**Internal Revenue Service**

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Washington, DC 20224

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Date:
April 08, 2008

**Legend:**

Taxpayer =

State A =

LP =

a =

Property =

City A =

Dear :

This is in reply to a letter dated December 5, 2007, requesting a ruling on behalf of Taxpayer. You requested a ruling that the generation and furnishing of electricity and steam to tenants at Property will not cause rental income from the Property to be treated as other than "rents from real property" and any amounts derived from the furnishing of electricity and steam to tenants of the Property will qualify as "rents from real property", under section 856(d) of the Internal Revenue Code.

**Facts:**

Taxpayer is a State A real estate investment trust (REIT) that has elected under section 856(c) to be treated as a REIT for federal income tax purposes. Taxpayer is the managing general partner of LP and owns approximately a percent of the outstanding common units of LP. LP, through business entities classified as partnerships or disregarded entities for federal income tax purposes (collectively, the “Owners”), owns and operates numerous real properties throughout the United States, including the Property, which is leased to office and commercial tenants.

The Owners currently acquire all of the electricity and steam needed for the tenants and common areas of the Property from the public utility companies that serve City A. Taxpayer represents that, as is customary in City A, the Owners submeter electricity and steam for some tenants and charge other tenants a fixed cost per square foot as provided in their leases. The electricity and steam charges may either be a component of the rent payment or separately stated.

Taxpayer wishes to restructure the way in which electricity is furnished to tenants of the Property. Taxpayer proposes to install an electrical generating unit at the Property to be used to generate electricity for use by the tenants of the Property. The Owners will engage an independent service provider to manage the generation of electricity and maintain the generating unit and the building engineers responsible for the mechanical equipment at the Property will also be responsible for the generating unit on a 24/7 basis. During the peak load period (8 A.M. – 8 P.M., Monday – Friday), the generating unit will provide a major portion of the electricity furnished to tenants and used by the Property generally. The balance of electricity needs will be provided by the utility companies.

The generating unit will also produce waste heat that can be supplied to tenants as steam. Tenants will be billed for electricity and steam furnished from the generating unit at the same rates and in the same manner as currently done for electricity and steam furnished by the utility companies. Taxpayer represents that the electricity and steam generated by the generating unit will be used solely by the tenants of the Property and by the Owners in the operation of the Property.

Taxpayer represents that the utility restructuring is intended to ensure that the Property has a secure source of electricity and that tenants have sufficient power during periods of peak demand and in the event of a transmission failure. It is intended to decrease the Property’s dependence on the regional power grid and to achieve the environmental benefits associated with on-site electricity generation.

**Law and Analysis:**

Section 856(c)(2) provides a REIT must derive at least 95 percent of its gross income from certain enumerated sources, including dividend, interest, and rents from real property.

Section 856(c)(3) provides that a REIT must derive at least 75 percent of its gross income from certain enumerated real estate sources, including rents from real property and qualified temporary investment income.

Under section 1.856-3(g) of the Income Tax Regulations, a REIT that is a partner in a partnership is deemed to own its proportionate share of each of the assets of the partnership and to be entitled to the income of the partnership attributable to that share. For purposes of section 856, the interest of a partner in the partnership's assets is determined in accordance with the partner's capital interest in the partnership.

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 tax year attributable to both the real and personal property leased under, or in connection with, the lease.

Section 1.856-4(b)(1) provides that, for purposes of sections 856(c)(2) and (c)(3), the term "rents from real property" includes charges for services customarily furnished or rendered in connection with the rental of real property, whether or not the charges are separately stated. Services rendered to tenants of a particular building will be considered customary if, in the geographic market in which the building is located, tenants in buildings of a similar class are customarily provided with the service. In particular geographic areas where it is customary to furnish electricity or other utilities to tenants in buildings of a particular class, the submetering of those utilities to tenants in the buildings will be considered a customary service.

Section 856(d)(2)(C) provides that any impermissible tenant service income is excluded 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 the REIT for services furnished or rendered by the REIT to tenants at the property, or for managing or operating the property.

Section 856(d)(7)(B) provides that if the amount of impermissible tenant service income exceeds one percent of all amounts received or accrued during the tax year directly or indirectly by the REIT with respect to the property, the impermissible tenant service income of the REIT will include all of the amounts received or accrued with respect to the property. Section 856(d)(7)(D) provides that the amounts treated as received by a REIT for any impermissible tenant service shall not be less than 150 percent of the direct cost of the REIT in furnishing or rendering the service.

Section 856(d)(7)(C) provides certain exclusions from impermissible tenant service income. Section 856(d)(7)(C) provides that for purposes of section 856(d)(7)(A), services furnished or rendered, or management or operation provided, through an independent contractor from whom the REIT does not derive or receive any income shall not be treated as furnished, rendered, or provided by the REIT, and there shall not be taken into account any amount which would be excluded from unrelated business taxable income under section 512(b)(3) if received by an organization described in section 511(a)(2).

Section 512(b)(3) provides, in part, that there shall be excluded from the computation of unrelated business taxable income all rents from real property and all 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, determined at the time the personal property is placed in service.

Section 1.512(b)-1(c)(5) 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 his 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, and the collection of trash are not considered as services rendered to the occupant.

In this case, the Owners are providing electricity and steam solely for the use of the Property's tenants and for the building itself. Taxpayer represents that this is a customary service provided in commercial office buildings in City A. Under section 1.512(b)-1(c)(5), the furnishing of heat and light are not considered services rendered to the occupant and therefore will not cause amounts received from tenants for those utility services to be treated as impermissible tenant service income under sections 856(d)(2)(C) and 856(d)(7). Accordingly, the generation and furnishing of electricity and steam to tenants in the manner described above will not cause income from the Property to be treated as other than "rents from real property" under section 856(d), and any amounts derived from the furnishing of electricity and steam to the tenants of the Property, as provided above, will qualify as "rents from real property" under section 856(d).

Except as specifically ruled upon above, no opinion is expressed concerning any federal income tax consequences relating to the facts herein under any other provision of the Code. Specifically, we do not rule whether otherwise qualifies as a REIT under part II of subchapter M of Chapter 1 of the Code. Also, no opinion is rendered concerning whether Taxpayer's method of allocating the cost of electricity and steam to tenants in City A is customary for purposes of section 1.856-4(b)(1).

This ruling is directed only to the taxpayer requesting it. Taxpayer should attach a copy of this ruling to each tax return to which it applies. Section 6110(k)(3) of the Code provides that this ruling may not be used or cited as precedent.

Sincerely,

Thomas m. Preston
Thomas M. Preston
Senior Counsel, Branch 2
Office of Associate Chief Counsel
(Financial Institutions & Products)