



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

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No third party contacts
UIL: 512.01-01

Contact Person:

Identification Number:

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Employer Identification Number:

Legend:

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Dear :

We have reconsidered the ruling we issued to you on March 28, 2006, PLR 200625035, concerning whether income you derive from a variety of activities is "unrelated business taxable income" within the meaning of section 512(a)(1) of the Internal Revenue Code.

After reviewing the ruling letter, we have determined that Ruling 1 is incorrect in broadly concluding that revenue from a variety of sources would not constitute unrelated business taxable income to you under section 512 of the Code. Further, a review of information you provided in response to subsequent requests for information discloses that PLR 200625035 is based on facts that do not sufficiently or adequately describe the operations for which the rulings were requested. Accordingly, pursuant to our authority in section 13.04 of Rev. Proc. 2010-4, 2010-1 I.R.B. 122, 150, this ruling revokes in part and modifies in part PLR 200625035. In addition, your request for retroactive relief under section 7805(b) of the Code has been granted. You may rely on the March 28, 2006 ruling letter for taxable periods ending before the date of this letter.

In PLR 200625035 we ruled as follows:

1. Revenue generated from providing living quarters in buildings that you own to your students and faculty; and temporary living quarters to family members of your students and faculty; potential students; family members of potential students; guests who are speakers at your institution; and guests of other non-affiliated non-profit organizations (A-F, above) in your immediate geographic area

who are also speakers or musical performers at your institution does not constitute unrelated business taxable income under section 512 of the Code.

2. Revenue generated from the renting of rooms to the general public constitutes unrelated business taxable income under section 512(a)(1) of the Code.

After reconsideration of your original request and consideration of all additional information submitted, we rule as follows:

1. Revenue generated from providing living quarters in buildings that you own to your students does not constitute unrelated business taxable income under section 512(a)(1) of the Code.
2. Revenue generated from the renting of rooms to persons other than your students constitutes unrelated taxable income under section 512(a)(1) of the Code.

Facts

You are exempt under section 501(a) of the Code as an organization described in section 501(c)(3) and are classified as an organization that is not a private foundation because you are an educational organization described in sections 509(a)(1) and 170(b)(1)(A)(ii). You are an independent, multi-denominational seminary whose mission includes educating leaders for ministry in churches and related organizations, extending the work of social justice, and academic teaching and research.

In furtherance of your educational purposes, you arrange for your students and faculty to participate in various programs with educational and religious institutions located near your campus. In this regard, you have several academic partnership agreements with A and offer dual degrees, a Ph.D. program and a Masters Program in Divinity and Social Work. Some of your senior faculty hold joint appointments in A's Department of Religion. Participating students may cross-enroll at either campus without any institutional tuition transfer. You maintain a large religious/theological research collection and your library facilities are shared by other religious and secular institutions of higher learning including but not limited to A, B, C, and D. In addition, your students rely on churches and religious organizations in the area for internships as part of their professional training. These include the E and its religious tenant, F.

Your campus is often used for meetings of individuals, groups, or institutions of differing backgrounds but similar purposes. Speakers and musical performers at your institution may also speak and perform at some of the other institutions, and speakers and musical performers at the other institutions may also speak and perform at your institution.

In addition to academic buildings, your campus includes dormitory-style and apartment-style housing for enrolled students and for your full-time faculty. You receive revenue, however, only from providing housing to students.

In one of the buildings on your campus, known as the H, you offer rooms on an overnight basis. One substantial use of the H was to temporarily house students waiting for long-term dormitory assignments to become available. You also offer accommodations, if available, to official visitors (speakers, performers, etc.) These guests are provided lodging in lieu of a lodging per diem allowance. You do not limit the rental of rooms in the H to individuals affiliated with your institution or with any of the other educational institutions located nearby. In fact, the information you submitted indicates that rooms are offered to the general public on a "first come-first served" basis and no one is denied lodging if a room is available.

Access to the H is on the inner corridor of the courtyard of your building complex but is open to the public. Your website indicates it is open 24 hours a day, 365 days per year. Although you do not post signs on the facility itself, you advertise the availability of rooms on your website, which mentions H's convenient location and amenities including: air-conditioning, private bath, cable television, wireless Internet access, an iron and a hair dryer, a miniature refrigerator, daily housekeeping services, 24-hour access front-desk security and free local telephone service and all incoming calls. Other commercial hotels are located in the area. Accommodations at the H and the rates charged to guests are comparable to other commercial hotels in the area. However, when the lodger is an official visitor who does not pay for his or her own lodging, the revenue entry is charged to the host department. When the H is used to provide temporary housing for your students, the rate is the daily portion of the student housing fee.

Law

Section 501(c)(3) of the Internal Revenue Code provides exemption from federal income tax for an organization organized and operated exclusively for religious, charitable or educational purposes, if no part of the net earnings of the organization inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(d)(2) and (3) of the Income Tax Regulations provide that the term "charitable" is used in section 501(c)(3) in its generally accepted legal sense, and includes the advancement of religion and education. Further, the term "educational" as used in section 501(c)(3), which relates both to instruction or training of the individual for the purpose of improving or developing his or her capabilities and instruction of the public on subjects useful to the individual and beneficial to the community, clearly includes an organization, such as a college, which has a regular curriculum, a regular faculty, and a regularly enrolled body of students in attendance at a place where the educational activities are regularly carried on.

Section 511(a)(1) of the Code imposes a tax on the unrelated business taxable income (as defined in section 512) of organizations described in section 501(c)(3).

Section 512(a)(1) of the Code provides that (except for provisions inapplicable here) 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 that are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

Section 513(a) of the Code defines the term "unrelated trade or business," in the case of any organization subject to the tax imposed by section 511, as 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 the purpose or function constituting the basis for its exemption under section 501 of the Code.

Section 513(a)(2) of the Code provides that the term "unrelated trade or business" does not include any trade or business which is carried on in the case of an organization described in section 501(c)(3) primarily for the convenience of its members or employees.

Section 1.513-1(a) of the regulations provides that unless one of the specific exceptions of section 512 or 513 is applicable, gross income of an exempt organization subject to the tax imposed by section 511 is includible in the computation of unrelated business taxable income if (1) it is income from trade or business, (2) such trade or business is regularly carried on by the organization, and (3) the conduct of such trade or business is not substantially related (other than through the production of funds) to the organization's performance of its exempt functions.

Section 1.513-1(b) of the regulations provides that for purposes of section 513 of the Code, the term "trade or business" has the same meaning as it has in section 162, and generally includes any activity carried on for the production of income from the sale of goods or performance of services. Activities of producing or distributing goods or performing services from which a particular amount of gross income is derived do not lose their identity as a trade or business merely because they are carried on within a larger aggregate of similar activities or within a larger complex of other endeavors which may, or may not, be related to the exempt purposes of the organization.

Section 1.513-1(c) of the regulations states that in determining whether a trade or business from which a particular amount of gross income derives is "regularly carried on," regard must be had to the frequency and continuity with which the activities productive of the income are conducted and the manner in which they are pursued. For example, specific business activities of an exempt organization will ordinarily be deemed to be "regularly carried on" if they manifest a frequency and continuity, and are pursued in a manner generally similar to comparable commercial activities of nonexempt organizations.

Section 1.513-1(d)(2) of the regulations provides that a trade or business is "related" to exempt purposes only when the conduct of the business activities has a causal relationship to the achievement of its exempt purposes. It is "substantially related" only if the causal relationship is a substantial one. To be substantially related, 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 those purposes.

Section 1.513-1(d)(4) of the regulations provides that gross income derived from charges for the performance of exempt functions does not constitute gross income from the conduct of unrelated trade or business.

Section 1.513-1(d)(4)(iii) of the regulations, provides that, with respect to dual use of assets or facilities, an asset or facility necessary to the conduct of exempt functions may also be employed in a commercial endeavor. In such cases, the mere fact of the use of the asset or facility in exempt functions does not, by itself, make the income from the commercial endeavor gross income from related trade or business. The test, instead, is whether the activities productive of the income in question contribute importantly to the accomplishment of exempt purposes.

Section 1.513-1(e)(2) of the regulations specifically states that the term "unrelated trade or business" does not include any trade or business carried on by an organization described in section 501(c)(3) primarily for the convenience of its members, students, patients, officers, or employees.

The Committee Reports accompanying the Revenue Act of 1950 [S Rep. No. 2375, 81st Cong., 2d Sess. 29 (1950)] explained the operation of section 513 in regard to university activities: "In the case of an educational institution, income from dining halls, restaurants, and dormitories operated for the convenience of the students would be considered related income and, therefore, would not be taxable." Section 1.513-1(e) of the regulations retained this distinction by excluding from the definition of "unrelated trade or business" the ancillary services (those provided primarily for the convenience of students) provided in connection with a residential college community. The example provided is that of a laundry operated by a college for the purpose of laundering dormitory linens and the clothing of students.

Rev. Rul. 58-194, 1958-1 C.B. 240, holds that an organization formed for the purpose of operating a book and supply store and a cafeteria and restaurant on the campus of a State university primarily for the convenience of its student body and faculty is operated exclusively for educational purposes. The organization was controlled by a board of directors composed of the president of the university, three elected faculty members and three elected student members. Membership in the organization was available to university students and employees for a nominal fee. The facility was open to all students at the university to afford them an opportunity to obtain their academic supplies without undue inconvenience. By providing these facilities to the university community in furtherance of its educational program, the organization is, for all intents and purposes, an integral part of the university. It is operated exclusively for educational purposes within the meaning of section 501(c)(3) of the Code.

Rev. Rul. 67-217, 1967-2 C.B. 181, holds that an organization formed to provide housing and food service exclusively for students and faculty of a university that lacks adequate student and faculty housing in accordance with the rules and regulations of the university and offers the university an option to acquire the property at any time upon payment of the outstanding indebtedness qualifies for exemption under section 501(c)(3). The facility is located near the university and is managed by a commercial firm in accordance with the rules and regulations of the university and made available to the student body at rates comparable to those charged by

similar facilities. By providing a housing facility under these circumstances, the organization was fulfilling the 'charitable' purpose of advancing education by aiding the university in fulfilling its educational purposes.

Rev. Rul. 69-69, 1969-1 C.B. 159, describes an organization created to stimulate and foster public interest in the fine arts by promoting art exhibits, sponsoring cultural events, conducting educational programs, and disseminating information relative to the fine arts. Its activities were carried on in a building that contained offices, galleries, music rooms, a library, a dining hall, and studio apartments where artists lived and worked. The studio apartments were leased only to artists, a few of whom were members of the organization. However, the apartments were not made available to the tenants on the basis of membership in the club or any criteria that would further the exempt purpose of the organization. The organization provided maid and switchboard services for the tenants similar to those provided to the occupants of rooms in hotels. The ruling holds that neither the leasing of the studio apartments nor the operation of the dining hall had a substantial causal relationship to the achievement of the organization's exempt purposes. Nor were these businesses carried on primarily for the convenience of the members within the meaning of section 513(a)(2) of the Code.

Rev. Rul. 76-336, 1976-2 C.B. 143, holds that an organization formed by community leaders to provide housing for students of a particular college unable to provide adequate student housing is operated exclusively for charitable purposes and qualifies for exemption under section 501(c)(3) of the Code. The organization operated the facility adjacent to the college campus and in an area where other suitable housing was not available. Only students of the college were eligible to apply for housing. The organization and the college consulted and cooperated to ensure that the needs of the college and its students were served by the operation of the facility. By providing a housing facility under these circumstances, the organization was both helping the college to fulfill its educational purposes, and aiding the students to attain an education. Therefore, the activities of the organization are advancing education.

Rev. Rul. 81-19, 1981- 1 C.B. 353, concerns an organization formed to assist a university by receiving contributions for the benefit of the university, assisting the university's academic departments in problems of financial management, and managing the operation of soft drink and food vending services as well as operating laundromat facilities on campus. Rev. Rul. 81-19 holds that these activities are an integral part of the exempt activities of the university, and the organization furthers the educational program of the university by operating facilities for the convenience of the university community. It concludes that the operation of the vending services and laundromat facilities are not unrelated trade or business under section 513 of the Code because these activities are substantially related to the organization's exempt purpose of furthering the university's educational program by aiding the university in performing its various administrative functions.

Analysis

Ruling #1:

A. Revenue Generated from Providing Student Housing

When Congress enacted the unrelated business income tax in the Revenue Act of 1950, it sought to exclude from the definition of "unrelated trade or business" activities carried on by an organization described in section 501(c)(3) primarily for the convenience of its members, students, patients, officers, or employees. As noted above, the committee reports clarified that this intended for an educational institution's income from dormitories operated for the convenience of students to be considered related income. Section 1.513-1(e) of the regulations effectuates the congressional intent by articulating that unrelated trade or business does not include the ancillary services provided for the convenience of students in connection with a residential college community. Your provision of campus housing, whether in the dormitories or temporarily in H, and related services to students, like those of the organizations described in the court cases and revenue rulings listed above, contribute importantly to your 'charitable' purpose of advancing education. Because this activity is substantially related to the purposes constituting the basis for your exemption under section 501 of the Code, it is not an unrelated trade or business within the meaning of section 513(a). Accordingly, the revenue generated from this activity does not constitute unrelated business taxable income within the meaning of section 512(a)(1).

You initially requested a ruling that revenue generated from providing housing to your faculty did not constitute unrelated business taxable income under section 512(a)(1) of the Code. However, you subsequently clarified that you do not earn revenue from such activity and have not submitted proposals for consideration. Thus, pursuant to section 8.03 of Rev. Proc. 2010-4, 2010-1 I.R.B. 122, 134, we are not ruling on any aspect of your provision of housing to faculty. As noted in the introduction of this letter, this part of PLR 200625035 is revoked.

B. Revenue Generated by use of the H

You have conceded that you operate the H as a "trade or business" and this activity is "regularly carried on" within the meaning of section 513 of the Code. You requested rulings that the income from various categories of guests be excluded from the unrelated business income tax because their use of the facility is "substantially related" to your exempt purposes within the meaning of section 1.513-1(d)(2) of the regulations. In addition, you requested rulings that the income from some categories of guests be excluded from the definition of "unrelated trade or business" because the activity is carried on primarily for the convenience of your members, students or employees within the meaning of section 513(a)(2).

Not all uses you described constitute trade or business. Specifically, guests of other departments, who do not themselves pay for their lodging, but whose costs are charged to the sponsoring department, do not result in income. For those guests, the lodging expense is a cost allocation rather than trade or business income. We do not address this issue herein.

a. Revenue from Students

Your use of the H to temporarily house students until their full-time housing becomes available is a part of your campus housing program. You provide this to students on the same basis as

full-time housing. As indicated in Ruling 1A, above, providing temporary housing for enrolled students awaiting their dormitory assignments to become available serves the same purpose as providing the long-term dormitories. Thus, revenue attributable to providing temporary lodging to your students in the H while they wait for their full-time campus housing to become available does not constitute unrelated business income within the meaning of section 512(a)(1). This ruling is affirmed.

b. Revenue from Other Paying Guests

You operate the H similar to a boutique hotel. The accommodations and rates are comparable to commercial hotels in the area. You advertise the H on your website. Rooms are available for rent by the general public. You do not limit the rental of rooms in the H to individuals affiliated with your institution or with any other educational institution located nearby. If there is a vacancy at the H, no one is denied lodging, whether or not they have any relationship to your institution. You have made various assertions for the categories of guests that purport to show that providing hotel accommodations for each is related to your exempt purposes. Although you may have shown some relatedness to you or other institutions in the area, you have not established a substantial and causal relationship between the guests' stays at the H and your tax-exempt purposes. Further, you provided no explanation how any of the various categories of paying guests came to the H other than through the general reservation system.

Accordingly, all parts of PLR 200625035 that differ from this analysis are also revoked.

Ruling #2

Revenue generated from renting rooms in the H to members of the general public constituted unrelated business taxable income under section 512(a)(1).

You provided no information that establishes your operation of the H is part of your educational program or that providing hotel accommodations to the general public contributes importantly to the accomplishment of your educational and charitable purposes. Providing hotel accommodations for the general public is a trade or business regularly carried on and is not substantially related to your exempt purposes within the meaning of section 1.513-1(d)(2) of the regulations. This part of PLR 200625035 is affirmed.

Rulings

Ruling #1

Revenue generated from providing housing for your students in your dormitories and the H does not constitute unrelated business taxable income under section 512(a)(1) of the Code.

Ruling #2

Revenue generated from renting rooms in the H to members of the general public constitutes unrelated business taxable income under section 512(a)(1). You have not established a

substantial and causal relationship for any of the categories of guests staying at the H and your tax-exempt purposes. You provided no explanation how any of the various categories of paying guests came to the H other than through the general reservation system. Accordingly, these individuals are also treated as members of the general public.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. 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. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

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.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Steve Grodnitzky
Manager, Exempt Organizations
Technical Group 1

Enclosure
Notice 437