



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

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512,10-00

200246032

Date:

AUG 19 2002

Contact Person:

Identification Number:

Telephone Number:

T:EO:B2

Employer Identification Number:

LEGEND:

M =
N =
O =
P =

Dear Sir or Madam:

This is in reply to your request for certain rulings regarding the proposed sale of your entire remaining interest in an apartment building complex.

You are recognized as exempt under section 501(a) of the Internal Revenue Code ("Code") as an organization described in section 501(c)(3), and you are classified as a supporting organization within the meaning of section 509(a)(3).

You currently own M and certain related common elements. M is one building constituting a single unit in N, a condominium apartment complex. N was contributed to you several years ago by a related for-profit corporation as a charitable gift, and it was your principal asset. You were not involved in the development of N and held it as a passive real estate investment. You previously concluded that it would be prudent to diversify your asset base and sell N in order to continue your exempt activities. You received an unsolicited offer to purchase N from an unrelated third party, O. O agreed to purchase all of your interests in N, but subsequently could not obtain sufficient financing for such a purchase unless you agreed to take certain steps prior to the closing of the sale, as O intended to sell the apartments as individual condominium units.

Prior to the expected sale, you requested and received a ruling from the Service that the sale of your interest in N to O would not adversely affect your tax-exempt status as an

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organization described in section 501(c)(3) of the Code, and that any gain on the sale of N would not constitute unrelated business taxable income under sections 511 and 512. After receipt of this ruling, O informed you that it could not obtain sufficient financing to purchase all of your interests in N, but instead wished to purchase two of the three buildings comprising N together with an option to purchase M. Thereafter, you received a revised private letter ruling that your sale to O of all your interests in N, except M, would not jeopardize your tax-exempt status, nor would any gain thereon be subject to taxation as unrelated business taxable income.

Since the first transaction, you have taken certain actions to dispose of your interest in M. You have represented that State law required you to register M with the State real estate commission before it could be offered for sale. You also contacted parties who had expressed a prior interest in N and/or M. Subsequently, you received and accepted an offer from P to purchase your entire interest in M in a single transaction. You executed an Option Agreement with P, whereby P received an option to purchase M. P expects to exercise this option, if it can obtain the requisite financing. This transaction would be completed pursuant to a Purchase and Sale Agreement you have negotiated with P. To meet certain financing requirements imposed by the lender, P has requested and you have agreed to permit P to take certain actions, including filing an application for a report from the State real estate commission so P can complete sales to individual buyers shortly after P completes its acquisition of M. Such report and the additional condominium documentation necessary to create the individual condominium units to be sold by P will not, however, be recorded or be effective unless and until the sale to P of your interest in M is completed. All expense and risk associated with these actions are borne by P, not you. The sale of your interest in M to P is also conditioned upon you obtaining a favorable private letter ruling from the Service regarding this transaction. The option payments are to be applied to the purchase price when the sale is closed.

You represent that the sale is at fair market value, that your interest in M will be sold on an as-is basis and that since you acquired your interest in N, you have made no physical improvements to N, including M. In addition, you have represented that there is no debt on M or any of the associated common elements and no "acquisition indebtedness" as defined in section 514 of the Code.

You represent that you hold no other interests in real property and the only prior sale of real property undertaken by you was the initial sale of your other interests in N, at which time you attempted to, but were unsuccessful in selling your remaining interest in M.

You represent that (1) you have had and will have no role in the sales or marketing of any individual condominium units by P; (2) all documentation necessary to further subdivide M into individual condominium units, market individual units and meet the requirements of State law will be completed by P at its sole cost and expense (subject to your review) and none of these documents will become effective unless the sale of your interest in M is completed; (3) the sale of M will be made to a single buyer, in a single closing; and, (4) P and its lender bear all risk that any individual units cannot be sold pursuant to any and all contracts executed between P and potential purchasers.

You have requested the following rulings:

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1. The sale of your interest in M will not adversely affect your tax-exempt status under section 501(c)(3) of the Code.
2. Any gain to you on the sale of your interest in M will not be "unrelated business taxable income" under sections 511 and 512 of the Code and will not be taxable to you as such.
3. Any option payment income received by you as a result of the Option Agreement, in the event the sale is not completed, will not be "unrelated business taxable income" under sections 511 and 512 of the Code and will not be taxable to you as such.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations that are organized and operated exclusively for one or more exempt purposes listed in such section, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 511 of the Code imposes a tax in the unrelated business taxable income of organizations described in section 501(c)(3).

Section 512(a)(1) of the Code defines the term "unrelated business taxable income" 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, both computed with the modifications provided in section 512(b).

Section 512(b)(5) of the Code excludes from the computation of unrelated business taxable income all gains or losses from the sale, exchange, or other disposition of property other than - (A) stock in trade or other property of a kind which would properly be includable in inventory if on hand at the close of the taxable year, or (B) property held primarily for sale to customers in the ordinary course of the trade or business. This provision also states that there shall be excluded from unrelated business taxable income all gains or losses recognized in connection with the organization's investment activities from the lapse or termination of options to buy or sell securities or real property.

In Malat v. Riddell, 383 U.S. 569 (1966), the Supreme Court defined the standard to be applied in determining whether property is held primarily for sale to customers in the ordinary course of business. The Court interpreted the word "primarily" to mean "of first importance" or "principally." By this standard, ordinary income would not result unless a sales purpose is dominant.

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The submitted information and representations indicate that you received your interest in M by charitable gift and took no major actions to improve N and, more specifically, M. M is your only real estate asset, and your only prior sale of real property has been the original liquidation of your other interests in N. In connection with the sale to P, P will change the characterization of M from a single condominium unit with multiple apartment rental units to individual condominium units, which it expects to sell to individual purchasers at its sole risk and expense. You have agreed to take certain actions in connection therewith so that P might obtain its financing to complete the transaction. You state that once M has been sold to P, you will continue to carry on the activities that are the basis for your exemption under section 501(c)(3) of the Code. In the event that P does not exercise its option to purchase M or does not complete its purchase, you will use the income you receive from the Option Agreement to continue to carry on the activities which are the basis for your exemption under section 501(c)(3). In addition, you have represented that there is no debt on M or any of the associated common elements.

Accordingly, the information you have submitted establishes that In accordance with section 1.501(c)(3)-1(c)(1) of the regulations, you will continue to engage primarily in activities that accomplish exempt purposes, and no substantial part of your activities will be in furtherance of nonexempt purposes. Amounts derived from the sale of M will be excluded from the computation of unrelated business taxable income under section 512(b)(5) of the Code. Furthermore, in the event that the sale of M does not occur, the income you might receive pursuant to the Option Agreement will also be excluded under section 512(b)(5).

Therefore, based on the information submitted we have concluded that:

1. The sale of your interest in M will not adversely affect your tax-exempt status under section 501(c)(3) of the Code.
2. Any gain to you on the sale of your interest in M will not be "unrelated business taxable income" under sections 511 and 512 of the Code and will not be taxable to you as such.
3. Any option payment income received by you as a result of the Option Agreement, in the event the sale is not completed, will not be "unrelated business taxable income" under sections 511 and 512 of the Code and will not be taxable to you as such.

These rulings are based on the understanding that there will be no material changes in the facts upon which they are based. Any changes that may have a bearing on your tax status should be reported to the Service.

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 as precedent.

This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described.

Re:

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter. Because this letter could help resolve future questions about your income tax responsibility, please keep a copy of this ruling in your permanent records.

Sincerely yours,



Joseph Chasin
Acting Manager,
Exempt Organizations
Technical Group 2