of the Code provides, in part, for the recognition of exemption from federal income tax of organizations that are organized and operated exclusively for charitable or educational purposes, no part of the net earnings of which inures to the benefit of any private share-holder or individual.

Section 511(a) of the Internal Revenue Code subjects organizations described in section 501(c) to a tax on their "unrelated business taxable income," as defined in section 512.

Section 512(a) of the Code provides that the term "unrelated business taxable income" means the gross income derived by any organization from any unrelated trade or business (as defined in section 513) regularly carried on by it, less the deductions allowed by this chapter which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

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Section 512(b)(3)(A) of the Code modifies the definition of unrelated trade or business by excluding (except as provided in subparagraph (B)):

(i) all rents from real property (including property described in section 1245(a)(3)(C)), and

(ii) all rents from personal property (including for purposes of this paragraph as personal property any property described in section 1245(a)(3)(B)) leased with such real property, if the rents attributable to such personal property are an incidental amount of the total rents received or accrued under the lease, determined at the time the personal property is placed in service.

Section 512(b)(3)(B) of the Code provides that subparagraph (A) shall not apply:

(i) if more than 50 percent of the total rent received or accrued under the lease is attributable to personal property described in Subparagraph (A)(ii), or

(ii) if the determination of the amount of such rent depends in whole or in part on the income or profits derived by any person from the property leased (other than an amount based on a fixed percentage or percentages of receipts or sales).

Section 513(a) of the Code states that the term "unrelated trade or business" means any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501(c).

Section 513(d)(1) of the Code states that the term "unrelated trade or business" does not include "qualified public entertainment activities" of an organization described in section 513(d)(2)(C) of the Code.

Section 513(d)(2)(A) of the Code defines the term "public entertainment activities" to include any entertainment or recreational activity of a kind traditionally conducted at fairs or expositions promoting agriculture and educational purposes including any activity one of the purposes of which is to attract the public to fairs or expositions or to promote the breeding of animals or the development of products or equipment.

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Section 513(d)(2)(B) of the Code defines the term "qualified public entertainment activities" to mean a public entertainment activity conducted by a "qualifying organization" described in section 513(d)(2)(C) of the Code.

Section 513(d)(2)(C) of the Code states, in pertinent part, that a "qualifying" organization is an organization described in section 501(c)(3) of the Code which regularly conducts, as one of its substantial exempt purposes, an agricultural and educational fair or exposition.

Section 1.512(a)-1(a) of the Income Tax Regulations defines the term "unrelated business taxable income" as the gross income derived from any unrelated trade or business regularly carried on, less those deductions allowed by chapter 1 of the Code which are directly connected with the carrying on of such trade or business. To be deductible in computing unrelated business taxable income, therefore, expenses, depreciation, and similar items not only must qualify as deductions allowed by chapter 1 of the Code, but also must be directly connected with the carrying on of unrelated trade or business. To be "directly connected with" the conduct of unrelated business for purposes of section 512, an item of deduction must have proximate and primary relationship to the carrying on of that business.

Section 1.512(a)-1(b) of the regulations provides, in pertinent part, that expenses attributable solely to unrelated business activities are proximately and primarily related to that business activity, and therefore qualify for deduction to the extent that they meet the requirements of section 162, or other relevant provisions of the Code. However, where facilities are used both to carry on exempt activities and to conduct unrelated trade or business activities, expenses, depreciation and similar items attributable to such facilities shall be allocated between the two uses on a reasonable basis. Similarly, where personnel are used both to carry on exempt activities and to conduct unrelated trade or business activities, expenses and similar items attributable to such personnel shall be allocated between the two uses on a reasonable basis. (See section 1.512(a)-1(c) of the regulations).

Section 1.512(b)-1(c)(2)(i) of the regulations excludes rents from property described in subdivision (ii) of this subparagraph, and the deductions directly connected therewith, in computing unrelated business taxable income (except as provided in subdivision (iii) of this subparagraph). However, notwithstanding subdivision (ii) of this subparagraph, certain rents from and certain deductions in connection with debt-financed property, as defined in section 514(b)), shall be included in computing unrelated business taxable income.

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Section 1.512(b)-1(c)(2)(ii) of the regulations excludes from unrelated business income, (a) all rents from real property; and (b) all rents from personal property leased with real property if the rents attributable to such personal property are an incidental amount of the total rents received or accrued under the lease. Rents attributable to personal property generally are not an incidental amount of the total rents if such rents exceed 10 percent of the total rents from all the property leased.

Section 1.512(b)-1(c)(5) of the regulations provide that payments for the use or occupancy of rooms and other space where services are also rendered to the occupant, such as for the use or occupancy of rooms or other quarters in hotels, boarding houses, or apartment houses furnishing hotel services, or in tourist camps or tourist homes, motor courts, or motels, or for the use of occupancy of space in parking lots, warehouses, or storage garages, does not constitute rent from real property. Generally, services are considered rendered to the occupant if they are primarily for his convenience and are other than those usually or customarily rendered in connection with the rental of rooms or other space for occupancy only. The supplying of maid service, for example, constitutes such service; whereas the furnishing of heat and light, the cleaning of public entrances, exits, stairways, and lobbies, the collection of trash, etc., are not considered as services rendered to the occupant. Payments for the use or occupancy of entire private residences or living quarters in duplex or multiple housing units, of offices in any office building, etc., are generally treated as rent from real property.

Section 1.513-1(d)(2) of the regulations provides that a trade or business is "substantially related" to an organization's exempt purposes when the business activity has a substantial causal relationship to the achievement of the exempt purposes for which such organization was formed.

Taxpayers Views:

Y states that it does not provide any services to the individuals renting space in its facilities. Y cites as authority section 1.512(b)-1(c)(5) of the regulations which provides that:

> payments for the use or occupancy of rooms and other space where services are also rendered to the occupant, such as for the use or occupancy of rooms or other quarters in hotels, boarding houses, or apartment houses furnishing hotel services, or in tourist camps or tourist homes, motor courts, or motels, or for the

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use of occupancy of space in parking lots, warehouses, or storage garages, does not constitute rent from real property.

Rationale:

The information furnished shows that Y is recognized as exempt from federal income tax under section 501(c)(3) of the Code and that its predominant activity is the operation of an annual agricultural/educational fair. Therefore, based on the information furnished, Y is a qualifying organization within the meaning of section 513(d)(2)(C) of the Code. Because Y is a qualifying organization and because Y offers "qualified public entertainment activities" to attract the public to X, which is an agricultural/ educational fair, the conduct of X is not an "unrelated trade or business" within the meaning of section 513(a) of the Code.

The information furnished shows that Y rents some or all of its land and buildings to other entities to conduct horse shows and other events during the summer. The information furnished shows that these "Summer Rentals" are rentals of real property and that the income derived from this activity is rental income within the meaning of section 512(b)(3)(A) of the Code.

Further, the information furnished establishes that the income derived from restroom care, barn and ground maintenance, and related services are services that are usual and customary services provided to lessees. Accordingly, pursuant to section 1.512(b)-1(c)(5) of the regulations, the income derived from the performance of these services is not "unrelated business income".

However, with respect to the "Winter Rentals", the information furnished shows that Y enters into storage contracts with individuals who lease floor space from it in which to store cars, motorhomes, trailers, and boats. The information furnished shows that Y does not lease these buildings to an individual or individuals to operate as a storage facility. Y's leasing of this space is analogous to the renting of parking space in a parking garage. (See Section 1.512(b)-1(c)(5) of the regulations).

Y has misinterpreted section 1.512(b)-1(c)(5) of the regulations concerning the phrase "where services are also rendered to the occupant". That phrase specifically refers to the use or occupancy of rooms or other quarters in hotels, boarding houses, or apartment houses furnishing hotel services, or in tourist camps or tourist homes, motor courts, or motels. The phrase does not refer to the use of occupancy of space in parking lots, warehouses, or storage garages.

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Section 1.512(b)-1(c)(5) of the regulations closely tracks the legislative history of section 512(b)(3) of the Code in which it is stated that parking lot income is not rental income.(See House Report at 36, 110, 1950-2 C.B. 409, 459).

Moreover, since section 1.512(b)-1(c)(5) of the regulations states categorically that parking lot revenue and revenue from warehouses, or storage garages are not rent from real property, income from the operation of a storage garage by an exempt organization does not constitute "rent" as defined in section 512(b)(3). Because the operation of a storage garage does not yield "rent," within the ambit of section 512(b)(3), it is not necessary to determine whether the exempt organization performs any services primarily for the convenience of the occupant.

Therefore, the income from the "Winter Rentals" is not rental income within the meaning of section 512(b)(3)(A) of the Code. Accordingly, the "Winter Rental" income is unrelated business taxable income.

Conclusions:

1. Y's income from the storage of cars, boats, motorhomes, trailers, etc., during the winter months constitutes unrelated business income under sections 511 and 512 of the Internal Revenue Code.

2. The leasing of space for the storage of cars, boats, motorhomes, trailers, etc., during the winter months does not constitute the rental of real property as defined in section 512(b)(3) of the Code.

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