Internal Revenue Service

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Washington, DC 20224

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Person To Contact:
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Date:
April 04, 2017

LEGEND:

Issuer =

County =

Hospital =

State A =

State B =

School =

Bonds =

Date 1 =

Date 2 =

Dear :

This responds to Issuer's request for a ruling that the Agreement described below will not result in private business use of the Hospital under § 141(b) of the Internal Revenue Code (the "Code").

Facts and Representations

Issuer makes the following representations. Issuer is a nonprofit public benefit corporation duly organized and existing under the laws of State A. Issuer was formed to assist County in financing capital improvements and acquisitions and qualifies as an on behalf of issuer with respect to County under Revenue Ruling 63-20, 1963-1 C.B. 24, and Revenue Procedure 82-26, 1982-1 C.B. 476.

The Bonds are currently outstanding and were issued on behalf of County by Issuer to finance or refinance Hospital.

Although Hospital is owned by Issuer while the Bonds are outstanding, County has exclusive beneficial possession of Hospital and will become owner of Hospital upon retirement of the Bonds. Hospital is operated by County, under the control and direction of the County Board of Supervisors. Hospital is an adult and pediatric medical care facility which includes operating rooms, trauma center, radiology services, intensive care units, a birthing center, and complete pulmonary services.

Hospital is also an accredited "teaching hospital" and offers training programs for nursing students, medical residents, and allied health professionals attending local universities and colleges. Teaching hospital arrangements provide mutual benefit to the hospital and the students by providing expertise for the hospital while allowing the students more contact with patients. The teaching hospital and students are able to collaborate in and stay current on the most advanced methods of delivery of medical care and assist with serving community members, including those that are economically disadvantaged.

Hospital plans to enter into an arrangement (the "Agreement") with School, a State B nonprofit organization. Pursuant to the Agreement and because it is a teaching hospital, County will make the Hospital facilities available for the provision of clinical practice experience for pharmacy students of School in clinical rotations.

School will select the students and faculty instructors and will develop the curriculum, educational activities, and proposed activities for the students. School will maintain all attendance and academic records of students, and will ensure that each student and faculty instructor possesses all appropriate and necessary licenses, permits, registrations, and certificates required under Federal, State, and local law. School will require each faculty instructor and each student to complete Hospital orientation prior to rotating at Hospital as well as complete training as specified from time to time by Hospital, including but not limited to Hospital's training for workforce members related to patient information privacy and confidentiality. School will also require that each student and each faculty instructor comply with all applicable Hospital rules, regulations, policies, and procedures when rotating at Hospital facilities.

Hospital does not guarantee availability of its facilities at all times or the number of students or faculty instructors that it may be able to accommodate at any particular time. Hospital will have the right to immediately remove any student or faculty instructor from Hospital if it determines that the student or faculty instructor is jeopardizing Hospital's licensing, accreditation, or the health and safety of patients, visitors or staff.

School will be required to maintain, at its sole cost and expense, worker's compensation insurance as well as professional liability insurance for the activities of its students and faculty instructors under the Agreement. No payment or other form of compensation will be made by County or Hospital to School or vice versa under the Agreement.

The Agreement will have a retroactive starting date of Date 1 and an ending date of Date 2, a term of five years. The parties have not yet signed the Agreement.

There is no provision of the Agreement allowing School to have any input on the annual budget of Hospital, capital expenditures with respect to Hospital, any disposition of property that is part of Hospital, any rates charged for use of Hospital, or the general nature and type of use of Hospital.

County bears all risk of loss upon damage or destruction to Hospital. School is not entitled to and will not take any tax position that is inconsistent with being a service provider to County with respect to Hospital.

School has no role or relationship with County that, in effect, limits School's ability to exercise rights, including cancellation rights, under the Agreement. None of the voting power of the County Board of Supervisors is vested in School or its board members, officers, and employees; there are no persons that serve both on the County Board of Supervisors and the board of School; and County and School are not related parties within the meaning of § 1.150-1(b) of the Income Tax Regulations.

As of Date 1, the term of the Agreement is not greater than the lesser of 30 years or 80 percent of the weighted average reasonably expected economic life of Hospital.

Law and Analysis

Section 103(a) of the Internal Revenue Code (the "Code") provides that, except as provided in § 103(b), gross income does not include interest on any state or local bond. Section 103(b) provides, in part, that § 103(a) shall not apply to any private activity bond which is not a qualified bond (within the meaning of § 141).

Section 141(a) provides that the term "private activity bond" means any bond issued as part of an issue which meets (1) the private business use test of § 141(b)(1) and the private security or payment test of § 141(b)(2), or (2) the private loan financing test of § 141(c).

Section 141(b)(1) provides that, except as otherwise provided, an issue meets the private business use test if more than 10 percent of the proceeds of the issue are to be used for any private business use. Section 141(b)(6)(A) defines "private business use" as use (directly or indirectly) in a trade or business carried on by a person other than a governmental unit. Section 1.141-3 provides that the 10 percent private business use test is met if more than 10 percent of the proceeds of an issue is used in a trade or business.

Section 141(b)(6)(A) generally provides that the term "private business use" for purposes of § 141(b), means use (directly or indirectly) in a trade or business carried on by any person other than a governmental unit. For purposes of § 141(b)(6)(A), use as a member of the general public shall not be taken into account. Section 141(b)(6)(B) provides that, for purposes of § 141(b)(6)(A), any activity carried on by a person other than a natural person shall be treated as a trade or business.

Section 1.141-3(a)(1) provides that the private business use test relates to the use of the proceeds of an issue, and, for this purpose the use of financed property is treated as the direct use of proceeds. Section 1.141-3(a)(2) provides that in determining whether an issue meets the private business use test, it is necessary to look to both the direct and indirect uses of proceeds.

Section 1.141-3(b)(1) generally provides that both actual and beneficial use by a nongovernmental person may be treated as private business use. In most cases, the private business use test is met only if a nongovernmental person has special legal entitlements to use the financed property under an arrangement with the issuer. In general, a nongovernmental person is treated as a private business user of proceeds and financed property as a result of ownership; actual or beneficial use of property pursuant to a lease, or a management or incentive payment contract; or certain other arrangements such as a take or pay or other output-type contract.

Section 1.141-3(b)(3) provides, with certain exceptions, that the lease of financed property to a nongovernmental person is private business use of that property. For this purpose, any arrangement that is properly characterized as a lease for federal income tax purposes is treated as a lease. In determining whether a management contract is properly characterized as a lease, it is necessary to consider all of the facts and circumstances, including (i) the degree of control over the property that is exercised by a nongovernmental person; and (ii) whether a nongovernmental person bears risk of loss of the financed property.

Section 1.141-3(b)(4)(i) provides, with certain exceptions, that a management contract with respect to financed property may result in private business use of that property based on all of the facts and circumstances. A management contract with respect to financed property generally results in private business use of that property if the contract provides for compensation for services rendered with compensation based, in whole or in part, on a share of net profits from the operation of the facility.

Section 1.141-3(b)(4)(ii) defines a management contract as a management, service, or incentive payment contract between a governmental person and a service provider under which the service provider provides services involving all, a portion of, or any function of, a facility. For example, a contract for the provision of management services for an entire hospital, a contract for management services for a specific department of a hospital, and an incentive payment contract for physician services to patients of a hospital are each treated as a management contract.

Revenue Procedure 2017-13, 2017-6 I.R.B. 787, provides safe harbor conditions under which a management contract does not result in private business use under § 141(b). If a management contract meets all of the applicable conditions of §§ 5.02 through 5.07 of the revenue procedure, the contract does not result in private business use.

Section 5.02 of Rev. Proc. 2017-13 provides in part that (1) payments to the service provider under the contract must be reasonable compensation for services rendered during the term of the contract, (2) the contract must not provide to the service provider a share of net profits from the operation of the facility, and (3) the contract must not, in substance, impose upon the service provider the burden of bearing any share of net losses from the operation of the managed property.

Section 5.03 of Rev. Proc. 2017-13 provides in part that the term of the contract, including all renewal options (as defined in § 1.141-1(b)), must not be greater than the lesser of 30 years or 80 percent of the weighted average reasonably expected economic life of the managed property. For this purpose, economic life is determined in the same manner as under § 147(b) as of the beginning of the term of the contract.

Section 5.04 of Rev. Proc. 2017-13 provides in part that the qualified user must exercise a significant degree of control over the use of the managed property. This control

requirement is met if the contract requires the qualified user to approve the annual budget of the managed property, capital expenditures with respect to the managed property, each disposition of property that is part of the managed property, rates charged for the use of the managed property, and the general nature and type of use of the managed property (for example, the type of services).

Section 5.05 of Rev. Proc. 2017-13 provides in part that the qualified user must bear the risk of loss upon damage or destruction of the managed property (for example, due to force majeure).

Section 5.06 of Rev. Proc. 2017-13 provides in part that the service provider must agree that it is not entitled to and will not take any tax position that is inconsistent with being a service provider to the qualified user with respect to the managed property.

Section 5.07 of Rev. Proc. 2017-13 provides that (1) the service provider must not have any role or relationship with the qualified user that, in effect, substantially limits the qualified user's ability to exercise its rights under the contract, based on all the facts and circumstances, and (2) as a safe harbor, a service provider will not be treated as having a role or relationship prohibited under § 5.07(1) of the revenue procedure if: (a) no more than 20 percent of the voting power of the governing body of the qualified user is vested in the directors, officers, shareholders, partners, members, and employees of the service provider, in the aggregate; (b) the governing body of the qualified user does not include the chief executive officer of the service provider or the chairperson (or equivalent executive) of the service provider's governing body; and (c) the chief executive officer of the service provider is not the chief executive officer of the qualified user or any of the qualified user's related parties (as defined in § 1.150-1(b)).

We conclude that the Agreement is a management contract as defined in § 1.141-3(b)(4)(ii) because School provides services to Hospital, has no control of Hospital, and does not bear the risk of loss of Hospital. However, we also conclude that the Agreement does not meet all of the safe harbor conditions under Rev. Proc. 2017-13. Thus, whether or not the Agreement results in private business use of the Hospital depends on the facts and circumstances. We conclude that it does not result in private business use. The safe harbors of Rev. Proc. 2017-13 are useful reference points for this analysis.

There is no payment of compensation from County to School for the services provided by School. The School also bears no share of the costs of, or losses from, the operation of Hospital. Thus, the School does not participate in the net profits from the operation of Hospital.

The contract has a term of five years and does not exceed the lesser of 30 years or 80 percent of Hospital's remaining economic life. County bears all risk of loss upon damage or destruction to Hospital. School is not entitled to and will not take any tax

position that is inconsistent with being a service provider to County with respect to Hospital.

School has no role or relationship with County that, in effect, substantially limits County's ability to exercise its rights under the Agreement. Similarly, under the Agreement, the School has no right to provide input on the annual budget of Hospital, capital expenditures with respect to Hospital, any disposition of property that is part of Hospital, any rates charged for use of Hospital, or the general nature and type of use of Hospital.

Conclusion

Under the facts and circumstances of this case, we conclude that the Agreement does not result in private business use of Hospital under § 141(b).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any transaction or item discussed or referenced in this letter.

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

In accordance with a Power of Attorney on file with this office, a copy of this letter is being sent to each of Issuer's authorized representatives.

The ruling contained in this letter is based upon information and representations submitted by Issuer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the materials submitted in support of the request for a ruling, it is subject to verification upon examination.

Sincerely,

Associate Chief Counsel
(Financial Institutions & Products)

By: _____
Timothy L. Jones
Senior Counsel, Branch 5