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LEGEND

Taxpayer =

LLC =

LLC1 =

LLC2 =

Team =

League =

Date 1 =

A =

B =

C =

D =

E =

Dear :

This letter responds to your request for a private letter ruling that the Membership Amount payable to LLC2 and received by LLC and LLC1 from its Members will not be includible in Taxpayer's gross income under § 61 of the Internal Revenue Code (Code).

FACTS

Taxpayer is an entity treated as a partnership for U.S. federal income tax purposes. Taxpayer's overall method of accounting is the accrual method. LLC, a disregarded single member limited-liability company of Taxpayer, owns and operates the Team, a professional sports franchise that is a member of the League. LLC1 is a disregarded single member limited-liability company of Taxpayer that is in the process of constructing a new arena (Arena) where the Team will play substantially all of its home games. To finance construction of the Arena, LLC2, an entity to be formed as a

disregarded single member limited-liability company of Taxpayer, will issue non-equity membership rights (Memberships). Persons wishing to obtain a Membership will be required to complete an application for LLC2's review. Upon LLC2's approval of the application, LLC2 and the applicant (Member) will enter into an agreement for a Membership (Membership Agreement).

The rights, privileges, duties, and obligations of the Membership will be set forth in a Membership Agreement. The Membership Agreement will provide that, in exchange for payment by the Member (Membership Amount), during the period beginning on the date the Membership Agreement is entered into and ending on the repayment date agreed to by the parties (Term), LLC2 will: (i) grant the Members privileges not generally available to the non-Members (e.g., access to exclusive presales to purchase tickets for the non-Team events at the Arena and invitations to attend certain exclusive events), (ii) obligate the Members to purchase Team season tickets from LLC for a specific designated seat in the Arena each season during the Term, and (iii) provide the Members the opportunity to purchase playoff tickets for the Team home games from LLC and tickets to other events at the Arena from event sponsors. The repayment date agreed to by the parties is the Date 1 immediately preceding the A anniversary of the date that the Arena has been substantially completed as determined by LLC2 (Repayment Date).

The Membership Amount due from the Member will be equal to an amount determined by LLC2. LLC2 will direct the Members to make payment of the Membership Amount directly to LLC1 or LLC, as applicable.¹ The Members will have the option to pay up to \$B of the Membership Amount in installments under a Deferred Payment Plan. Under the Deferred Payment Plan, the Members may pay the Membership Amount in installments over two alternative payment schedules: either in C annual payments or in D monthly payments, plus interest on the deferred portion of the Membership Amount accruing at a rate of E percent per annum. Under either payment schedule, the first payment of a certain percent of the Membership Amount is due to LLC1 or LLC, as applicable, with the signing of the Membership Agreement, and the subsequent payments commence with the opening of the Arena.² The Membership Amount is not considered paid in full until the entire principal amount of the Membership Amount has been paid to LLC1 or LLC, as applicable. However, all rights, privileges, duties, and obligations under the Membership Agreement arise and are fully in effect on the date

¹ As discussed above LLC, LLC1, and LLC2 are disregarded entities of Taxpayer for U.S. federal income tax purposes. Therefore, any transfers of the Membership Amounts between these entities are also disregarded for U.S. federal income tax purposes.

² For any interest payable by a Member that elects to pay the Membership Amount in installments, LLC and LLC1, as applicable, will include the interest in income as required under § 1.1272-1 of the Income Tax Regulations if the interest is original issue discount or under §§ 1.446-2 and 1.451-1(a) if the interest is not original issue discount.

that LLC2 and the Member enter into the Membership Agreement. LLC and LLC1 intend to use the Membership Amount primarily for financing construction of the Arena.

The Membership Agreement will provide that, upon entry into the Membership Agreement, LLC2, as the sole party entering into the Membership Agreement with the Members, has an unconditional obligation to repay to the Member the principal amount of the Membership Amount paid by the Member to LLC1 or LLC during the Term, without interest, no later than the Repayment Date. Further, LLC2 may prepay all or part of this amount without penalty. The Membership Amount will be repaid without interest and, except as may be required by the debt financing for construction of the Arena, will not be placed in a separate account, but rather, will be commingled with the other operating funds and proceeds of LLC and/or LLC1.

In addition, Taxpayer, LLC, and LLC1 will cause LLC2 to establish and maintain, including through equity contributions by the direct and indirect owners of Taxpayer (Principal Owners), a money market account (Reserve Account) with a nationally-recognized commercial bank for the purpose of collecting funds for the repayment of the Membership Amount. The Principal Owners, Taxpayer, LLC, LLC1, and LLC2 will cause the Reserve Account to be maintained free and clear of any liens, claims, charges or encumbrances; will not withdraw or permit the withdrawal or application of any funds in the Reserve Account other than to repay the Membership Amount; and will provide monthly account statements for the Reserve Account to be delivered directly to the League. On dates specified and as may be requested by the League from time to time, LLC will deliver to the League evidence of the deposit into the Reserve Account and a certificate of Taxpayer's CFO setting forth in reasonable detail the aggregate amount of the Membership Amount repayments reasonably expected to be payable on or before the Repayment Date.

The Principal Owners will provide LLC2 the funds necessary for LLC2 to pay its expenses, liabilities and obligations (including, without limitation, the Membership Amount if there are not enough funds in the Reserve Account when repayment is due), and will jointly and severally provide these funds to the extent not provided by any other investor in Taxpayer.

The Membership Agreement will provide that termination of a Membership will take place upon the occurrence of one or more of the following events:

- (a) The expiration of the Term;
- (b) The death of a Member who is an individual, unless an immediate family member reasonably acceptable to LLC2 elects to assume the obligations of the Membership Agreement;

- (c) The failure of a Member to comply with the terms and conditions of the Membership Agreement (including, failure to pay when installments of the Membership Amount are due);
- (d) A Member's failure to purchase Team season tickets for the applicable designated seat(s) by the payment deadline specified by LLC; or
- (e) The transfer by a Member that is not permitted by the Membership Agreement.

In the event of the termination of a Membership, the Membership Agreement will provide that the Member will be entitled to repayment of the principal amount of the Membership Amount that the Member paid to LLC2 or its designees (e.g., LLC or LLC1) during the Term, without interest, no later than the Repayment Date. Further, LLC2 may prepay all or part of this amount without penalty.

The Membership Agreement will provide that, subject to LLC2's approval, which is not to be unreasonably withheld, a Member (Transferor) can, prior to the expiration of the Term, transfer (Transfer) its Membership rights, privileges, duties, and then-outstanding obligations to a third party (Transferee). The consideration payable to the Transferor (Transfer Amount) will not be: (i) greater than the original principal amount of the Transferor's Membership Amount and (ii) less than any outstanding principal amount of the Membership Amount payable by the Transferor to LLC2 or its designees (e.g., LLC or LLC1) as of the date of the Transfer (Transfer Minimum Amount), if any. On the date of the Transfer, the Transferee must pay directly to LLC2 or its designee an amount equal to the Transfer Minimum Amount in full. The amount of the Transfer Amount that exceeds the Transfer Minimum Amount (Excess Amount), if any, will be payable by the Transferee to the Transferor upon the terms and conditions as the parties may negotiate, provided that LLC2's obligation to repay the Transferor upon expiration of the Term will be reduced by an amount equal to the Excess Amount.

On or before the expiration of the Term, LLC2 will repay the Transferee an amount equal to the Transfer Amount. In addition, on or before the expiration of the Term, any remaining balance of the original principal amount of the Membership Amount (i.e., after taking into account the Excess Amount) will be repaid to the Transferor. At no time will a Transferor be entitled to receive, in the aggregate from Transferee and LLC2, more than the original principal amount of the Membership Amount paid by the Transferor, and a Transferee will not be entitled to more than the Transfer Amount.

REPRESENTATION

The Membership Agreement will clearly and explicitly inform the Member that the Membership Amount is not deductible by the Member for federal income tax purposes. In the case of previously executed Membership Agreements, Taxpayer will provide notification that will clearly and explicitly inform the Member that the Membership Amount is not deductible for federal income tax purposes.

RULING REQUESTED

The Membership Amount received by Taxpayer from each Member is not includible in taxable income under § 61 of the Code for federal income tax purposes at the time the Membership Amount is received.

LAW AND ANALYSIS

Section 61 of the Code and the underlying regulations provide that gross income means all income from whatever source derived unless excluded by law.

The Supreme Court in *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426 (1955), defined gross income as any item that increases a taxpayer's net worth. The Supreme Court specifically referred to gross income as "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion."

In *James v. United States*, 366 U.S. 213 (1961), the Supreme Court explained that, in order for gain (e.g., money) to be includible in gross income, there must be a claim of right to the alleged gain and the absence of a definite, unconditional obligation to repay or return that which would otherwise constitute a gain. *See also Commissioner v. Tufts*, 461 U.S. 300 (1983) (indicating that when a taxpayer receives the proceeds of a loan, the taxpayer incurs an obligation to repay the loan at some future date and, therefore, the loan proceeds are not gross income to the taxpayer).

The facts submitted and the representations made that are the subject of this ruling request are governed by, and within the parameters of, the Supreme Court's decisions in *Glenshaw Glass* and *James*. A taxpayer does not have an accession to wealth, nor complete dominion over an item, if received subject to an unconditional obligation to repay the item. If a taxpayer receives money or other property with an unconditional obligation to return or repay it, the taxpayer is not enriched by the transaction and, therefore, does not realize gross income within the meaning of section 61 of the Code.

In the present case, Taxpayer represents that the Membership Amount received by Taxpayer through LLC, LLC1, or LLC2 from the Members is subject to LLC2's unconditional obligation to repay the Members. Because of this, Taxpayer does not have the requisite complete control over the Membership Amount required for the Membership Amount to be gross income to Taxpayer within the meaning of section 61 of the Code.

CONCLUSION

Based on the facts submitted and the representations made, we rule as follows:

The Membership Amount received by Taxpayer from each of the Members is not includible in gross income under § 61 of the Code for federal income tax purposes at the time the Membership Amount is received because it is received subject to LLC2's unconditional obligation to repay the Membership Amount to the Members.

CAVEATS

The ruling contained in this letter is based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. Specifically, this ruling is based on the representation that the Membership Agreement between LLC2 and its Members will clearly and explicitly inform the Members that their Membership Amount is being received by Taxpayer subject to an unconditional obligation of LLC2 to repay the Membership Amount to the Member. While this office has not verified any of the material submitted in support of the request for ruling, it is subject to verification on examination.

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, this ruling is limited to only the Membership Amount received by Taxpayer from its Members, and does not address the treatment of any interest payments made by its Members in connection with the Membership Amount.

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.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

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,

Stephen J. Toomey
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Income Tax & Accounting)