INTERNAL REVENUE SERVICE
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CASE-MIS No.: TAM-T-105599-15

Director, Exempt Organizations Examinations

Through: Program Manager, Exempt Organizations Examinations
Financial Investigations Unit 7733

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification No
Year(s) Involved:
Date of Conference:

LEGEND:

M =

N =

P =

ISSUE(S):

1) Whether the operation of the P is substantially related to M's exempt purpose within the meaning of § 513 of the Internal Revenue Code.

2) Whether the fees paid to M by P vendors constitute rents from real property within the meaning of § 512(b)(3)(A)(i).

CONCLUSION(S):

1) The operation of the P is not substantially related to M's exempt purpose within the meaning of § 513.

2) The fees paid by P vendors do not constitute rents from real property within the meaning of § 512(b)(3)(A)(i).

FACTS:

M is organized as a nonprofit public benefit corporation under State law. M is recognized by the Internal Revenue Service as an organization described in § 501(c)(3), and is not considered to be a private foundation within the meaning of § 509.

M's articles of incorporation provide that M is organized for the specific purpose of developing and maintaining an alumni association for N and providing financial and civic support for the benefit of N, and that it shall not engage in activities which themselves are not in furtherance of such educational and charitable purpose. N is a public two-year community college, serving a predominantly low-income community. Nearly 70 percent of N's students are Hispanic.

M's sole voting member is the community college district that comprises N. The district is a political subdivision of the State. Under M's bylaws, the president of the district has the right to designate two of M's ten directors, to approve the election of all directors, and to approve certain major actions by the board of directors.

Aside from the operation of the P (discussed below), M funds scholarships and other financial aid for the students of N. In addition, M provides direct financial support to N for the enhancement of N's facilities, such as by providing funds to purchase a computer room in the library and to maintain the football field. M publishes a bi-annual alumni newsletter, and, in conjunction with N, conducts several annual ceremonies and social events at which former students, graduates, community leaders, faculty, and staff are recognized and afforded opportunities to interact.

While M encourages support from graduates of N, it derives substantially all of its revenue from the operation of a weekly event known as the P. The P is held in the parking areas of N's campus every Saturday and Sunday year round. N allows M to use its grounds for the P, including the use of parking lots, rest rooms, and utilities. M used the grounds without charge for two of the three years under examination.

The P features vendors offering arts and crafts, entertainment, a farmer's market, and refreshment booths. The P is open to the general public free of charge. According to a survey conducted by M, the majority of visitors to the P are age 55 and older.

Persons wishing to sell merchandise at the P must submit a "vendor space application." According to the "monthly vendor application procedures," an applicant must pay a uniform "application fee" and, if the application is accepted, a monthly "space fee" which varies according to the "season" and the size of the assigned space. If a vendor fails to occupy his or her usual space by a certain time, that space is leased to a "standby" vendor based on a lottery system.

Any vendor who fails to make a space fee payment when it is due is placed in probationary status. In that event, the vendor must participate in the P through a "standby line" for four consecutive weekends. If the probationary period is completed successfully, the vendor may regain "monthly vendor" status by paying a reinstatement fee.

As part of the application process, a prospective vendor must read, and agree to abide by, the general principles and rules and regulations set forth in the "vendor rules and regulations." The final paragraph of the general principles states:

> The acceptance and use of any selling space at the P constitutes an agreement by any and all vendors (whether monthly or standby) and all persons helping or working with such vendor to comply with all of these vendor regulations as well as any and all state and federal laws.

Part 4 of the rules and regulations pertains to "space assignments." Among its provisions are the following:

B. Selling spaces are marked by number and/or letters painted on the ground in white paint. Vendor's vehicles and/or merchandise must remain within space boundaries and behind the visible white line. Vendors are not permitted to conduct business outside their assigned spaces.

* * * * *

E. Vendors do not have any ownership rights to a selling space nor do they have any seniority status.... Vendor's status at the P is that of a seller of merchandise and/or services, and not as a tenant, licensee, or other form of permissive user.

Vendors provide their own tents, booths, and equipment, and must timely assemble and disassemble them with their own labor or that of their own contractors.

The P website provides a comprehensive listing of the vendors. Each listing includes the business name of the vendor, merchandise category, merchandise description, booth number (location), vendor's website, phone number, photo, and a link to "email this vendor."

An ATM machine is on site for customer use during the P. M has entered into an ATM placement agreement with an ATM provider under which the provider agrees to place an ATM at a location mutually agreed to with M. The ATM remains the property of the provider. M agrees that the ATM will at all times remain available for use by customers during the P's normal business hours. M receives $1.50 for each transaction made on the ATM. M authorizes the provider to surcharge $3.00 per transaction. Under the agreement, M is required to provide and maintain, at its own expense, a business telephone line and operating electrical power outlet at the ATM site.

M operates and manages the P through its own officers, employees, and agents. It employs a full-time manager and executive assistant to oversee the P. In addition:

- M's executive director meets with vendors and decides the space allocation for the vendors.
- The P manager oversees vendor needs and requests.
- The P college liaison manages the maintenance of the P premises with regards to cleanliness, safety and upkeep, parking lots, sidewalks, restrooms, and golf carts, and also supervises automobile parking and addresses traffic control problems.
- The information liaison staffs the information booth and—
    - Answers questions about the P and gives directions and other information;
    - Assists in daily vendor assignments, collection of money, and box office reports;
    - Resupplies and maintains the customer information rack;
    - Maintains the restroom maintenance checklist;
    - Performs activities for P staff and shuttle drivers; and
    - Exchanges P gift certificates for cash to vendors.
- The P crew leader supervises and patrols assigned lot areas for parking and traffic control, and takes part in the setting up of banners, signs, barricades, cones, trash pickup, traffic and parking control, customer relations, and clean-up of grounds and restrooms.

- The shuttle/work cart driver operates the shuttle cart or work cart to transport passengers, supplies, and merchandise.

M owns several golf carts that are used by employees to tend to bathrooms, remove trash, and conduct routine maintenance on the P grounds. M also owns several shuttles that are used to carry elderly, handicapped, and other P patrons to and from the parking areas.

N and M have entered into a memorandum of understanding for the purpose of providing indemnification to M in order to ensure that M continues to provide critical contributions and donations to N. Specifically, N agrees to indemnify, defend, and hold harmless M, its officers, agents, and employees from any liabilities, attorney's fees, and costs arising as a consequence of any alleged injury or damage caused by any work or improvements provided by M to N directly or as a result of contributions or donations made by M to N. Nevertheless, M shall remain responsible and liable for injuries or damages caused by M's own operations such as the P.

LAW AND ANALYSIS:

Section 501(a) exempts from federal income tax organizations described in § 501(c).

Section 501(c)(3) describes organizations organized and operated exclusively for charitable and other specified exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 511(a)(1) imposes a tax for each taxable year on the unrelated business taxable income of every organization described in § 501(c).

Section 512(a)(1) provides that the term "unrelated business taxable income" means the gross income derived by any organization from any unrelated trade or business regularly carried on by it, less the deductions allowed by Chapter 1 which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

Section 512(b)(3)(A)(i) excludes from unrelated business taxable income all rents from real property.

Section 513(a) provides that the term "unrelated trade or business" means, in the case of any organization subject to the tax imposed by § 511, 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 its charitable, educational, or other purpose or function constituting the basis for its exemption under § 501.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that, in order to be exempt as an organization described in § 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section.

Section 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of the exempt purposes specified in § 501(c)(3). 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 1.501(c)(3)-1(d)(1)(i) includes "charitable" among the list of purposes for which an organization described in § 501(c)(3) may be organized and operated.

Section 1.501(c)(3)-1(d)(2) provides that the term "charitable" is used in § 501(c)(3) in its generally accepted legal sense, and includes the advancement of education, erection or maintenance of public buildings, monuments, or works, and lessening of the burdens of government.

Section 1.512(b)-1(c)(2)(i) provides that, for taxable years beginning after December 31, 1969, rents from property described in subdivision (ii) of this subparagraph, and the deductions directly connected therewith, shall be excluded in computing unrelated business taxable income.

Section 1.512(b)-1(c)(2)(ii)(a) provides that the rents which are excluded from unrelated business taxable income under § 512(b)(3)(A) and this paragraph include all rents from real property.

Section 1.512(b)-1(c)(5) provides that, for purposes of this paragraph, 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, does 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, the collection of trash, etc., are not considered as services rendered to the occupant.

Section 1.513-1(a) provides that the term "unrelated business taxable income" means the gross income derived by an organization from any unrelated trade or business regularly carried on by it, less the deductions and subject to the modifications provided in § 512. Section 513 specifies, with certain exceptions, that the phrase "unrelated trade or business" means, in the case of an organization subject to the tax imposed by § 511, 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 its charitable, educational, or other purpose or function constituting the basis for its exemption under § 501. Therefore, unless one of the specific exceptions of § 512 or 513 is applicable, gross income of an exempt organization subject to the tax imposed by § 511 is includible in the computation of unrelated business taxable income if: (1) it is income from a 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) provides that, for purposes of § 513, the term "trade or business" has the same meaning it has in § 162, and generally includes any activity carried on for the production of income from the sale of goods or performance of services.

Section 1.513-1(c)(1) provides that, in determining whether trade or business from which a particular amount of gross income derives is "regularly carried on" within the meaning of § 512, 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. This requirement must be applied in light of the purpose of the unrelated business income tax to place exempt organization business activities upon the same tax basis as the nonexempt business endeavors with which they compete. Hence, 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(c)(2) provides that the conduct of year-round business activities for one day each week would constitute the regular carrying on of a trade or business. Thus, the operation of a commercial parking lot on Saturday of each week would be the regular conduct of a trade or business.

Section 1.513-1(d)(1) provides that gross income derives from "unrelated trade or business" within the meaning of § 513(a), if the conduct of the trade or business which produces the income is not substantially related (other than through the production of funds) to the purposes for which exemption is granted. The presence of this requirement necessitates an examination of the relationship between the business activities which generate the particular income in question—the activities, that is, of producing or distributing the goods or performing the services involved—and the accomplishment of the organization's exempt purposes.

Section 1.513-1(d)(2) provides that trade or business is "related" to exempt purposes, in the relevant sense, only where the conduct of the business activities has causal relationship to the achievement of exempt purposes (other than through the production of income); and it is "substantially related," for purposes of § 513, only if the causal relationship is a substantial one. Thus, for the conduct of trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, 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. Where the production or distribution of the goods or the performance of the services does not contribute importantly to the accomplishment of the exempt purposes of an organization, the income from the sale of the goods or the performance of the services does not derive from the conduct of related trade or business. Whether activities productive of gross income contribute importantly to the accomplishment of any purpose for which an organization is granted exemption depends in each case upon the facts and circumstances involved.

Rev. Rul. 59-310, 1959-2 C.B. 146, concerns an organization that was formed to establish, maintain, and operate a public swimming pool, playground, and other recreational facilities for the children and other residents of the community. Residents of the community making use of the facilities consist principally of low-income groups who are unable to pay the cost of privately sponsored recreation facilities for themselves and their children. The funds of the association are raised by public subscription with the exception of small amounts derived from nominal charges made for admission to the swimming pool. Funds are used to pay for the cost of construction of facilities and for operating expenses. The ruling concludes that, insofar as the property and its uses are dedicated to members of the general public of the community and are charitable in that they serve a generally recognized public purpose which tends to lessen the burdens of government, the organization is exclusively charitable within the meaning of § 501(c)(3).

Rev. Rul. 67-218, 1967-2 C.B. 213, concerns an organization, subject to the tax imposed by § 511, that holds title to a pipeline system consisting of right-of-way interests in land, pipelines buried in the ground, pumping stations, equipment, and other appurtenant property. The organization leases the system to an operating company and collects rents therefrom. As to whether the income derived from the lease of the pipeline system is rent within the exception provided by § 512(b)(3), it is reasoned that the easement giving right-of-way interests in the land constitutes real property. Consequently, it is held that the income derived from a lease of the pipeline system constitutes rent from real property (including personal property leased with the real property) within the meaning of § 512(b)(3).

Rev. Rul. 69-178, 1969-1 C.B. 158, concerns an organization that owns a meeting hall and that permits its members and outside individuals and groups to use the hall for a fee. The individuals or groups normally use the facilities for a single afternoon or evening, but, at most, for periods of two or three days. The agreement to use the facilities is usually verbal, and only utilities and janitorial services are provided. Since the charges in this case are made for the use and occupancy of space in real property and only utilities and janitorial services are provided, it is held that the receipts constitute rents from real property excludable from unrelated business taxable income under § 512(b)(3). The fact that the use is only for short periods of time does not destroy the character of the receipts.

Rev. Rul. 75-198, 1975-1 C.B. 157, concerns an organization formed to serve the recreational, intellectual, social, physical, and health needs of senior citizens, primarily age 65 and over, in a particular community. The organization has established a service center to provide information, referral, and counseling services relating to health care, housing, education, finances, and employment. The center provides recreational activities such as dances, picnics, and card games. It is used as a meeting place where senior citizens can just sit and talk. All recreational facilities are uniquely suited to the needs of the elderly. The ruling states that the satisfaction of the special needs of the elderly (including suitable housing, physical and mental health care, civic, cultural, and recreational activities, and an overall environment conducive to dignity and independence, all specially designed to meet the needs of the aged) contributes to the prevention and elimination of the causes of the unique forms of "distress" to which the aged, as a class, are highly susceptible and may, in the proper context, constitute charitable purposes or functions even though direct financial assistance in the sense of relief of poverty may not be involved. The ruling concludes that the organization relieves the distress of the elderly by providing them with specialized recreational activities, and by counseling them on health care, housing, financial security, education,

and employment. Accordingly, the organization is operated exclusively for charitable purposes within the meaning of § 501(c)(3).

Rev. Rul. 77-246, 1977-2 C.B. 190, concerns an organization formed for the purpose of providing low cost transportation services to senior citizens and handicapped persons of a particular community. The organization owns and operates a bus which makes frequent daily trips to transport senior citizens and handicapped persons to downtown shopping areas and medical facilities. Public transportation is otherwise unavailable or inadequate for these members of the community, who must be able to show proof of age or handicap. The ruling recognizes that the elderly and the handicapped, because of advanced age or disability, encounter forms of distress aside from financial considerations, and concludes that providing the elderly and the handicapped with necessary transportation within the community is an activity directed toward meeting the special needs of these charitable classes of individuals.

Rev. Rul. 80-297, 1980-2 C.B. 196, concerns a school that is exempt from federal income tax under § 501(c)(3). The school's facilities include tennis courts and dressing rooms which are used in the school's educational programs during the regular academic year. The ruling posits two situations. In *Situation 1*, the school operates a tennis club for ten weeks during the summer. For a fee, the public is invited to join the club and use the school's tennis courts and dressing rooms during designated periods. Two employees of the school's athletic department conduct the affairs of the club, including collecting membership fees and scheduling court time. The net income of the club is used for the exempt purposes of the school. In *Situation 2*, the school makes the facilities available to an unrelated individual for ten weeks at a fixed fee which does not depend, in whole or in part, on the income or profits derived from the leased property. The individual forms a tennis club and hires employees to administer the affairs of the club. Under these circumstances, it is determined that furnishing tennis facilities in the manner described does not have a substantial causal relationship to the achievement of the school's exempt educational purpose. Thus, the school's furnishing of its tennis facilities in both situations is unrelated trade or business under § 513. Furthermore, in *Situation 1*, the school furnishes more than just its facilities. It operates the tennis club through its own employees, who perform substantial services for the participants in the tennis club. Accordingly, income from the school's furnishing of its tennis facilities through the operation of a tennis club in the manner described is not excluded from unrelated business taxable income as rents from real property under § 512(b)(3) and § 1.512(b)-1(c)(5). In *Situation 2*, on the other hand, the school furnishes its tennis facilities to an unrelated individual without services for a fee that does not depend in whole or in part on the income or profits derived from the leased property. Accordingly,

income from the school's furnishing of its tennis facilities through an individual operator is excluded from unrelated business taxable income as rents from real property under § 512(b)(3) and § 1.512(b)-1(c)(5).

Rev. Rul. 80-298, 1980-2 C.B. 197, concerns a university that is exempt from tax under § 501(c)(3). The university's facilities include a stadium that the university uses in its physical education program and intramural and intercollegiate sports program. In addition, for a fixed fee, the university permits a professional football team to use the stadium for practice during several months of the year. Under the lease agreement with the professional football team, in addition to heat, light, and water, the university is responsible for maintaining the playing surface and all other grounds maintenance. It also provides dressing room, linen, and stadium security services for the team. Security services include crowd and traffic control, guarding the stadium, and maintaining the privacy of practice sessions. Under these circumstances, it was determined that the lease of the stadium to the professional football team in the manner described is a trade or business, regularly carried on, that does not have a substantial causal relationship to the achievement of the university's exempt purposes. Accordingly, it is held that the leasing of the stadium is an unrelated trade or business under § 513. Furthermore, by providing extensive grounds and playing field maintenance, dressing room linens, and stadium and dressing rooms pursuant to the lease, the university is furnishing substantial services for the convenience of the lessee that go beyond those usually rendered in connection with the rental of space for occupancy only. Accordingly, income from the university's leasing of its stadium to a professional football team is not excluded from unrelated business taxable income as rents from real property under § 512(b)(3) and § 1.512(b)-1(c)(5).

Rev. Rul. 85-2, 1985-1 C.B. 178, concerns an organization that was created and is operated for the sole purpose of providing legal counsel and training to volunteers who serve as guardians ad litem in juvenile court dependency and deprivation proceedings. The law of the state in which the organization is incorporated authorizes, and the local court's rules of practice require, the appointment of a guardian ad litem to represent a child's interest in a proceeding relating to child abuse. For several years prior to the implementation of the volunteer program, the court appointed and paid attorneys to serve as guardians ad litem. The court was experiencing problems in the appointment of attorneys and decided to initiate the volunteer program. Under these circumstances, the ruling holds that the organization qualifies for exemption under § 501(c)(3) because its activities lessen the burdens of government within the meaning of § 1.501(c)(3)-1(d)(2). A determination of whether an organization is lessening the burdens of government requires consideration of whether the organization's activities are activities

that a governmental unit considers to be its burdens, and whether such activities actually "lessen" such governmental burden. To determine whether an activity is a burden of government, the question to be answered is whether there is an objective manifestation by the government that it considers such activity to be part of its burden. The fact that an organization is engaged in an activity that is sometimes undertaken by the government is insufficient to establish a burden of government. Similarly, the fact that the government or an official of the government expresses approval of an organization or its activities is also not sufficient to establish that the organization is lessening the burdens of government. To determine whether the organization is actually lessening the burdens of government, all of the relevant facts and circumstances must be considered. A favorable working relationship between the government and the organization is strong evidence that the organization is actually lessening the burdens of the government.

In Living Faith v. Comm'r, 950 F.2d 365 (7th Cir. 1991), a nonprofit organization that operates restaurants and health food stores in accordance with the doctrines of the Seventh-day Adventist Church appealed the decision of the Tax Court which had held that the organization operated for a substantial commercial purpose (considering such factors as the particular manner in which an organization's activities are conducted, the commercial hue of the activities, competition with commercial firms, and the existence and amount of annual or accumulated profits) and, thus, did not qualify for exemption under § 501(c)(3). On appeal, the organization argued that the Tax Court had relied unduly on an analysis of the organization's activities and had given insufficient weight to assertions of religious purpose made in good faith on behalf of the organization. The organization asserted that good health is an especially important component of the Seventh-day Adventist Church, and that its restaurant and health food store operation furthers this exempt purpose. In affirming the decision of the Tax Court, the appeals court answered that, while an organization's good faith assertion of an exempt purpose is relevant to the analysis of tax-exempt status, such assertions are not self-justifying and cannot be dispositive. Rather, an organization's purposes may be inferred from its manner of operations. Thus, while keeping in mind the organization's good faith assertion of a religious purpose, the court went on to examine the organization's activities and manner of operations and concluded that the organization operates with a substantial commercial purpose, and is therefore not entitled to § 501(c)(3) tax-exempt status.

Issue 1: Whether the operation of the P is substantially related to M's exempt purpose within the meaning of § 513.

M is recognized as exempt from federal income tax as an organization described in § 501(c)(3). Section 511(a) imposes a tax on the unrelated business taxable income of organizations described in § 501(c). Section 512(a) provides that the term "unrelated business taxable income" means the gross income derived by an organization from an unrelated trade or business (as defined in § 513) regularly carried on by it, less the deductions allowed, computed with the modifications provided in § 512(b). Section 513(a) provides that the term "unrelated trade or business" means any trade or business the conduct of which is not substantially related (aside from the need of such organization for income) to the exercise or performance by such organization of its charitable, educational, or other purpose constituting the basis for its exemption under § 501.

Unless one of the specific exceptions of § 512 or 513 applies, gross income of an exempt organization is includible in the computation of unrelated business taxable income if: (1) it is income from a 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.

The Examinations agent takes the position that the operation of the P is a trade or business, regularly carried on, that is not substantially related to the performance of M's exempt functions. M, in turn, does not dispute that the P is a trade or business that is regularly carried on. M contends, however, that the operation of the P is substantially related to its exempt purposes in three respects.

Recruiting

First, M states that the P contributes importantly to its exempt purposes by drawing potential student recruits and donors to the N campus, thereby serving to develop civic support for the benefit of N and to endear N to its alumni and others as potential volunteers, contributors, and supporters.

However, as the court in Living Faith, Inc. v. Comm'r observed, a merely speculative assertion that an activity is in furtherance of exempt purposes is neither self-justifying nor dispositive, and that an organization's purposes may be inferred from its activities and manner of operations. Significantly, we find nothing on the P website or in advertisements of the P that does anything more than mention that the funds raised at the P are used to provide student scholarships and to fund other programs and projects at N. Thus, aside from crediting the P with generating funds, M's own communications provide little support for its assertions that public attendance at the P serves to "develop

civic support" (other than funding), "increase the size of the student population interested in N," or "endear the College to its alumni and others."

Even if we were to grant the possibility of a positive correlation between the P and an increase in admission of students to N or in the terms of endearment among alumni, M has made no showing that such correlation (as opposed to the mere raising of additional funds by the operation of the P) contributes importantly or is substantially related to its exempt purpose of developing and maintaining an alumni association for N and providing financial and civic support for the benefit of N

Lessening the Burdens of Government

Second, M states that the P lessens the burdens of government because N is a governmental entity. Revenue Ruling 85-2 applies a two-part test to determine whether an organization is lessening the burdens of government. First, the organization must perform an activity that the governmental unit itself considers to be a governmental burden. Second, such activity must actually lessen the burden of the governmental unit.

Applying the analysis and factors discussed in Rev. Rul. 85-2, we do not find that N considers the P to be its burden. M maintains that N's memorandum of understanding with M as to the conduct of the P on the N campus reflects an objective manifestation by N that it considers the operation of the P to be its burden. M does not explain, and we fail to see, how that memorandum – essentially, an indemnification agreement – conveys that N considers the P to be its burden. Further, N does not control M. The president of the community college district that comprises N may appoint only two of M's ten directors, and has approval rights over only certain actions taken by the board. In addition, N takes no part in the operation of the P. Moreover, unlike the situation in Rev. Rul. 85-2 in which the organization assumed responsibility for an activity previously conducted by, and required of, the governmental unit, N has never engaged in the operation of a P. The P is not an activity required by N or the community college district. Finally, M receives no funding from N. The mere fact that M expends its earnings from the P in support of N does not establish the operation of the P as a governmental burden.

M states that the P furthers a charitable purpose like the operation of the public swimming pool, playground, and recreation facilities described in Rev. Rul. 59-310. In that ruling, an organization that was formed to establish, maintain, and operate recreational facilities for the children and other residents of the community – particularly those residents who are unable to pay the cost of privately sponsored recreation facilities – was found to be charitable within the meaning of § 501(c)(3) insofar as the

property and its uses are dedicated to members of the general public and serve a generally recognized public purpose which tends to lessen the burdens of government. While government commonly provides public swimming pools, playgrounds, and other recreation facilities for its residents at taxpayer expense, such that an organization which provides such facilities from its own funds can be said to lessen the burdens of government, a sales event, like the P, does not have the characteristics of those public services or facilities that are normally the burden of government.

Relieving the distress of the elderly

Finally, M states that the P is substantially related to M's exempt purpose because the P serves the charitable purpose of relieving the distress of the elderly. M has conducted a survey that shows that a majority of the visitors to the P are age 55 and over. M cites Rev. Rul. 77-246 for the proposition that "the elderly and the handicapped, because of advanced age or disability, encounter forms of distress aside from financial considerations." M maintains that the P serves the area's elderly population as a meeting place for social purposes where older residents of the community and visitors may meet and congregate. M states that the entertainment and musical performances that occur at the P further the charitable purpose of relieving the distress of the elderly.

The organization described in Rev. Rul. 77-246 is organized and operated exclusively for the charitable purpose of relieving the distress of the elderly. By providing necessary transportation for the elderly and handicapped of the community, transportation that otherwise would be unavailable or inadequate, the organization described in the revenue ruling is clearly engaged in activities that meet a special need of the elderly and disabled. By contrast, M has failed to demonstrate that the activities of the P are directed toward meeting any special needs of the elderly. M fails to identify any "special need" of the elderly that the P is supposed to address. For instance, M does not claim that, absent the P, elderly members of the community would suffer from social isolation. Although elderly persons may choose to socialize at the P, there is no indication that the P is conducted for their particular benefit or to serve their particular needs. The fact that the elderly find the P conducive to socializing is insufficient to establish a substantial causal relationship between conduct of the P and the now asserted purpose of relieving the distress of the elderly. At most, the relationship is both an accidental and incidental consequence of the P's activities. Insofar as M would have us regard the P as a social meeting place for the elderly, the analysis in Rev. Rul. 75-198 is instructive. That ruling concerned a senior center that was formed to serve the specific recreational, intellectual, social, physical, and health needs of the elderly. It provides specialized recreational activities and counseling in a facility uniquely suited to the needs of the elderly. By contrast, the activities at the P that M claims relieve the

distress of the elderly – the parking lot shuttles and the entertainment programs – are not specifically tailored to the needs of the elderly, but are available to anyone in attendance. Moreover, the organization in Rev. Rul. 75-198 not only served as a meeting place for the elderly, but also provided information and counseling services for the elderly. We are unaware of any activities at the P that are specifically directed at serving the needs of the elderly.

For the conduct of the P to be substantially related to M's exempt purposes, it must contribute importantly to those purposes *other than through the production of income* [emphasis added]. Section 1.513-1(d)(2). While the operation of the P produces income that enables M to accomplish its exempt purposes, M has not shown that the operation of the P otherwise contributes importantly to an exempt purpose. Consequently, we conclude that the operation of the P is not substantially related to M's exempt purpose, but is, instead, an unrelated trade or business within the meaning of § 513.

Issue 2: Whether the fees paid to M by P vendors constitute rents from real property within the meaning of § 512(b)(3)(A)(i).

Having concluded that the operation of the P is an unrelated trade or business within the meaning of § 1.513-1(d) and regularly carried on, the fees paid to M by P vendors would be considered unrelated business taxable income under § 512(a)(1) unless excluded by one of the modification provisions under § 512(b). Section 512(b)(3) excludes all rents from real property from unrelated business taxable income. M contends that revenue from the P constitutes rents from real property within the meaning of § 512(b)(3).

The term "rent" is not defined in the code. Black's Law Dictionary (9th ed. 2009) defines "rent" as "consideration paid, usually periodically, for the use or occupancy of property (esp. real property)." Under the P rules and regulations, a vendor is treated as "a seller of merchandise and/or services, and not as a tenant, licensee, or other form of permissive user" of property. Nevertheless, M states that its arrangement with P vendors is comparable to the one described in Rev. Rul. 69-178, in which payments made under a verbal agreement to use a meeting hall for a single afternoon were determined to constitute rents from real property. Further, M cites Rev. Rul. 67-218 to contend that its right to use the parking lot constitutes an interest in real property. However, the question is not whether M's (or the vendors') use of N's parking lot involves an interest in real property, but whether the fees paid by the vendors are simply for the use of real property – as in the case in Rev. Rul. 69-178 – or, instead, for the

opportunity to sell merchandise at an organized event that requires extensive preparation and services to stage.

Payments for the use or occupancy of rooms or other space where services are also rendered to the occupant do not constitute rents 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. Section 1.512(b)-1(c)(5). The Examinations agent asserts that the fees paid by the vendors are not "rents from real property" because M provides substantial services for the convenience of the vendors, services which are "other than those customarily rendered in connection with the rental of space for occupancy only" within the meaning of § 1.512(b)-1(c)(5), including advertising, entertainment, direction of traffic, shuttle services from parking lot, an ATM machine, and insurance. M counters that these services are not rendered for the convenience of the vendors because M is not contractually obligated to provide any services to the vendors, but merely confers the right to use and occupy a particular piece of real property for a particular period of time. It is immaterial whether these services are enumerated in a written agreement. They are regularly provided by M, M incurs time and expense in providing the services, the services help to make the P successful, and, under these circumstances, a vendor would reasonably consider these services to be a part of the arrangement related to participation in the P for which fees are paid.

Section 1.512(b)-1(c)(5) identifies a limited number of examples of customarily rendered services that include furnishing heat and light, cleaning public entrances, exits, stairways, and lobbies, and collecting trash. M contends that the services it does provide – supervising the use of the property, providing parking for vendors' customers and employees, furnishing electricity, cleaning public spaces, entrances, and exits, and collecting trash – are usual and customary under the terms of the regulation, and do not amount to the extensive services provided to the tenant by the university in Rev. Rul. 80-298. Although M maintains that its lease of vendor spaces is similar to the short-term, often verbal, leases of a bare meeting hall by the organization described in Rev. Rul. 69-178, with respect to which only utilities and janitorial services were provided, we find that the services provided to the vendors at the P go far beyond mere utilities, janitorial services, and services usually rendered for occupancy only.

M asserts that the various activities conducted by it with respect to the P are simply activities customarily undertaken by a landlord of commercial retail space. M compares the vendors at the P with the tenants of a shopping mall, and states that all the services provided at the P are similar to those customarily rendered by the landlord of a shopping mall for its tenants. M also points to § 856 (which defines the term "real estate

investment trust") to demonstrate that "rents from real property" include "charges for services customarily furnished or rendered in connection with the rental of real property." However, as pointed out in Rev. Rul. 2004-24, 2004-1 C.B. 550 (discussing whether amounts received by a real estate investment trust from providing parking facilities at its rental real properties qualify as rents from real property under § 856(d)), the definition of "rents from real property" for purposes of § 856 differs significantly in scope and structure from the definition of "rents from real property" under § 512(b)(3). Rev. Rul. 2004-24 points to differences in congressional intent and differences in the regulations interpreting the sections.

Comparing the operation of the P to leasing shopping mall space is specious because the P itself is not physical retail space; rather, it is an *event*. The vendors are paying not merely to occupy a space, in this case a plot of bare parking lot. Rather, the vendors at the P are paying to be part of an organized event that must be arranged, assembled, staged, and disassembled each weekend. Vendors would not lease space in a parking lot except to be part of the P. And the P would not exist but for the week-in, week-out preparations and services provided by M's employees to turn a parking lot into a successful, well-attended commercial event and back again into a parking lot. Arranging, assembling, staging, and disassembling a P are not services usually or customarily rendered to the occupant of a few square feet of a parking lot. Furthermore, even the operation of a parking lot, with its attendant services—services that are more limited than that provided in the operation of the P—are not treated as rents from real property under § 1.512(b)-1(c)(5).

Like the extensive "grounds maintenance" services provided by the lessor of a football stadium described in Rev. Rul. 80-298, M's employees provide extensive services to transform an empty parking lot into an attractive and efficient emporium for the vendors. Among other things, M's employees determine selling space sizes and configurations, demarcate such spaces with white lines and identifying numbers or letters painted on the ground, assign and reassign the spaces to vendors and stand-by vendors, and ensure that those vendors comply with an extensive set of space use regulations. More specifically, to ensure the successful operation of the P, M has developed, and must administer and enforce, an extensive set of rules and regulations governing the successful operation of the P. M's employees select appropriate vendors through a rigorous vendor application process. In addition, M's employees regulate vendors with respect to their selling spaces, the goods they sell, and the services they provide.

In addition, to further ensure the success of the P, M promotes the P as though it were a business and not the mere lease of real property. For instance, M advertises the P in various print outlets and on radio and television. In addition, M maintains a website

dedicated to the P on which one finds a comprehensive listing of vendors. A vendor's listing is more than just a mere statement of the vendor's name, merchandise category, and location, but also includes a description of the merchandise, the vendor's website address, phone number and photo, and a link to "email this vendor."

Finally, M's employees engage in a number of "customer relations" services that are not usual or customary in the context of a mere lease of bare ground, such as—

- Staffing an information booth;
- Assisting customers in seeking to resolve any problems or complaints directed toward any vendor;
- Arranging for live entertainment;
- Providing and maintaining restroom facilities;
- Providing shuttle service from parking lots to the vendor areas; and
- Providing an ATM machine on site.

Most of these services are not necessary to, or customarily rendered in connection with, the rental of space for occupancy only.

M asks us to compare its operation of the P to the two situations involving the use of a school's tennis courts for the conduct of a tennis club described in Rev. Rul. 80-297. M states that its operation of the P is more similar to situation 2 than situation 1. In situation 2, the school leased its tennis courts to an unrelated third party for a fee without services. In situation 1, the school operated the tennis club through its own employees. Plainly, it is not the case that M has leased the parking lot to an unrelated third party without services. Rather, M operates the P through its own employees who perform substantial services for the vendors and visitors to the P. Accordingly, as in situation 1 of Rev. Rul. 80-297, the income M receives from vendors in connection with the operation of the P is not excludable from unrelated business taxable income as rent from real property under § 512(b)(2).

CAVEAT(S):

A copy of this technical advice memorandum is to be given to the taxpayer(s). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.