

- (1) The Facilities (defined below) do not meet the definition of “health care facility” under section 856(e)(6)(D)(ii);
- (2) OpCo TRS (defined below) 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 described in this letter, including the Resident Services (defined below), by Operator (defined below) does not give rise to impermissible tenant service income, and does not cause any portion of the Monthly Rents (defined below) to fail to qualify as rents from real property under section 856(d).

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”) beginning with its first taxable year ended Date 1. Taxpayer primarily invests in senior housing, post-acute communities, and outpatient medical properties in Countries. Taxpayer primarily derives its income through rents from real property within the meaning of section 856(d) and, in some instances, interest on mortgages secured by real property within the meaning of section 856(c)(3)(B).

Independent Retirement Living Facilities

The independent retirement living facilities that are the subject of this letter ruling consist of a facilities located in Country (each, a “Facility,” and collectively, the “Facilities”). The Facilities are marketed as “Independent Retirement Living” and require that at least one resident per household be at least age b. The Facilities are not licensed under state or local law as hospitals, nursing facilities, assisted living facilities, congregate care facilities, qualified continuing care facilities, or any other similar facility licensed to extend medical or nursing or ancillary services to patients. 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, guest accommodations, a large screen TV lounge, community grounds, and, in some instances, a library, a chapel, or both. Additionally, the hallways and common bathroom areas of the Facilities are generally equipped with handrails.

The Lease Agreements

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 continuing 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 under or in connection with a Lease Agreement 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 within 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. The Lease Agreement further stipulates 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.

Resident Services

The following services are provided at the Facilities and included in the Monthly Rent (*i.e.*, not separately stated) under the Lease Agreement: (1) three daily meals plus daily snacks; (2) light housekeeping including linen service; (3) limited scheduled transportation to and from local destinations and group activities; (4) a variety of social, educational, and recreational opportunities, technology classes, arts and crafts, movement activities, social storytelling, and social mixers; (5) an emergency call system device; (6) utilities such as tap water, heat, electricity, sewer, basic cable television, and garbage collection; (7) parking for Residents' cars and visitor parking for Residents' guests; and (8) upon a Resident's request, hard plastic containers to safely dispose of hypodermic needles and other sharp medical instruments (the "Resident Services"). The emergency call system is operated by an independent contractor as defined in section 856(d)(3) from whom Taxpayer itself does not derive or receive any income ("Emergency Operator"). The emergency call system device is a hand-held, wearable device that connects the Resident to an agent of Emergency Operator who will (i) confirm the location of the Resident (ii) call emergency services, roadside assistance, a locksmith, or family of the Resident, and (iii) stay on the line with the Resident until the situation is resolved.

The Facilities are intended to provide amenities and services to Residents for their living convenience and social purposes. Prior to move-in, the Facilities may interview prospective Residents to ensure they are ambulatory and have no apparent cognitive decline that would interfere with activities of daily living. The Facilities do not otherwise provide any health care related services. The Facilities 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. 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. The Facilities also do not provide for supervision of a Resident's oxygen equipment or require the employees on the premises to be licensed nurses or have any medical training. The Facilities also do not keep "Do Not Resuscitate" forms on file. In the event of an emergency, on-site personnel are allowed to call 911 and follow

instructions provided by the 911 operator. Finally, the Facilities do not have 24-hour on-site staff to monitor the Residents. The exteriors of the Facilities are equipped with lock boxes so that first responders can gain access after normal business hours.

Taxpayer represents that the services included in the Monthly Rent that are provided to the Residents, including the Resident Services, are customarily furnished or rendered to tenants of age-restricted, non-healthcare independent living facilities in the geographic markets in which the Facilities are located.

Commercial Tenants

In addition to leasing living quarters to Residents, the Facilities typically lease two to three small commercial spaces to unrelated third-party businesses (the "Commercial Tenants"). The Commercial Tenants enter into a standard lease agreement (a "Commercial Lease") that generally has an initial term of e years and will automatically renew thereafter on a month-to-month basis. The Commercial Leases provide for a fixed amount of monthly rent that the lease parties stipulate is reasonable, consistent with the fair market value of the premises, and not determined by reference to the volume or value of actual or anticipated referrals, which are prohibited under the Commercial Leases. The Commercial Leases provide for no revenue sharing arrangements or kickbacks from the Commercial Tenants to the landlord or vice versa. Per Facility, the amount of rent received from Commercial Tenants will represent less than f percent (i.e., a de minimis amount) of total rent that will be received from Residents and Commercial Tenants combined. Taxpayer represents that the rent it receives from Commercial Tenants qualifies as rents from real property for purposes of section 856(d)(1).

The Commercial Leases do not require the Commercial Tenants to provide any services or exclusively serve a Facility's Residents. The Commercial Leases provide that neither the Commercial Tenant nor any of its employees are employees of the Facility, and the Commercial Tenants agree under the Commercial Leases not to represent to any person at any time that the Commercial Tenant is an employee of the Facility, the owner of the Facility or any affiliate thereof, or that the Commercial Tenant is providing services or conducting business at the direction of the Facility. As stated in the Commercial Leases, nothing in the leases will be construed to require the Commercial Tenant, the Facility, or the landlord to make referrals of Residents or clients to one another, and the payment of any referral fees is prohibited. The Facilities exercise no control over the services provided or business conducted by the Commercial Tenant, and the Commercial Leases do not require a Commercial Tenant to share any information with the Facility as to the Commercial Tenant's customer base. The Facilities do not track the extent to which Residents or non-Residents may call or visit the leased space of a Commercial Tenant.

It is common for the Commercial Tenants to be beauty salon businesses or in-home health and personal care service providers. Taxpayer represents that health and

personal care provider tenants tend to be attracted to renting space in age-restricted independent retirement living facilities and, therefore, it is common to find such tenants in these types of facilities. The in-home health and personal care services offered by Commercial Tenants are expected to consist of (i) non-medical personal services, such as companionship and assistance with the activities of daily living (e.g., eating and personal hygiene, shopping and errands, transportation to and from doctors' visits, dog walking, etc.); (ii) medical-related home health care services, such as skilled nursing, rehabilitation therapy, and hospice care; or (iii) both. These providers generally use their leased space as office space to answer phone calls, schedule appointments, and store equipment. Some of these Commercial Tenants maintain physical therapy and other rehabilitation equipment within their leased premises and provide services relying on that equipment within the leased spaces.

As stated above, nothing in the Commercial Leases requires Commercial Tenants that provide in-home health and personal care services to exclusively serve Residents, and no formal or informal agreement or understanding requires any in-home health and personal care provider to exclusively serve the Residents of a Facility where that Commercial Tenant is leasing space. The Commercial Tenant's leased space is open to and accessible by both Residents and non-Residents who seek services from a Commercial Tenant. Taxpayer does not actively seek out Commercial Tenants who provide in-home health and personal care services. Instead, in-home health or personal care service providers tend to seek out open commercial space in age-restricted, non-healthcare independent living facilities.

Taxpayer represents that nothing in the Residents' Lease Agreements or any marketing materials provided to the Residents provides any assurances or expectations that in-home health and personal care providers are among the businesses operated by the Commercial Tenants. The presence of the Commercial Tenants is not a result of the Facilities' coordination of in-home health and personal care services in any way. Taxpayer neither tracks the percentage of Residents at a given Facility who use in-home and personal care services (including both non-medical home aide services and medical-related home health care services) nor receives such data from its Commercial Tenants; however, Taxpayer estimates that g% to h% of Residents will utilize in-home and personal care services, irrespective of whether those services are provided by a Commercial Tenant or another provider. Notwithstanding the presence of any Commercial Tenant, Residents remain free to choose any service provider they see fit to meet their needs.

Taxpayer may make information available to Residents regarding in-home health and personal care service providers located at the Facility and nearby but does not engage in marketing activities with respect to the Commercial Tenants in any way. Taxpayer does not encourage Residents to obtain any in-home services (or to choose any particular provider of such services) or otherwise facilitate the engagement of such services by Residents. Commercial Tenants must be licensed as required by applicable law, maintain their own liability insurance, and adhere to each Facility's code of conduct,

which, for example, prohibits Commercial Tenants from soliciting Residents' business door-to-door or in common areas.

Operational Structure of Taxpayer

Taxpayer and Subsidiary REIT, a subsidiary of Taxpayer that will elect to be taxed as a REIT beginning with its first taxable year ending Date 2, currently own the stock of Company 1. Taxpayer and Subsidiary REIT intend to restructure the ownership of Company 1 such that it will be wholly owned by Subsidiary REIT and treated as a qualified REIT subsidiary of Subsidiary REIT within the meaning of section 856(i)(2). Upon the completion of this restructuring, Taxpayer, through an entity disregarded for U.S. federal income tax purposes, and Subsidiary REIT, through Company 1, will hold the equity interests in Company 2, a State limited partnership. Company 2 and a number of unrelated partners own the equity interests in Company 3 ("PropCo"), a State limited partnership. Directly and through disregarded entities, PropCo is the owner of the Facilities.

PropCo leases the individual living quarters at the Facilities to the Residents under the Lease Agreements and the commercial space at the Facilities to Commercial Tenants under the Commercial Leases. Under a management contract (the "Management Contract") between PropCo and a taxable REIT subsidiary ("TRS") of Taxpayer and Subsidiary REIT ("OpCo TRS"), OpCo TRS is responsible for providing the Resident Services, as well as staffing, managerial oversight, accounting services, information technology services, billing, collections, marketing, maintenance, advertising, rate setting, leasing, and regulatory compliance matters (the "Management Services," and collectively with the Resident Services, the "Operator Services") on arm's length terms as described in section 482.

OpCo TRS entered into a management subcontract (the "Management Subcontract") with a third party in the business of providing Resident Services ("Operator"). Under the Management Subcontract, Operator provides all the Operator Services on arm's length terms. Taxpayer represents that Operator is an independent contractor as defined in section 856(d)(3) from whom Taxpayer itself does not derive or receive any income.

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.

Section 856(e)(6)(D)(ii) defines a health care facility 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 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 the services and the TRS pays all 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).

While the amenities and services the Facilities offer may be some of the amenities and services 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. Instead, the Facilities focus on providing the Residents a convenient and social living environment. 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 employees of the Facilities are not licensed nurses and are not available 24 hours per day to monitor or assist Residents. Furthermore, the Residents are interviewed prior to signing the Lease Agreement to ensure that they are capable of providing for their own health care needs. 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. The absence of nurses, other medical personnel, health screenings, monitoring of medical needs, or transfer programs also suggests that the Facilities do not have a health care focus. Moreover, the terms of the Resident Agreements place responsibility for health care on the Residents themselves. Considering all the facts and circumstances, the services provided at the Facilities are not focused on the health and wellbeing of the Residents.

While the Commercial Tenants may offer in-home health and personal care services that do place an emphasis on the health and wellbeing of the Residents, neither PropCo, Taxpayer, Subsidiary REIT, OpCo TRS, nor anyone else affiliated with the Facilities coordinates with, exercises control over, or otherwise actively supports or directs the Commercial Tenants in the provision of any in-home health and personal care services to the Residents. Further, the Commercial Tenants pay only fixed monthly rent (i.e., no referral fees) that is, on a Facility-by-Facility basis, de minimis in comparison to aggregate rents that will be received from the Residents and the Commercial Tenants. Taxpayer represents that it does not actively seek out (or seek to replace) Commercial Tenants that provide in-home health and personal care services. Rather, the demographic profile of the Residents attracts the Commercial Tenants to rent space in the Facilities. The Commercial Tenants' businesses are open to and reasonably accessible by the general public. However, given the demographic profile of the Residents and location of the businesses, the Residents are more likely than the

general public to procure services from the Commercial Tenants. Taxpayer represents that the presence of in-home health and personal care service providers as tenants is common in the independent retirement living industry. Taxpayer further represents that it is not marketing health-related Commercial Tenants to its existing or prospective Residents. Under these circumstances the mere presence of the Commercial Tenants that provide in-home health and personal care services does not cause the Facilities to be treated as furnishing services and amenities with an emphasis on the health and wellbeing of the Residents.

The Resident Services are provided by Operator through a subcontract with OpCo TRS. Taxpayer represents that OpCo TRS will be compensated at an arm's length rate for the provision of the Operator Services, including Resident Services. Taxpayer further represents Operator will be an independent contractor as defined in section 856(d)(3), compensated on arm's length terms, from whom Taxpayer itself does not derive or receive any income. Although PropCo will collect the compensation for the Resident Services as part of the Monthly Rent, the Resident Services will not be considered rendered by PropCo or Taxpayer for purposes of section 856(d)(7)(C)(i). The Facilities will provide an emergency call device to the Residents; however, the device will connect to Emergency Operator, which will also be also an independent contractor as defined in section 856(d)(3) from whom Taxpayer itself does not derive or receive any income.

CONCLUSION:

Accordingly, based on the facts provided and representations made, we rule that:

- (1) The Facilities do not meet the definition of "health care facility" under section 856(e)(6)(D)(ii);
- (2) Direct or indirect operation or management of the Facilities by OpCo TRS does not prevent OpCo TRS from being treated as a TRS for purposes of section 856(l)(3)(A); and
- (3) The provision by Operator and Emergency Operator of the services described above, including the Resident Services for which fees are not separately stated, does not give rise to impermissible tenant service income and does not cause any portion of the Monthly Rents 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 or implied (1) whether Taxpayer or Subsidiary REIT otherwise qualifies as a REIT, (2) whether OpCo TRS otherwise qualifies as a TRS of Taxpayer and Subsidiary REIT under part II of subchapter M of chapter 1 of the Code, (3) whether any services provided at the

Facilities are customary services within the meaning of section 1.856-4(b)(1), or (4) whether the Monthly Rents otherwise qualify as rents from real property within the meaning of section 856(d).

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,

Jason D. Kristall
Chief, Branch 3
Office of the Associate Chief Counsel
(Financial Institutions & Products)

cc: