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Person To Contact:  
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Telephone Number:

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Legend

Taxpayer =

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Dear :

This is in reply to a letter dated August 13, 2019, and supplemental correspondence requesting rulings on behalf of Taxpayer. Taxpayer has requested rulings with respect to the independent retirement living facilities described below.

FACTS:

Taxpayer is a State corporation that elected to be taxed as a real estate investment trust ("REIT") under sections 856 through 860 of the Internal Revenue Code ("Code"). Taxpayer's business primarily consists of the acquisition, financing, and owning of real property to be leased to third-party tenants in the healthcare sector. Taxpayer primarily invests in senior health care facilities such as skilled nursing

facilities, independent living, assisted living, continuing care retirement communities, and memory care facilities. Taxpayer primarily derives its income through rents from real property and in some instances, interest on mortgages secured by real property. Rents received by Taxpayer are predominantly earned through triple net lease arrangements whereby tenants bear the responsibilities for the maintenance, upkeep and operating expenses of the facilities.

### Independent Retirement Living Facilities

The independent retirement living facilities that are the subject of this ruling letter consist of a facilities located in the United States (the "Facilities"). The Facilities are not licensed health care facilities. The Facilities are marketed through brochures as "Independent Retirement Living" and require that at least one resident be at least the age of b. The marketing materials and resident leases specifically state that the Facilities do not provide any health care services. Each Facility generally offers amenities such as a common dining area, an activity room, a barber and beauty salon, guest accommodations, a large screen TV lounge, community grounds, and, in some instances, a chapel. Additionally, the hallways and common bathroom areas of the Facilities are equipped with handrails.

### The Lease Agreement

A resident of a Facility (the "Resident") enters into a lease agreement (the "Lease Agreement") for an initial term of between c days and d months and continues month-to-month thereafter. The Lease Agreement entitles the Resident to individual living quarters within a Facility in exchange for fixed monthly payments (the "Monthly Rent"). The living quarters include at least one bedroom, a kitchenette, bathroom, and living room area. Taxpayer represents that any amounts to be received by Taxpayer that are attributable to personal property leased in connection with the Facilities will not exceed 15 percent of the total rent for any taxable year attributable to both the real and personal property leased under or in connection with such lease with the meaning of section 856(d)(1)(C).

Each Lease Agreement specifically stipulates that the Resident is responsible for his or her own personal and health care needs and that the relevant facility is not licensed as a nursing or health care facility. Thus, the Resident must be capable of providing for his or her own health care and personal care needs and is responsible for the provision of such care for the duration of the Lease Agreement. Also included as part of the Monthly Rent (and not separately stated) are the Resident Services described below.

### Resident Services

The following services are provided at the Facilities and included in the Monthly Rent: (1) three daily meals plus daily snacks; (2) light housekeeping including linen service; (3) scheduled transportation to and from local destinations and group activities; (4) an emergency call system device; (5) utilities such as tap water, heat, electricity, sewer, basic cable television, and garbage collection; and (6) upon a Resident's request, hard plastic containers are provided to safely dispose of hypodermic needles and other sharp medical instruments (the "Resident Services"). The emergency call system device is a hand-held, wearable device that is operated by an unrelated third party (the "Emergency Operator"). The device connects the Resident to an agent of the Emergency Operator who will (i) confirm the location of the Resident (ii) call emergency services, roadside assistance, locksmith, or family of the Resident, and (iii) stay on the line with the Resident until the situation is resolved.

The Facilities intend to provide amenities and services to Residents for their living convenience and social purposes. The Facilities specifically do not provide a number of health care related services. They do not conduct preventative health screening, monitor the Residents' medical needs, or provide for a streamlined resident transfer program to a facility with higher health care options. Prior to move-in, the Facilities may conduct pre-admission interviews to ensure that the Residents are ambulatory and have no apparent cognitive decline that would interfere with activities of daily living. Additionally, the Facilities do not require a Resident to obtain consent from the Facility before the Resident contracts with third-parties for in-home or other health care services. They also do not provide for supervision of a Resident's oxygen equipment or require the employees on the premises to be licensed nurses. Finally, the Facilities do not keep "Do Not Resuscitate" forms on file and do not have 24-hour on-site staff to monitor the Residents. However, in the event of an emergency, on-site personnel are allowed to call 911.

### Operational Structure of Taxpayer

Currently, a wholly-owned taxable REIT subsidiary ("TRS") of Taxpayer (the "PropCo TRS") holds the Facilities. The PropCo TRS leases the Facilities to another wholly-owned TRS of Taxpayer (the "OpCo TRS"). The OpCo TRS subleases the individual residences to the Residents under the Lease Agreements. The OpCo TRS entered into a management contract with an eligible independent contractor, within the meaning of section 856(d)(9), (the "Operator") to provide the Resident Services (the "Management Contract"). Under the Management Contract, the Operator is responsible for the Resident Services, as well as staffing, managerial oversight, accounting services, information technology services, billing, collections, marketing, maintenance, advertising, rate setting (subject to the approval of Taxpayer/OpCo TRS), admissions and regulatory compliance matters.

Upon receipt of the ruling, Taxpayer intends to revoke the PropCo TRS's election to be treated as a corporation for U.S. federal income tax purposes and its TRS election. As a result of these revocations, the PropCo TRS will become a disregarded entity of Taxpayer. The OpCo TRS will assign the Lease Agreements (subleases of individual residences in the Facilities) to the PropCo TRS. The PropCo TRS and the OpCo TRS will enter into a management contract providing that the OpCo TRS will be responsible for providing the Resident Services. The OpCo TRS will subcontract the provision of the Resident Services to the Operator who will continue providing the Resident Services pursuant to the Management Contract. The PropCo TRS will collect the Monthly Rent from the Residents and remit the payment to the OpCo TRS for the Resident Services under arm's-length terms based on principles described under section 482.

### Rulings Requested

Taxpayer requests the following rulings: (1) the Facilities do not meet the definition of health care facilities under section 856(e)(6)(D)(ii); (2) the OpCo TRS is not precluded from directly or indirectly operating or managing the Facilities for purposes of section 856(l)(3)(A); and (3) the provision of services, including the Resident Services, by the Operator does not give rise to impermissible tenant service income, and will not cause any portion of the rents received by Taxpayer (through PropCo TRS as a disregarded entity of Taxpayer) to fail to qualify as rents from real property under section 856(d).

### LAW & ANALYSIS:

Section 856(c)(2) 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(c)(3) provides that at least 75 percent of a REIT's gross income must be derived from, among other sources, rents from real property.

Section 856(d)(1) provides that rents from real property include (subject to exclusions provided in section 856(d)(2)): (A) rents from interests in real property; (B) charges for services customarily furnished or rendered in connection with the rental of real property, whether or not such charges are separately stated; and (C) rent attributable to personal property leased under, or in connection with, a lease of real property, but only if the rent attributable to the personal property for the taxable year does not exceed 15 percent of the total rent for the taxable year attributable to both the real and personal property leased under, or in connection with, such lease.

Section 1.856-4(b)(1) provides that services furnished to tenants of a particular building will be considered customary if, in the geographic market in which the building is located, tenants in buildings that are of a similar class are customarily provided with the service.

Section 856(d)(2)(C) excludes impermissible tenant service income from the definition of rents from real property. Section 856(d)(7)(A) defines impermissible tenant service income to mean, with respect to any real or personal property, any amount received or accrued directly or indirectly by a REIT for services furnished or rendered by the REIT to tenants of such property, or for managing or operating such property.

Section 856(d)(7)(C)(i) 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 does not derive or receive any income or through a TRS of the REIT.

Section 856(e)(6)(D)(i) defines qualified health care property as any real property, and any personal property incident to such real property, which is a health care facility or is necessary or incidental to the use of a health care facility.

A health care facility is defined in section 856(e)(6)(D)(ii) as a hospital, nursing facility, assisted living facility, congregate care facility, qualified continuing care facility (as defined in section 7872(g)(4)), or other licensed facility which extends medical or nursing or ancillary services to patients and which, immediately before the termination, expiration, default, or breach of the lease of or mortgage secured by such facility, was operated by a provider of such services which was eligible for participation in the Medicare program under Title XVII of the Social Security Act (42 U.S.C.A. § 1395 et seq.) with respect to such facility.

Section 856(l)(1) defines TRS to mean, with respect to a REIT, a corporation (other than a REIT) if (A) such REIT directly or indirectly owns stock in such corporation, and (B) such REIT and such corporation jointly elect that such corporation shall be treated as a TRS of such REIT.

Section 856(l)(3)(A) provides that any corporation that directly or indirectly operates or manages a lodging facility or a health care facility is not a TRS. Section 856(l)(4)(B) provides that the term "health care facility" has the meaning given such term in section 856(e)(6)(D)(ii).

In Rev. Rul. 2002-38, 2002-2 C.B. 4, a REIT pays its TRS an arm's length rate to provide noncustomary services to tenants. The REIT does not separately state charges to tenants for the services. Thus, a portion of the amounts received by the REIT from tenants represents an amount received for services provided by the TRS. The TRS employees perform all of the services and the TRS pays all of the costs of providing the services. The revenue ruling concludes that the services provided to the REIT's tenants are considered to be rendered by the TRS, rather than the REIT, for purposes of section 856(d)(7)(C)(i).

The Facilities focus on providing the Residents a convenient and social living environment. While they do offer amenities and services that may be found in

congregate care health care facilities, the emphasis of the amenities and services provided at the Facilities is not the health and wellbeing of the Residents. Although the Residents are provided with shared meals and transportation to local destinations and group activities, these Resident Services are provided for convenience and to enhance the social lives of the Residents as opposed to providing a health benefit. The Facilities provide an emergency call device to Resident, however the device connects to the Emergency Operator, which is a third party unrelated to Taxpayer, PropCo TRS, OpCo TRS, and Operator. The employees of the Facilities are not licensed nurses and are not available 24 hours to monitor or assist Residents. Furthermore, the Residents are screened prior to signing the Lease Agreement to ensure that they are capable of providing for their own health care needs, but the Residents are not monitored after they move in, which suggests that the Facilities are not meant to be relied on to provide for health care needs. Considering all the facts and circumstances, the services provided at the Facilities are not focused on the health and well-being of the Residents.

The Resident Services will be provided by the Operator through a subcontract with the OpCo TRS. Taxpayer represents that the OpCo TRS will be compensated at an arm's length rate for the provision of the Resident Services. Although the PropCo TRS will collect the compensation for the Resident Services as part of the Monthly Rent, the Resident Services are not considered to be rendered by PropCo TRS or the Taxpayer for purposes of section 856(d)(7)(C)(i).

#### CONCLUSION:

Accordingly, based on the facts as represented, we rule that the Facilities do not constitute health care facilities within the meaning of section 856(e)(6)(D)(ii), and, as a result, direct or indirect operation or management of the Facilities by the OpCo TRS will not prevent the OpCo TRS from being treated as a TRS under section 856(l)(3)(A). Additionally, the provision by the Operator of the services described above, including the Resident Services that are not separately stated, will not be considered to be provided by Taxpayer and, therefore, the provision of these services will not give rise to impermissible tenant service income and will not cause any portion of the rents received by Taxpayer (through PropCo TRS as a disregarded entity of Taxpayer) to fail to qualify as rents from real property under section 856(d).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed whether Taxpayer otherwise qualifies as a REIT or whether PropCo TRS or OpCo TRS otherwise qualifies as a TRS of Taxpayer under part II of subchapter M of chapter 1 of the Code. Furthermore, no opinion is expressed as to whether the Monthly Rents otherwise qualify as rents from real property within the meaning of section 856(d). Specifically no opinion is expressed as to whether any of the services provided at the Facilities, including the Resident Services, are customary services within the meaning of section 1.856-4(b)(1).

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

Andrea M. Hoffenson

Andrea M. Hoffenson

Chief, Branch 2

Office of Associate Chief Counsel

(Financial Institutions & Products)