Internal Revenue Service

Department of the Treasury

200147058

Washington, DC 20224

Significant Index Numbers:

512.00-00

Contact Person:

Telephone Number:

Refer reply to: T:EO:B3

Date: AUG 28 2001

Employer Identification Number:

Legend:

M =

N =

Dear Sir or Madam:

This is in response to letters dated May 23 and July 31, 2001, and previous correspondence submitted by your authorized representatives on behalf of M and its title holding corporations, requesting a ruling on the proper treatment under section 512 of the Internal Revenue Code of certain payments M and its title holding corporations intend to receive in connection with the provision of telecommunications services, telecommunications related services, and utility services.

M is a group trust of which N is the trustee. M's principal purpose is to act as a medium for the collective investment of the funds of pension, profit-sharing and other qualified benefit trusts in real estate and real estate interests. M qualifies as a group trust arrangement as described in Rev. Rul. 81-100, 1981-1 C.B. 326. Accordingly, M is exempt from federal income tax under section 501(a) of the Code for the funds that equitably belong to its participating trusts that qualify under section 401(a), and is exempt under section 408(e) for the funds that equitably belong to its participating individual retirement accounts that qualify under section 408. M is subject to the provisions of section 502, relating to feeder organizations, and sections 511–515, relating to the tax on unrelated business income.

M is the sole shareholder of each title holding corporation, each of which is exempt under section 501(a) of the Code as an organization described in either section 501(c)(2) or 501(c)(25).

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M holds interests in a substantial portfolio of real estate investments (the "Properties"), none of which M owns directly. All of the Properties are owned indirectly through M's interests in various partnerships, limited liability companies, the title holding corporations, and other entities. The title holding corporations may own one or more Properties and, in the case of title holding corporations that are described in section 501(c)(2) of the Code, may hold interests in partnerships or limited liability companies which own the Properties. No title holding corporation that is described in section 501(c)(25) holds any interest in any Property through a partnership or limited liability company. The Properties include residential real estate and commercial real estate (including various shopping centers and malls, industrial centers, and offices and office complexes). All of the Properties are held for leasing to tenants.

The owners of the Properties (the "Owners") intend to enter into various agreements with independent contractors (the "Service Providers"), under which the Service Providers are given either exclusive or non-exclusive rights to provide various telecommunications services (as defined below) to tenants at the Properties who wish to subscribe for such services (each agreement, a "Telecommunications Agreement"). "Telecommunications Services" may include the transmission or provision of: multi-channel television services (such as basic, premium, pay-per-view and, as technology becomes available, video-on-demand television services), direct and high speed Internet access and data transmission services, and video, telephone (including any communication services deliverable over telephone systems) and radio services, as well as certain ancillary services, including security, medical, smoke and fire alert, and other information retrieval services. The Telecommunications Services may be provided by wire or cable, by fiber optic or digital transmission, over-the-air transmission (including microwave transmission), by satellite, or by any other means which may become customary and technologically feasible in the future. The Service Provider may also provide, sometimes at no charge to the Owner, Telecommunications Services in common areas of the Properties, including, but not limited to, clubhouses, and recreational and exercise facilities.

In most circumstances the Service Provider will construct, provide, install, operate, maintain, upgrade and improve the transmission wires and cables, amplifiers, conduits, and related apparatus and equipment, electronic or otherwise (the "Communications System"), that are necessary for the provision of the Telecommunications Services. Some portion of the Communications System, however, may include pre-existing wiring or other equipment of the Owner that the Service Provider is granted the right to use and may sometimes be obligated to maintain and/or upgrade.

Except for any portion of the Communications System which, as just described, may be owned by the Owner, the Communications System is generally owned by the Service Provider during the term of the Telecommunications Agreement and may be removed by the Service Provider upon the expiration of such Agreement. In certain circumstances, however, some or all of the Communications System, such as internal and underground wiring or equipment, may become the property of the Owner upon the expiration of the Telecommunications Agreement (either automatically or upon payment

by the Owner) and may not be removed by the Service Provider. Alternatively, the Communications System may become the property of the Owner within a given time period after the expiration of the Agreement as a result of the Service Provider's failure to exercise its right to remove some or all of the Communications System.

Under each of the Telecommunications Agreements, the Owner will grant the Service Provider the rights to use, occupy and access those portions of the Property necessary to enable the Service Provider to provide the Telecommunications Services under the Telecommunications Agreement (the "Easement Rights"), including rights of use and access to install, maintain, service, operate, repair, replace, upgrade, expand and remove the various elements comprising the Communications Systems. Rights of access to the Property by personnel or representatives of the Service Provider may be limited to business hours, with exceptions made in the event of an emergency, and in the case of access to certain parts of the Property, such as the roof, may require prior notice and/or consent of the Owner. In some cases, the Easement Rights will be formally designated as an "easement" and the easement may or may not be recorded. In other cases, the Easement Rights will constitute rights in the nature of an easement, but will not be formally designated or legally recordable as such. In conjunction with the granting of the Easement Rights, the Owner may also grant to the Service Provider a leasehold or license of a defined space in or on the Property to house certain equipment and materials necessary for the provision of the Telecommunications Services. This space may include closet and other floor space for storing transformers and related electrical equipment, as well as rooftop space for the placement of satellite dishes and antennae.

The Owner will be entitled to receive compensation in return for granting the Service Provider the Easement Rights and any related leasehold or license rights, including the rights to provide Telecommunications Services at the Property. The Owner will generally be compensated by the Service Provider under any or a combination of the following payment methods (the "Payment Methods"):

a) Owner will receive a fixed percentage or percentages of the gross revenues derived by the Service Provider from providing Telecommunications Services to the Tenants (which percentage(s) may, in certain cases, vary depending on the type of Telecommunications Service provided, the number of subscribers for Telecommunications Services and/or the amount of gross receipts, but which percentage(s) are fixed and determinable under the terms of the Telecommunications Agreement and are not subject to the discretion of either of the parties to the Telecommunications Agreement);

b) Owner will receive fixed periodic payments;

c) Owner will receive a flat amount from the Service Provider for each tenant that subscribes or newly subscribes for the Telecommunications Services;

d) Owner will receive a lump-sum payment due upon entry into the

Telecommunications Agreement (or at some other time provided in the Agreement) which payment amount may be based on the number of units that can be occupied within the Property.

While the payment to the Owner is sometimes entitled rent, it may also be referred to as a fee, a license payment or simply as consideration or compensation. In any event, the payment is intended to qualify as rents from real property for purposes of section 512(b)(3) of the Code and such intention may or may not be explicitly stated in the Telecommunications Agreement.

In many of the Telecommunications Agreements, the Owner will agree to cooperate with the Service Provider in allowing the Service Provider to market the Telecommunications Services to tenants at the Properties. Such cooperation will be limited to passive activities. For instance, the Owner may be required to: provide new residents or applicants for residency with marketing materials and service order forms provided by the Service Provider (the "Promotional Materials"); include the Promotional Materials among the Owner's own promotional kits or packages relating to the Property; allow the Service Provider to display (and replenish) its Promotional Materials in the leasing office or other agreed upon location at the Property; give the Service Provider notice of any changes in tenancies at the Property and the names and addresses of new tenants; and allow the Service Provider access to the common or lobby areas or recreational or meeting rooms at the Property or such other agreed upon space so that the Service Provider may hold informational and marketing sessions relating to the Telecommunications Services (and providing any reasonable assistance relating thereto). The Owner is not required under the terms of a Telecommunications Agreement to engage in any more than passive marketing activities similar to the types just described.

Tenants at the Properties will generally be furnished with certain utility services, including electricity, heat, light, water, sewer and gas (the "Utility Services"). All of the Utility Services will be usual and customary in the geographic market in which the Properties are located. The Utility Services may be separately metered and/or sub-metered for particular tenants. The Owner typically will pay a utility provider directly for the Utility Services and then charge its tenants for those services. The charges to the tenant will generally be consistent with current market rates in the geographical location of the Properties and, at industrial, commercial or business properties, the charges to a tenant may include an extra fee for overtime usage (that is, usage beyond customary business hours or excessive usage based on the nature of the tenant's activities). The Owner will retain the difference between the price it charges its tenants and the amount it owes the utility provider for the Utility Services, which may result in a profit to the Owner. The charge to the tenants may be a component of the rent payable to the Owner or may be separately stated. In certain cases, the Owner may be the provider of the Utility Services and will charge the tenants directly for those Utility Services at a price that exceeds the cost of such Utility Services to the Owner. Such will be the case, for example, if the Property is equipped with its own emergency electricity generator or backup power source.

The following representations have been made:

1) M qualifies as a group trust arrangement that meets the requirements of Rev. Rul. 81-100.
2) Not more than 50% of the total rents under each Telecommunications Agreement is attributable to personal property, as provided in section 512(b)(3)(B)(i) of the Code and section 1.512(b)-1(c)(2)(iii)(a) of the Income Tax Regulations;
3) None of the payments received under any of the Payment Methods described in this ruling request will depend in whole or in part on the income or profits derived by any person from the Properties or the Easement Rights, but may be based on a fixed percentage or percentages of receipts or sales within the meaning of section 512(b)(3)(B)(ii) of the Code and section 1.512(b)-1(c)(2)(iii)(b) of the regulations; and
4) The Owners will not engage in any marketing, promotional or advertising activities relating to any Telecommunications Services, other than marketing activities similar to the types described above.

Section 511 of the Code imposes a tax on the unrelated business taxable income of organizations and trusts exempt from federal income tax under section 501(a).

Section 512(a)(1) of the Code provides, in relevant part, that the term "unrelated business taxable income" is defined as the gross income derived by any organization from any unrelated trade or business (as defined in section 513) regularly carried on by it, less allowable deductions directly connected with the carrying on of such trade or business, subject to the modifications provided in section 512(b).

Section 512(b)(3) of the Code provides that unrelated business taxable income shall not include amounts which constitute rents from real property and rents from personal property 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, provided that

1) 50 percent or less of the total rent received or accrued under the lease is attributable to the personal property (See section 512(b)(3)(B)(i) of the Code and section 1.512(b)-1(c)(2)(iii)(a) of the regulations), and
2) the amount of rent does not depend 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) (See section 512(b)(3)(B)(ii) of the Code and section 1.512(b)-1(c)(2)(iii)(b) of the regulations.)

Section 1.512(b)-1 of the regulations provides that whether a particular item of income falls within any of the modifications provided in section 512(b) of the Code shall be determined by all the facts and circumstances of each case. For example, if a payment termed "rent" by the parties is in fact a return of profits by a person operating the property for the benefit of the tax-exempt organization or is a share of the profits

retained by such organization as a partner or joint venturer, such payment is not within the modification for rents provided in section 512(b).

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 the occupant's 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, or offices in any office building, etc., are generally rent from real property.

Section 512(c) of the Code and section 1.512(c)-1 of the regulations provide that if a trade or business regularly carried on by a partnership of which an organization is a member is an unrelated trade or business with respect to such organization, such organization in computing its unrelated business taxable income shall, subject to the exceptions, additions, and limitations contained in section 512(b), include its share (whether or not distributed) of the gross income of the partnership from such unrelated trade or business and its share of the partnership deductions directly connected with such gross income.

Rev. Rul. 67-218, 1967-2 C.B. 213, provides that income from the lease of a pipeline system consisting of right-of-way interests in land, pipelines buried in the ground, pumping stations, equipment, and other appurtenant property constitutes rent from real property (including personal property leased with the real property) within the meaning of section 512(b)(3) of the Code because the basic component to the pipeline system, i.e., the easement giving right-of-way interest in land, constitutes real property.

Rev. Rul. 67-218 establishes that an easement giving right-of-way interests in land constitutes real property, the leasing of which can give rise to "rents from real property" within the meaning of section 512(b)(3) of the Code. The Easement Rights granted under the Telecommunications Agreements are directly analogous to the right-of-way interests in land addressed in Rev. Rul. 67-218. The Telecommunications Agreements establish rights to use, occupy and access the Properties, which, like the land in Rev. Rul. 67-218, constitute real property. Accordingly, payments that an Owner receives under the Telecommunications Agreements in consideration of the Easement Rights constitute "rents from real property" within the meaning of section 512(b)(3). In addition, to the extent an Owner grants a leasehold or license of a defined space in or on the Property to house certain equipment and materials as described above, payments to the Owners for the use or right to use such space constitute "rents from real property" within the meaning of section 512(b)(3) since the space subject to the lease or license is

real property.

Section 512(c) of the Code and section 1.512(c)-1 of the regulations provide that, in computing unrelated business taxable income, a member of a partnership shall include, subject to the exceptions provided in section 512(b), its share of the partnership's income from an unrelated trade or business. Accordingly, to the extent M or a title holding corporation described in section 501(c)(2) does not receive the income from a Telecommunications Agreement directly as an Owner, but rather receives its allocable share of such income through a partnership or limited liability company that is the direct Owner of the Property, the character of the income as "rents from real property" within the meaning of section 512(b)(3) flows through from the partnership or limited liability company to M or the title holding corporation. Thus, (i) M's share of any income derived under a Telecommunications Agreement by any partnership or limited liability company in which M is a partner or member, will qualify as "rents from real property" within the meaning of section 512(b)(3), and (ii) each title holding corporation's share of any income derived under a Telecommunications Agreement by any partnership or limited liability company in which such title holding corporation is a partner or member, as well as any income derived directly by a title holding corporation under a Telecommunications Agreement, will qualify as "rents from real property" within the meaning of section 512(b)(3).

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 do not constitute rent from real property. It further provides, however, that (i) services are considered rendered to the occupant if they are primarily for the occupant's convenience and are other than those usually or customarily rendered in connection with the rental of rooms or other space for occupancy; and (ii) 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.

Because heat and light are specifically excluded from treatment as services rendered to the occupant, their provision does not affect the characterization of otherwise qualifying "rents from real property" within the meaning of section 512(b)(3) of the Code. Additionally, any income derived by the Owners in connection with the provision of heat and light is not services income, but is includable in "rents from real property" within the meaning of section 512(b)(3), whether or not the charges for heat and light are separately stated or are incorporated into a tenant's rental obligations.

Electricity, water, sewer and gas are substantially similar to those services which, under section 1.512(b)-1(c)(5) of the regulations, are not considered rendered to the occupant. These services, like the services listed in the regulations section, are essential to the operation of the Properties and thus are not primarily rendered for the convenience of the tenants. They are also customarily rendered in connection with the rental of property. Moreover, since heat and light are not services that are rendered to the occupant, it follows that electricity and gas, which are generally necessary for the generation of heat and light, also are not services that are rendered to the occupant. Accordingly, the provision of electricity, water, sewer and gas service does not affect the

characterization of otherwise qualifying "rents from real property" within the meaning of section 512(b)(3) of the Code. Further, any income derived by the Owners in connection with the provision of electricity, water, sewer and gas service is not service income, but is includable in "rents from real property" within the meaning of section 512(b)(3) of the Code, whether or not the charges for electricity, water, sewer or gas service are separately stated or are incorporated into the tenant's rental obligations.

For the same reasons listed above in connection with the analysis of the Telecommunications Services, to the extent M or a title holding corporation described in section 501(c)(2) of the Code does not receive the income from the provision of a Utility Service directly as Owner, but rather receives its allocable share of such income through a partnership or limited liability company that is the direct Owner of the Property, the character of the income as "rents from real property" within the meaning of section 512(b)(3) flows through from the partnership or limited liability company to M or the title holding corporation. See section 512(c) and section 1.512(c)-1 of the regulations.

Based on the facts and information submitted and the representations made, we conclude that:

1) M's share of any income derived under a Telecommunications Agreement by any partnership or limited liability company in which M is a partner or member, will qualify as "rents from real property" within the meaning of section 512(b)(3) of the Code;

2) Any income derived directly by a title holding corporation under a Telecommunications Agreement, and each title holding corporation's share of any income derived under a Telecommunications Agreement by any partnership or limited liability company in which such title holding corporation is a partner or member, will qualify as "rents from real property" within the meaning of section 512(b)(3) of the Code.

3) M's share of any income derived by any partnership or limited liability company in which M is a partner or member, in connection with the provision of Utility Services, will qualify as "rents from real property" within the meaning of section 512(b)(3) of the Code, and the provision of the Utility Services to tenants of the Properties will not cause M's share of any otherwise qualified amounts to be excluded as "rents from real property" within the meaning of section 512(b)(3); and

4) Any income derived directly by a title holding corporation in connection with the provision of Utility Services, and each title holding corporation's share of any income derived by any partnership or limited liability company in which such title holding corporation is a partner or member, in connection with the provision of Utility Services, will qualify as "rents from real property" within the meaning of section 512(b)(3) of the Code, and the provision of the Utility Services to tenants of the Properties will not cause a title holding corporation's direct receipt of, or share of, any otherwise qualified amounts to be excluded as "rents from real property" within the meaning of section 512(b)(3).

Rulings (1) and (2) are limited and apply only with respect to Telecommunications Agreements having terms and provisions which are similar, in all material respects, to the corresponding terms and provisions described above. Neither of such rulings may be relied upon with respect to, and no inference shall be drawn with respect to the proper treatment under section 512 of the Code of payments made under, any other Telecommunications Agreement.

Except as specifically ruled upon above, no opinion is expressed concerning the federal income tax consequences of the transactions described above under any other provision of the Code.

Pursuant to a Power of Attorney on file in this office, a copy of this letter is being sent to your authorized representatives. You should keep a copy of this letter in your permanent records.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

If you have any questions, please contact the person whose name and telephone number appear in the heading of this letter.

Sincerely,

(signed) Robert C Harper, Jr.

Robert C. Harper, Jr.
Manager, Exempt Organizations
Technical Group 3

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