

INTERNAL REVENUE SERVICE
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CC:DOM:P&SI:2 - PLR-113755-98
November 3, 1998

X =

a =

b =

c =

x =

y =

d1 =

Dear :

This responds to your letter dated June 29, 1998, submitted on behalf of X, requesting a ruling that rents received by X will not constitute "passive investment income" within the meaning of § 1362(d)(3)(C)(i) of the Internal Revenue Code.

The information submitted states that X is an S corporation with accumulated C corporation earnings and profits. X develops, owns, operates, and leases commercial real estate. X owns a single-story office buildings, which combined have b tenants, none of which are related to X. The buildings combined contain approximately c leasable square feet.

X represents that X performs significant services and incurs substantial costs in the development, operation and leasing of its properties. X employs, for a fee, an unrelated third-party management company to assist in conducting the operation of the buildings. X, through the management company, provides the following services to its tenants: management office staff during regular business hours, Monday through Friday; on call office staff 24 hours per day, seven days per week; daily janitorial service for each tenant's space and the common areas; parking lot and sidewalk repairs; trash pick-up; snow removal;

replacement of light bulbs; window replacement and annual exterior and interior window washing; lawn care; and exterior roof and exterior structural repairs. X, through its officers, makes all major decisions affecting the management of the buildings, repairs, lease negotiations, improvements and expenses.

For the d1 taxable year, X received gross rents from the tenants of the buildings of \$x and incurred rental real estate expenses (not including depreciation) of \$y, which included property taxes, insurance, cleaning, maintenance, utilities and property management.

Section 1362(d)(3)(C)(i) provides that, except as otherwise provided, the term "passive investment income" means gross receipts derived from royalties, rents, dividends, interest, annuities, and sales or exchanges of stock or securities.

Section 1.1362-2(c)(5)(ii)(B)(1) of the Income Tax Regulations defines "rent" as amounts received for the use of, or the right to use, property (whether real or personal) of the corporation.

Section 1.1362-2(c)(5)(ii)(B)(2) provides that the term "rents" does not include rents derived in the active trade or business of renting property. Rents are derived in an active trade or business of renting property only if, based on all the facts and circumstances, the corporation provides significant services or incurs substantial costs in the rental business. Generally, significant services are not rendered and substantial costs are not incurred in connection with net leases. Whether significant services are performed or substantial costs are incurred in the rental business is determined based upon all the facts and circumstances including, but not limited to, the number of persons employed to provide the services and the types and amounts of costs and expenses incurred (other than depreciation).

Based solely on the facts and the representations submitted, we conclude that the rental receipts from commercial rental real estate received by X are not passive investment income under § 1362(d)(3)(C)(i).

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code.

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.

Pursuant to a power of attorney on file in this office, a copy of this letter will be sent to X.

Sincerely yours,

H. GRACE KIM
Assistant to the Chief
Branch 2
Office of the Assistant
Chief Counsel
(Passthroughs and
Special Industries)

Enclosures: 2
Copy of this letter
Copy for § 6110 purposes