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PRIVATE RULING 9740007

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Section 145
Qualified Sec. 501(c)(3) Bonds

0145.00-00, 0142.04-00

PRIVATE RULING 9740007; 1997 PRL LEXIS 1039

DATE: June 27, 1997

[*5]

Refer Reply to: CC:DOM:FI&P:5/PLR-254130-96

LEGEND:

Facility = * * *
Bonds = * * *
Issuer = * * *
Operator = * * *
State = * * *
State Law = * * *
x = * * *
y = * * *

[*6]

Dear * * *

1 This letter is in reply to a ruling request regarding whether Facility, financed with the proceeds of the Bonds of Issuer, is a residential rental property for family units within the meaning of section 145(d) of the Internal Revenue Code. The facts and representations made are summarized below.

2 Operator was formed to assist and provide services to senior citizens and frail and disabled individuals. Operator has been recognized as exempt from federal income tax under sections 501(c)(3) and 509(a)(2) of the Code. Issuer issued the Bonds shortly before submitting this ruling request and loaned the proceeds to Operator. Operator used the proceeds of the Bonds to finance its acquisition of the Facility [*7] and an adjacent lot, completion of the Facility, financing costs, and to establish appropriate reserves, as permitted by law and regulations. No proceeds have been or will be used in a trade or business other than activities related to Operator's exempt purpose.

3 From the time that the Bonds were issued and thereafter, the Operator has maintained the Facility as a qualified residential rental project within the meaning of section 142(d), regarding the requirements pertaining to the incomes of the residents, and Issuer elected to meet the 20-50 Test under section 142(d)(1)(A).

4 State Law defines, in part, a "health care facility" as any institution, sanitarium, hospital, nursing home, or assisted living center in which any accommodation is maintained, furnished or [*8] offered for the hospitalization, nursing care, or supervised care of the sick or injured. State Law defines an assisted living center facility ("ALCF") as any institution, rest home, boarding home, place, or building maintained and operated to provide personal care and services which meet some need beyond basic provision of food, shelter and laundry in a facility which is not otherwise required to be licensed under the law. No health care facility may be operated in State without first obtaining a license from State's Department of Health. Lodging establishments that furnish only board and room, or either, to their guests, are exempt from licensing.

5 In this case, Facility is licensed and regulated by State's Department of Health under State Law as an ALCF. At the time of its acquisition Facility consisted of x completed units. An additional y units have been added with a portion of the Bond [*9] proceeds. In order to retain its license under State Law, Facility must meet specific structural requirements, provide specific services, and maintain significant health and personal standards for persons staying at an ALCF. State Law provides that each resident of an ALCF must receive daily care by facility personnel as needed to keep skin, nails, hair, mouth, clothing, and body clean and healthy. The facility must provide linens, (including maintenance of a supply of towels and bed linen equal to 3 times resident census, have procedures for handling of soiled linens including required washing of such linens in accordance with regulatory requirements for disinfection), equipment, and supplies for personal care and for other activities of daily living commensurate with the needs of the resident served.

6 An ALCF is required to provide at least [*10] three meals a day that must be served in the common dining facility. Residents must be encouraged to eat in the common dining room and dietetic services must be provided (in a wholesome and programmed fashion). Each resident is required to have (1) have a physical exam before admission, (2) must be tested for Tuberculosis, and (3) may not work in any capacity that might allow the spread of a communicable disease. Detailed records of medical care and medications must be kept for each resident.

7 A planned activities program must be provided with therapeutic activities designed to meet the needs and interests of

individual residents." Supplies and materials for such activities must be provided by the ALCF as well. Finally, an ALCF must also provide services and information to residents regarding durable powers of attorney for health care, [*11] how to protect assets, how to apply for Medicare and Medicaid benefits, how to contact physicians, and other services.

8 The information submitted indicates that Facility meets or exceeds each of the requirements for licensing discussed above. In addition, the individual units in Facility for one or two persons consist of an unfurnished living area (for bed and other furniture), a closet, a bathroom, a small food preparation area, and a system to allow communication between the medical staff and residents. Each bathroom includes a toilet, sink, and a handicap accessible shower, but not a bathtub. The food preparation area includes kitchen-type appliances such as a refrigerator, sink, and in some instances a stove. Where the presence of a stove might be potentially hazardous, given the particular resident's condition, a stove (if present) would be removed and a hot [*12] plate or microwave would be substituted to avoid fire hazards or personal burns. Thus, some units could be provided without stoves in recognition that some residents will not be able to safely live with a stove.

9 Although husbands and wives may share a unit, it is not permitted unless both persons qualify for residency. In addition, no other family members may reside temporarily or otherwise (such as overnight visits) in a unit, and visitation to residents of a unit is subject to regulation by Operator consistent with State Law.

10 Detailed information has also been provided regarding common areas of Facility that are available to all residents, programs and activities that are or will be provided to all residents, as well as a general explanation of the monthly charges each [*13] resident must pay. The monthly charges cover not only space in an individual unit, but also not less than 14 meals per week to be served in the common dining area, housekeeping services (including the linens and towels required by State Law), laundry services, bathing assistance as needed, assistance in dressing and undressing, a 24-hour monitored emergency call system, daily checks on each resident's activity, and extensive personal services care.

LAW AND ANALYSIS

11 Section 103(a) provides that except as provided in subsection (b), gross income does not include interest on any State or local bond.

12 Section 103(b)(1) provides that subsection (a) does not [*14] apply to any private activity bond that is not a qualified bond within the meaning of section 141. Section 141(e)(1) provides, in

pertinent parts, that the term "qualified bond" means any private activity bond that is (A) an exempt facility bond, or (G) a qualified 501(c)(3) bond.

13 Section 142(a)(7) provides, in part, that the term "exempt facility bond" includes any bond issued as part of an issue 95 percent or more of the net proceeds of which are to be used to provide qualified residential rental projects. Section 142(d) provides that the term "qualified residential rental project" means any project for residential rental property if, at all times during the qualified project period, such project meets one of the two tests described, whichever is elected by the issuer at the time of the issuance of the issue with respect to such project. Subparagraph [*15]

(1)(A) of section 142(d) provides that a project meets the requirements of the 20-50 Test if 20 percent or more of the residential units in such project are occupied by individuals whose income is 50 percent or less of area median gross income.

14 Under section 145(a), qualified 501(c)(3) bonds are defined as bonds that would not be private activity bonds if section 501(c)(3) organizations were treated as governmental units with respect to their activities that do not constitute unrelated trades or businesses by applying section 513(a).

15 Section 145(d)(1) provides generally, that a bond which is part of an issue shall not be a qualified 501(c)(3) bond if any portion of the net proceeds of the issue are to be used directly or indirectly to provide residential rental property [*16] for family units.

16 Section 145(d)(2) provides that paragraph (1) shall not apply to any bond issued as part of an issue if the portion of such issue which is to be used as described in paragraph (1) is to be used to provide-

(A) a residential rental property for family units if the first use of such property is pursuant to such issue,

(B) qualified residential rental projects (as defined in section 142(d)), or

(C) property which is to be substantially rehabilitated in a rehabilitation beginning within the 2-year period ending 1 year after the date of the acquisition of such property. [*17]

17 Section 1.103-8(b)(4)(i) of the Income Tax Regulations defines, in pertinent part, a qualified residential rental project as a building or structure, together with any functionally related and subordinate facilities, containing one or more similarly constructed units that are used on other than a transient basis. In addition, the regulations provide that hotels, motels, dormitories, fraternity and sorority houses, rooming houses, HOSPITALS, NURSING HOMES,

SANITARIUMS, REST HOMES, and trailer parks and courts for use on a transient basis are not residential rental projects. (Emphasis added.)

18 The residential rental property exempt facility provision originated with section 103(c)(4)(A) of the Internal Revenue Code of 1954 which was added by the Revenue [*18] and Expenditure Control Act of 1968, section 107(a), 1968-2 C.B. 715, 731. This provision allowed tax-exempt bond financing for certain exempt activities, including residential real property for family units. The Conference Report, H.R. Conf. Rep. No. 1533, 90th Cong., 2d Sess., 37, (1968), 1968-2 C.B. 801, 809, describes a family unit as follows:

> A family unit is a building or portion thereof which contains complete living facilities which are to be used on other than a transient basis by only one family consisting of one or more persons. Thus, an apartment which is to be used on other than a transient basis by one family, which contains complete facilities for living, sleeping, eating, cooking, and sanitation constitutes a family unit. Hotels, motels, dormitories, fraternity and sorority houses, rooming houses, HOSPITALS, SANITARIUMS, REST [*19] HOMES, and parks and courts for mobile homes DO NOT CONSTITUTE RESIDENTIAL REAL PROPERTY. (Emphasis added.)

19 Similarly, in the legislative history of section 142(d) of the Internal Revenue Code of 1986, the Conference Report in note 24 describes the conference agreement with respect to multifamily residential rental projects as follows:

> As under present law, multifamily residential rental property is eligible for tax-exempt financing only if the housing units are used other than on a transient basis. In addition, each residential rental unit must include separate and complete facilities for living, sleeping, eating, cooking, and sanitation. Hotels, dormitories, HOSPITALS, NURSING HOMES, RETIREMENT HOMES, and trailer parks DO NOT QUALIFY AS RESIDENTIAL [*20] RENTAL PROPERTY. 2 H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. 11-699, (1986), 1986-3 (Vol. 4) C.B. 699. (EMPHASIS ADDED.)

20 Section 1.103-8(b)(4)(i), consistent with the foregoing cited legislative history, also provides that hospitals, nursing homes and sanitariums do not qualify as residential rental property for purposes of what is now section 142(d). Although the terminology "assisted living center" or similar term is not among the specifically excluded facilities, the nomenclature for a health care facility, which may change as innovations occur, is not determinative. Rather, the focus of the legislative history and the regulation is whether the institution involved is providing residences for individuals, as compared to bed-space in a health care facility.

[*21]

21 For this purpose, health care facilities may be characterized by certain common qualities: (1) they are regulated by the appropriate health department of a state as health care institutions, (2) they specifically accentuate the availability of immediate medical services to and/or the care of the persons being serviced, (3) the laws of the state, and/or the regulations and rules of that state's health department specify numerous procedures, measures, and standards pertaining to both the medical treatment of residents and the staff, and (4) the required treatment of the residents/patients is far beyond a landlord-tenant relationship that may limit use by the tenant or may require the landlord to provide amenities such as food and laundry services.

22 Facility is maintained and operated in accordance with [*22] statutory and regulatory requirements that exist under State Law, including requirements for continued licensing as an ALCF in State. Its operation is consistent with providing bedspace for individuals in a health care facility and is not consistent with being a residential rental facility for family units.

CONCLUSION

23 Based on the information and documentation provided, we conclude that Facility does not provide residential rental property for family units. Accordingly, Facility is not excluded from being financed with the proceeds of a qualified 501(c)(3) bond under section 145(d)(1).

24 No opinion is expressed regarding the consequences [*23] of the transaction described herein under any section of the Code, including sections 103 and 141 through 150, and the Income Tax Regulations or the temporary Income Tax Regulations thereunder, except as specifically stated in this ruling.

25 This ruling letter is directed only to the taxpayer which requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent. Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling will be modified or revoked by adoption of temporary or final regulations, to the extent the regulations are inconsistent with any conclusion in the ruling. See section 12 of Rev. Proc. 97-1, 1997-1 I.R.B. 11, 43. However, when the criteria in section 12.05 are satisfied, a ruling is not revoked or modified retroactively, except in rare or [*24] unusual circumstances.

Sincerely,

Assistant Chief Counsel
(Financial Institutions &

Products)

By:
Timothy L. Jones
Assistant to
Branch 5

Enclosure:

Copy for section 6110 purposes [*25]

A BULLETIN FROM:
McDERMOTT, WILL & EMERY

Boston
Chicago
Los Angeles
Miami
Newport Beach
New York
Silicon Valley
Washington, D.C.

Moscow
St. Petersburg
Vilnius

ON THE SUBJECT . . .

November 1997

Assisted Living Care Facilities as Qualified Residential Rental Projects

Be careful what you ask for, you may get it. The old adage came to light again recently when an assisted living facility applied to the Internal Revenue Service (IRS) for a ruling that the bonds used to finance the facility were Section 145 "qualified 501(c)(3) bonds" rather than Section 142 "qualified residential rental bonds." While the organization obtained the ruling it requested from the IRS, the rationale used by the IRS in reaching its conclusion was flawed and overly broad. Read literally, the private letter ruling implies that assisted living care facilities may not qualify as residential rental projects within the meaning of Section 142 of the Code and, therefore, may not be financed with the proceeds of a tax-exempt bond offering, unless the operator is a Section 501(c)(3) organization, which would allow the bonds to be classified as qualified Section 501(c)(3) bonds under Section 145 of the Code. For obvious reasons, this letter has caused significant concern in the tax-exempt bond and assisted living communities.

This article will briefly discuss the recently released private letter ruling, explain the fallacy in its rationale and, more importantly, provide guidance to both existing and developing assisted living facilities that are or will be financed with the proceeds of Section 142 bonds.

Background

The Internal Revenue Code (the "Code") has provided since 1968 that the interest received by bondholders on certain types of bonds will be exempt from federal income tax. Specifically, Section 103 of the Code provides that interest earned on certain governmental bonds and qualified private activity bonds will not be taxable to the bondholders. Governmental bonds are generally obligations issued by the government to fund essential governmental operations. Private activity bonds, in general, are issued by a governmental unit but the proceeds are used by someone (the "qualified user") other than a governmental entity. The qualified user is usually a Section 501(c)(3) organization. In the case of private activity bonds, the interest earned on such bonds is only exempt from federal income tax to the bondholder if the bonds are "qualified." To be qualified, the bonds must satisfy the conditions of Section 145 and/or Section 142 of the Code.

Tax-exempt bonds used for residential real property are treated unusually by Section 145(d) of the Code. First, Section 145(d)(1) provides that if any portion of the proceeds of a tax-exempt bond issue is used to provide residential rental property for family units, the bonds are not qualified 501(c)(3) bonds. Immediately after disqualifying bonds used for residential rental property, however, the very next section of the Code states that Section 145(d)(1) does not apply to exclude any bonds issued for: (a) a new residential rental property for family units, (b) qualified residential rental projects that satisfy the conditions of Section 142 of the Code for low-income and (c) property which has been substantially rehabilitated. What Section 145(d) accomplishes is that bonds used for residential rental property will not be considered "qualified Section 501(c)(3) bonds" unless the facility is new, substantially rehabilitated, or meets the requirements in Section 142 for low-income residential units. Stated simply, satisfaction of the requirements of Section 142(d) requires that a significant portion of the tenants in the facility be comprised of individuals or families whose income levels are 50 percent or less of the area's median gross income.

Private Letter Ruling 9740007

Private Letter Ruling (PLR) 9740007 (June 27, 1997), involved a Section 501(c)(3) organization (the "Operator") that was formed to provide services to senior citizens and disabled individuals. Prior to submitting the ruling request, the Operator had used the proceeds of a tax-exempt bond offering to finance the acquisition of an existing assisted living center facility (the "Facility"). In the particular state where the Facility was located, the state's Department of Health was responsible for licensing and regulating assisted living center facilities (ALCFs). In order to retain its license under state law, the Facility had to meet specific structural requirements, provide specific services, and maintain significant health and personal standards for its residents. The facts in the letter ruling indicate that as of the date of the ruling request, the Facility had been operated as a qualified residential rental project within the meaning of Section 142 of the Code, regarding the requirements pertaining to the income level of the residents.

For reasons not made clear in the letter ruling, the Operator requested a ruling from the IRS that the Facility did not provide residential rental property for family units, within the meaning of Section 145(d)(1) of the Code and, therefore, the Facility was not excluded from being financed with the proceeds of qualified Section 501(c)(3) bonds. While not discussed in the letter ruling, it appears that the ruling was requested because either (i) the Facility could no longer meet the Section 142 "20-50 Test" described above, or (ii) the Operator simply did not want to continue to provide units for low-income tenants in the ALCF.

If the Facility was no longer going to be providing low-income units, the bonds would become taxable bonds to the bondholders unless the Facility was determined not to be a residential rental project and, therefore, not excluded from treatment as qualified Section 501(c)(3) bonds.

Right Answer, Wrong Analysis

The IRS reviewed the facts, the statute, and the relevant legislative history and determined that the Facility was not a residential rental property for family units within the meaning of Section 145(d)(1) and, therefore, the bonds were not excluded from classification as qualified Section 501(c)(3) bonds. As described below, while the conclusion reached in the letter ruling may be correct, the rationale used to arrive at the conclusion is flawed.

The rationale used by the IRS is as follows. Section 1.103-8(b)(4)(i) of the Income Tax Regulations defines, in pertinent part, a qualified residential rental project as a building or structure, together with any functionally related and subordinate facilities, containing one or more similarly constructed units that are used on other than a transient basis. In addition, the regulations provide that hotels, motels, dormitories, fraternity and sorority houses, rooming houses, hospitals, nursing homes, sanitariums, rest homes, and trailer parks and courts for use on a transient basis are not residential rental projects.

In reviewing the legislative history concerning residential rental projects, the IRS notes that Congress described a family unit as follows.

> A family unit is a building or portion thereof which contains complete living facilities which are to be used on other than a transient basis by only one family consisting of one or more persons. Thus, an apartment which is to be used on other than a transient basis by one family, which contains complete facilities for living, sleeping, eating, cooking, and sanitation, constitutes a family unit. Hotels, motels, dormitories, fraternity and sorority houses, rooming houses, hospitals, sanitariums, rest homes, and parks and courts for mobile homes do not constitute residential real property.

H.R. Conf. Rep. No. 1533, 90th Cong., 2d Sess., 37, (1968), 1968-2 C.B. 801, 809.

The letter ruling also notes that in the legislative history of Section 142(d) of the Code, the Conference Report, in note 24, describes the conference agreement with respect to multifamily residential rental projects as follows:

> As under present law, multifamily residential rental property is eligible for tax-exempt financing only if the housing units are used other than on a transient basis. In addition, each residential rental unit must include separate and complete facilities for living, sleeping, eating, cooking, and sanitation. Hotels, dormitories, hospitals, nursing homes, retirement homes, and trailer parks do not qualify as residential rental property.

H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. 11-699, (1986), 1986-3 (Vol. 4) C.B. 699.

Based on the above, the letter ruling concludes that "the focus of the legislative history and the regulation is whether the institution involved is providing residences for individuals, as compared to bed-space in a health care facility." Accordingly, because the Facility is maintained and operated in accordance with statutory and regulatory requirements that exist under state law for health care facilities, including the requirements for continued licensing as an ALCF, it is a health care facility and, therefore, is not consistent with being a residential rental property for family units.

The conclusion is unfounded. In reviewing Section 1.103-8(b)(4)(i) of the regulations and the legislative history thereunder, there is absolutely no discussion whatsoever that implies assisted living facilities may not qualify as residential rental projects. To the contrary, the clear and sole focus of the regulations and the legislative history is that a facility whose tenants are primarily transient in nature may not qualify as a residential real property. The mere fact that hospitals and nursing homes were included by Congress in a list of facilities that may not qualify as residential rental properties cannot be interpreted to mean that other types of facilities which may provide some limited types of health care services as a whole may not qualify. Instead, Congress was merely providing a list of the types of facilities in which it believed the residents were transient in nature. Whether the facility is a health care facility, in and of itself, is irrelevant.

In fact, the legislative history for Section 145(d) of the Code directly contradicts the rationale used by the IRS in PLR 9740007. Specifically, the Conference Committee Reports for the Technical and Miscellaneous Revenue Act of 1988 provide that Section 145(d) of the Code is to be applied to the residential care facilities of a continuing care center. According to Congress, Section 145(d) provides that if an existing continuing care facility is purchased by a Section 501(c)(3) organization with tax-exempt bonds, the provisions of Section 142 must be followed.

H.R. 4333, Conf. Rep. No. 100-1104, 100th Cong., 2d Sess. (1988), 1988-3 C.B. 617.

This statement by the Conference Committee is in direct contrast to the rationale used by the IRS in PLR 9740007.

The private letter ruling also neglected to mention general factors about the typical assisted living resident and residence which would have warranted treating the facility as a qualified residential rental project including: the average length of stay of most residents is over two years, while most facilities require a minimum lease of one year (and deposit); state laws circumscribe the level of skilled medical care which can be provided in ALCFs; and most operators of ALCF market their projects as residential in atmosphere rather than institutional (like health care facilities). rights of tenancy!

Life After PLR 9740007

It is understood by the IRS and practitioners that private letter rulings may not be used or cited as precedent for any organization other than the one that requested and received the actual letter ruling. Nonetheless, private letter rulings are an indication of how the IRS may rule under similar facts. Accordingly, the release of PLR 9740007 may result in certain bond counsels refusing to give the requisite opinions in order to use tax-exempt bonds to finance the acquisition of existing ALCFs. There are, however, a number of ways to distinguish the Ruling for future ALCF bond financings.

First, as discussed above, the conclusion reached by the IRS that health care facilities may not qualify as residential real property for purposes of Section 142 of the Code is incorrect. A more thorough analysis of the relevant statutes, regulations, and legislative history make it clear that whether a facility is a health care facility, in and of itself, has no impact on whether it may qualify as a qualified residential rental project within the meaning of Section 142(d). Nonetheless, because the IRS appears to be standing by its conclusion in PLR 9740007, at least initially, we are hopeful that someone located in a state other than the state in which the Operator was located will file a ruling request to resolve the issue.

Second, even assuming arguendo that the IRS' rationale was correct, it is limited to the facts in PLR 9740007. The facts in the letter ruling indicate that the Facility was located in a state where ALCFs are highly regulated by the State Department of Health. In PLR 9740007 the IRS defined the type of "health care facility" that could not qualify as a residential rental project as follows:

> "[These] Health care facilities may be characterized by certain common qualities: (1) they are regulated by the appropriate health department of a state as health care institutions, (2) they specifically accentuate the availability of immediate medical services to and/or the care of the persons being serviced, (3) the laws of the state, and/or the regulations and rules of that state's health department specify numerous procedures, measures, and standards pertaining to both the medical treatment of residents and the staff, and (4) the required treatment of the residents/patients is far beyond a landlord-tenant relationship that may limit use by the tenant or may require the landlord to provide amenities such as food and laundry services.

Accordingly, for those facilities located in states where ALCFs are not highly regulated, the letter ruling should not preclude the issuance of the requisite bond counsel opinions. However, the breadth of the IRS' definition of "health care facilities" is enough to include a significant number of state ALCF regimens—even those based on and favoring a "residential" model. A modification by the IRS of the Ruling is unlikely; but any "chill" it may have on future ALCF financing would be dissipated significantly by a clarifying rule in the context of a petitioner seeking 142(d) treatment (and not therefore attempting to avoid the same) in a state regulating ALCFs through its social service or elder affairs department.

For more information regarding this Ruling, please contact your regular McDermott, Will & Emery attorney or:

Christopher J. Donovan, Boston
cdonovan@mwe.com (617)345-5036

Robert C. Louthian, III, Washington, D.C.
rlouthian@mwe.com (202)778-8172

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1ST ITEM of Level 1 printed in FULL format.

PRIVATE RULING 9740007

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possible "hooks"
- rights of tenancy provided
- licensure is an issue
- involving licensing the "service package" which is co-located, but it's a voluntary mechanism to permit use of categorical funding in a more flexible, efficient manner in someone's home!

Section 145
Qualified Sec. 501(c)(3) Bonds

0145.00-00, 0142.04-00

PRIVATE RULING 9740007; 1997 PRL LEXIS 1039

DATE: June 27, 1997

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Refer Reply to: CC:DOM:FI&P:5/PLR-254130-96

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proceeds. In order to retain its license under State Law, Facility must meet specific structural requirements, provide specific services, and maintain significant health and personal standards for persons staying at an ALCF. State Law provides that each resident of an ALCF must receive daily care by facility personnel as needed to keep skin, nails, hair, mouth, clothing, and body clean and healthy. The facility must provide linens, (including maintenance of a supply of towels and bed linen equal to 3 times resident census, have procedures for handling of soiled linens including required washing of such linens in accordance with regulatory requirements for disinfection), equipment, and supplies for personal care and for other activities of daily living commensurate with the needs of the resident served.

6 An ALCF is required to provide at least [*10] three meals a day

that must be served in the common dining facility. Residents must be encouraged to eat in the common dining room and dietetic services must be provided (in a wholesome and programmed fashion). Each resident is required to have (1) have a physical exam before admission, (2) must be tested for Tuberculosis, and (3) may not work in any capacity that might allow the spread of a communicable disease. Detailed records of medical care and medications must be

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kept for each resident.

7 A planned activities program must be provided with therapeutic activities designed to meet the needs and interests of individual residents." Supplies and materials for such activities must be provided by the ALCF as well. Finally, an ALCF must also provide services and information to residents regarding durable powers of attorney for health care, [*11] how to protect assets, how to apply for Medicare and Medicaid benefits, how to contact physicians, and other services.

8 The information submitted indicates that Facility meets or exceeds each of the requirements for licensing discussed above. In addition, the individual units in Facility for one or two persons consist of an unfurnished living area (for bed and other furniture), a closet, a bathroom, a small food preparation area, and a system to allow communication between the medical staff and residents. Each bathroom includes a toilet, sink, and a handicap accessible shower, but not a bathtub. The food preparation area includes kitchen-type appliances such as a refrigerator, sink, and in some instances a stove. Where the presence of a stove might be potentially hazardous, given the particular resident's condition, a stove (if present) would be removed and a hot [*12] plate or microwave would be substituted to avoid fire hazards or personal burns. Thus, some units could be provided without stoves in recognition that some residents will not be able to safely live with a stove.

9 Although husbands and wives may share a unit, it is not permitted unless both persons qualify for residency. In addition, no other family members may reside temporarily or otherwise (such as overnight visits) in a unit, and visitation to residents of a unit is subject to regulation by Operator consistent with State Law.

10 Detailed information has also been provided regarding common areas of Facility that are available to all residents, programs and activities that are or will be provided to all residents, as well as a general explanation of the monthly charges each [*13] resident must pay. The monthly charges cover not only space in an individual unit, but also not less than 14 meals per week to be served in the common dining area, housekeeping services (including the linens and towels required by State Law), laundry services, bathing assistance as needed, assistance in dressing and undressing, a 24-hour monitored emergency call system, daily checks on each resident's activity, and extensive personal services care.

LAW AND ANALYSIS

11 Section 103(a) provides that except as provided in subsection (b), gross income does not include interest on any State or local bond.

12 Section 103(b)(1) provides that subsection (a) does not [*14] apply to any private activity bond that is not a qualified bond within the meaning of section 141. Section 141(e)(1) provides, in pertinent parts, that the term "qualified bond" means any private activity bond that is (A) an exempt facility bond, or (G) a qualified 501(c)(3) bond.

13 Section 142(a)(7) provides, in part, that the term "exempt facility bond" includes any bond issued as part of an issue 95 percent or more of the net proceeds of which are to be used to provide qualified residential rental projects. Section 142(d) provides that the term "qualified residential rental project" means any project for residential rental property if, at all times during the qualified project period, such project meets one of the two tests described, whichever is elected by the issuer at the time of the issuance of the issue with respect to such project. Subparagraph [*15] (1)(A) of section 142(d) provides that a project meets the requirements of the 20-50 Test if 20 percent or more of the residential units in such project are occupied by individuals whose income is 50 percent or less of area median gross income.

14 Under section 145(a), qualified 501(c)(3) bonds are defined as bonds that would not be private activity bonds if section 501(c)(3) organizations were treated as governmental units with respect to their activities that do not constitute unrelated trades or businesses by applying section 513(a).

15 Section 145(d)(1) provides generally, that a bond which is part of an issue shall not be a qualified 501(c)(3) bond if any portion of the net proceeds of the issue are to be used directly or indirectly to provide residential rental property [*16] for family units.

16 Section 145(d)(2) provides that paragraph (1) shall not apply to any bond issued as part of an issue if the portion of such issue which is to be used as described in paragraph (1) is to be used to provide-

(A) a residential rental property for family units if the first use of such property is pursuant to such issue,

(B) qualified residential rental projects (as defined in section 142(d)), or

(C) property which is to be substantially rehabilitated in a rehabilitation beginning within the 2-year period ending 1 year after the date of the acquisition of such property. [*17]

17 Section 1.103-8(b)(4)(i) of the Income Tax Regulations

defines, in pertinent part, a qualified residential rental project as a building or structure, together with any functionally related and subordinate facilities, containing one or more similarly constructed units that are used on other than a transient basis. In addition, the regulations provide that hotels, motels, dormitories, fraternity and sorority houses, rooming houses, HOSPITALS, NURSING HOMES,

SANITARIUMS, REST HOMES, and trailer parks and courts for use on a transient basis are not residential rental projects. (Emphasis added.)

18 The residential rental property exempt facility provision originated with section 103(c)(4)(A) of the Internal Revenue Code of 1954 which was added by the Revenue [*18] and Expenditure Control Act of

1968, section 107(a), 1968-2 C.B. 715, 731. This provision allowed tax-exempt bond financing for certain exempt activities, including residential real property for family units. The Conference Report, H.R. Conf. Rep. No. 1533, 90th Cong., 2d Sess., 37, (1968), 1968-2 C.B. 801, 809, describes a family unit as follows:

> A family unit is a building or portion thereof which contains complete living facilities which are to be used on other than a transient basis by only one family consisting of one or more persons. Thus, an apartment which is to be used on other than a transient basis by one family, which contains complete facilities for living, sleeping, eating, cooking, and sanitation constitutes a family unit. Hotels, motels, dormitories, fraternity and sorority houses, rooming houses, HOSPITALS, SANITARIUMS, REST [*19] HOMES, and parks and courts for mobile homes
>
> DO NOT CONSTITUTE RESIDENTIAL REAL PROPERTY. (Emphasis added.)

19 Similarly, in the legislative history of section 142(d) of the Internal Revenue Code of 1986, the Conference Report in note 24 describes the conference agreement with respect to multifamily residential rental projects as follows:

> As under present law, multifamily residential rental property is eligible for tax-exempt financing only if the housing units are used other than on a transient basis. In addition, each residential rental unit must include separate and complete facilities for living, sleeping, eating, cooking, and sanitation. Hotels, dormitories, HOSPITALS, NURSING HOMES, RETIREMENT HOMES, and trailer parks DO NOT QUALIFY AS RESIDENTIAL [*20] RENTAL PROPERTY. 2 H.R. Conf. Rep. No. 841, 99th
>
> Cong., 2d Sess. 11-699, (1986), 1986-3 (Vol. 4) C.B. 699. (EMPHASIS ADDED.)

20 Section 1.103-8(b)(4)(i), consistent with the foregoing cited legislative history, also provides that hospitals, nursing homes and sanitariums do not qualify as residential rental property for purposes of what is now section 142(d). Although the terminology

"assisted living center" or similar term is not among the specifically excluded facilities, the nomenclature for a health care facility, which may change as innovations occur, is not determinative. Rather, the focus of the legislative history and the regulation is whether the institution involved is providing residences for individuals, as compared to bed-space in a health care facility.

[*21]

21 For this purpose, health care facilities may be characterized by certain common qualities: (1) they are regulated by the appropriate health department of a state as health care institutions, (2) they specifically accentuate the availability of immediate medical services to and/or the care of the persons being serviced, (3) the laws of the state, and/or the regulations and rules of that state's health department specify numerous procedures, measures, and standards pertaining to both the medical treatment of residents and the staff, and (4) the required treatment of the residents/patients is far beyond a landlord-tenant relationship that may limit use by the tenant or may require the landlord to provide amenities such as food and laundry services.

* people qualify for the services (i.e. are eligible) as they would on their own home.

22 Facility is maintained and operated in accordance with [*22] statutory and regulatory requirements that exist under State Law, including requirements for continued licensing as an ALCF in State. Its operation is consistent with providing bedspace for individuals in a health care facility and is not consistent with being a residential rental facility for family units.

CONCLUSION

23 Based on the information and documentation provided, we conclude that Facility does not provide residential rental property for family units. Accordingly, Facility is not excluded from being financed with the proceeds of a qualified 501(c)(3) bond under section 145(d)(1).

24 No opinion is expressed regarding the consequences [*23] of the transaction described herein under any section of the Code, including sections 103 and 141 through 150, and the Income Tax Regulations or the temporary Income Tax Regulations thereunder, except as specifically stated in this ruling.

25 This ruling letter is directed only to the taxpayer which requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent. Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling will be modified or revoked by adoption of temporary or final regulations, to the extent the regulations are inconsistent with any conclusion in the ruling. See section 12 of Rev. Proc. 97-1, 1997-1 I.R.B. 11, 43. However, when

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the criteria in section 12.05 are satisfied, a ruling is not revoked or modified retroactively, except in rare or [*24] unusual circumstances.

Sincerely,

Assistant Chief Counsel
(Financial Institutions &

Products)

By: ____________________
Timothy L. Jones
Assistant to
Branch 5

Enclosure:

Copy for section 6110 purposes [*25]