199914038

Internal Revenue Service

Department of the Treasury

Washington, D.C. 20224

Index No.: 856.04-00

Person to Contact:

Telephone Number:

Refer Reply to:
CC:DOM:FI&P:3/PLR-113891-98
Date:
JAN - 6 1999

Legend:

Trust =

Operating Partnership =

State X =

State Y =

Date 1 =

a =

This ruling responds to a letter dated June 26, 1998, and subsequent correspondence, submitted by your authorized representatives requesting rulings under § 856 of the Internal Revenue Code regarding the provision of telecommunications services.

FACTS

Trust is a State X corporation that has filed an election under § 856(c) of the Code to be treated as a real estate investment trust (REIT) commencing with its taxable year that ended Date 1. Trust is a fully integrated real estate company which, through Operating Partnership, a State Y limited partnership, owns and operates commercial office buildings (individually a Property and collectively the Properties). Trust owns an interest in Operating Partnership of approximately a percent.

To retain existing tenants as well as attract new tenants (collectively, Tenants) to the Properties, certain or all of the Properties will be improved with a network of voice, video, and data communications systems (System). For any particular Property, the System will be owned by Trust and/or by one or more third-parties (Provider). The Provider or Trust may provide telecommunications-related equipment to the Tenants in connection with the provision of Telecommunications Services. Telecommunications Services means the transmission and provision of the following information and information services: telephone and other communications, e-mail, video communications, electronic research, internet access, communications networking, safety and security systems, and environmental control systems.

Trust or Operating Partnership will derive income (Charges) in connection with the provision of Telecommunications Services as follows. First, pursuant to an agreement between a Provider and Trust, a Provider may pay Trust or Operating Partnership a fee that may be expressed as a fixed dollar amount, as a percentage of the Provider's gross receipts or as some combination of the two. Second, in addition to or in lieu of such fees received from a Provider, a Tenant may pay Trust or Operating Partnership a fee that may be expressed as a fixed dollar amount, as a percentage of the Tenant's payments made to any Provider, or as some combination of the two. Third, in the case where Trust or Operating Partnership owns an equity interest in an entity that is treated as a partnership for Federal income tax purposes, Trust or Operating Partnership may derive income in connection with the provision of Telecommunications Services by reason of Trust's or Operating Partnership's proportionate share of charges received by such entity from Tenants and Providers in connection with the provision of Telecommunications Services to Tenants.

The Telecommunications Services described above may be included in a package of services provided to Tenants for a fee or Tenants may be charged a fee for each individual Telecommunications Service received. In addition, Tenants may be charged a fee based upon the actual amount of usage of a particular Telecommunications Service.

Trust makes the following three representations:

(1) Trust represents that the Telecommunications Services offered to the Tenants are of the type usually and customarily offered or provided to tenants of similar office properties located in the same geographic markets where the Properties are located.

(2) Trust represents that no Provider that has entered into agreements with Trust offers any Telecommunications Services

to Tenants that the Provider does not also offer to its customers that are not Tenants.

(3) Trust represents that the actual Telecommunications Services provided to Tenants by Providers are not customized to fit the specific needs of a particular Tenant; Tenants merely are offered a menu of Telecommunications Services that are generally available to customers of the Provider, and the Tenants can pick from that menu the Telecommunications Services they wish to receive.

LAW AND ANALYSIS

Section 856(c)(2) of the Code 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(d)(1) of the Code provides that "rents from real property" include (subject to the exclusions in § 856(d)(2)): (i) rents from interests in real property, (ii) charges for services customarily furnished or rendered in connection with the rental of real property (whether or not such charges are separately stated), and (iii) rent attributable to personal property which is leased under, or in connection with, a lease of real property, but only if the rent attributable to such personal property for the taxable year does not exceed 15 percent of the total rent for the year attributable to both the real and personal property leased under, or in connection with the lease.

Section 1.856-4(b)(1) of the Income Tax Regulations provides that, for purposes of §§ 856(c)(2) and 856(c)(3) of the Code, the term "rents from real property" includes charges for services customarily furnished or rendered in connection with the rental of real property, whether or not the charges are separately stated. Services rendered to tenants of a particular building will be considered customary if, in the geographic area in which the building is located, tenants in buildings of a similar class are customarily provided with the service. In particular geographic areas where it is customary to furnish electricity or other utilities to tenants in buildings of a particular class, the submetering of such utilities to tenants will be considered a customary service.

Section 856(d)(2)(C) of the Code excludes from the definition of "rents from real property" any "impermissible tenant service income" as defined in § 856(d)(7). Section 856(d)(7)(A) provides that "impermissible tenant service income" means, with respect to any real or personal property, any amount received or accrued directly or indirectly by a REIT for furnishing or rendering services to the tenants of such property or managing or operating such property. Section 856(d)(7)(B)

provides that if the amount of impermissible tenant service income with respect to a property for any taxable year exceeds one percent of all amounts received or accrued directly or indirectly by the REIT with respect to such property, the impermissible tenant service income of the REIT with respect to the property shall include all such amounts.

Section 856(d)(7)(C)(i) of the Code excludes from the definition of impermissible tenant service income amounts received for services furnished or rendered, or management or operation provided through an independent contractor from whom the REIT itself does not derive or receive any income. Additionally, § 856(d)(7)(C)(ii) excludes from the definition of impermissible tenant service income any amount which would be excluded from unrelated business taxable income under § 512(b)(3) if received by an organization described in § 511(a)(2).

Section 1.512(b)-1(c)(5) of the Regulations 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 use or occupancy of space in parking lots, warehouses, or storage garages, do 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, and the collection of trash 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, or offices in any office building, are generally treated as rent from real property.

One of the principal purposes for the income restrictions imposed by §§ 856(c) and 856(d) of the Code is to ensure that the bulk of the REIT's income is from passive sources and not from the active conduct of a trade or business. See H.R. Rep. No. 2020, 86th Cong., 2d Sess., 6 (1960), 1960-2 C.B. 819, 822-823.

The provision of Telecommunications Services is similar to the provision of services by public utilities and has become an essential means of communicating business information and data. The ability of Trust to provide Telecommunication Services to Tenants of the Properties will allow Trust to offer services similar to those being offered to tenants of similar classes of office buildings in the same geographic markets where the Properties are located.

Accordingly, the Telecommunication Services offered by Trust to Tenants of the Properties will not be considered to be rendered primarily for the convenience of the tenants under § 1.512(b)-1(c)(5) of the regulations. As a result, the services will fall within the exception contained in § 856(d)(7)(C)(ii) of the Code and the provision of Telecommunication Services will not prevent Trust's share of amounts derived from the Properties from qualifying as "rents from real property" under § 856(d)(1) of the Code. Moreover, based on Trust's representation that the Telecommunications Services are of the type usually and customarily offered or provided to tenants of similar office properties located in the same geographic markets where the Properties are located, Charges received or accrued by Trust, if otherwise qualifying, will constitute "rents from real property" within the meaning of § 856(d)(1)(B) of the Code.

Under § 1.856-3(g) of the regulations, a REIT that is a partner in a partnership is deemed to own its proportionate share of each of the assets of the partnership and to be entitled to the income of the partnership attributable to that share. For purposes of § 856 of the Code, the interest of a partner in the partnership's assets shall be determined in accordance with the partner's capital interest in the partnership. The character of the various assets in the hands of the partnership and items of gross income of the partnership shall retain the same character in the hands of the partners for all purposes of § 856.

HOLDINGS

Accordingly, based on the facts submitted and representations made, we rule as follows:

1. The provision of Telecommunications Services to the Tenants as described above will not cause Trust's allocable share of otherwise qualifying income received by Operating Partnership from the Properties to be excluded from the term "rents from real property" within the meaning of § 856(d)(1) of the Code.

2. Charges received or accrued directly by Trust, or Trust's receipt of Trust's allocable share of Charges received or accrued by Operating Partnership if otherwise qualifying will constitute "rents from real property" within the meaning of § 856(d)(1)(B) of the Code. For example, Charges received or accrued from a person described in § 856(d)(2)(B)(i) or § 856(d)(2)(B)(ii) will not constitute "rents from real property."

Except as specifically ruled upon above, no opinion is expressed or implied regarding the consequences of this transaction under any other provision of the Code. In

particular, no opinion is expressed whether Trust qualifies as a REIT under § 856 of the Code.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) of the Code provides that this ruling may not be used or cited as precedent.

In accordance with the power of attorney on file, we are sending a copy of this letter to Trust's authorized representatives.

Sincerely yours,

Assistant Chief Counsel
(Financial Institutions
and Products)

By: Alice M. Bennett
Alice M. Bennett
Chief, Branch 3

Enclosures:
Copy of this letter
Copy of section 6110 purposes