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PLRs: Parking revenue qualifies as rents from real property for REITs

The IRS publicly released two substantially similar private letter rulings* concluding that the share that a real estate investment trust (REIT) receives as parking revenue will qualify as rents from real property for purposes of section 856(d).

PLR 202013006 [PDF 110 KB] and **PLR 202013007** [PDF 110 KB]. Both letter rulings were released on March 27, 2020, and are dated December 20, 2019.

*Private letter rulings are taxpayer-specific rulings furnished by the IRS Office of Chief Counsel in response to requests made by taxpayers and can only be relied upon by the taxpayer to whom issued. Pursuant to section 6110(k)(3), written determinations such as private letter rulings are not intended to be relied upon by third parties and may not be cited as precedent. These written determinations may, however, offer an indication of the IRS's position on the issues addressed.

Summary

Each of the REITs owns rental property with underground parking across the street from each other. These garages will be physically interconnected, so it will be impractical to determine in which parking garage any individual car has been parked. Thus, the two REITs decided to operate their garages (through an independent contractor) as if they were one parking garage and to share parking revenue and expenses in a manner replicating as closely as possible the revenue and expenses that each REIT would have if the parking garages were operated separately rather than jointly. Based on certain representations—including that each REIT's garage is appropriate in size and expected to be used for parking predominantly by tenants of each REIT (and their customers and guests)—the IRS ruled that each REIT's share of the parking revenue will qualify as rents from real property for purposes of section 856(d).

KPMG observation

This ruling is meaningful because parking revenue is ordinarily treated as qualifying rents to a REIT if the parking service is furnished to the REIT's own tenants or, primarily for the convenience or benefit of the REIT's tenants or to the guests, customers, or subtenants of the tenants. However, as the garages in the two PLRs are physically interconnected, it is impractical to conclude that tenants of one

REIT are using the garage of that very REIT. Having said that, because each REIT represents that its garage is appropriate in size and is expected to be used predominantly by tenants of each REIT (and their customers and guests), these garages on a combined basis would remain to be used predominantly by tenants (and their guest, customers, and subtenants) of these REITs. That is, parking revenue would mostly be for the parking services rendered in connection with rental of real property, so the conclusion reached in these letter rulings is viewed by tax professionals as a sensible finding.

Letter rulings

In the letter rulings, there are two land parcels across the street from each other that are part of a mixed-use development project.

- Parcel 1 is intended to have an office condo unit (owned by REIT A) and a retail condo unit (owned by LLC). Parcel 1 will have an underground parking garage that is used by REIT A, but REIT A is required to leave a certain number of parking spaces available for daily public parking (including to be used by retail tenants of LLC and their customers and guests). REIT A represents that the Parcel 1 garage (including the number of spaces set aside for public parking) is appropriate in size for the expected number of tenants and their respective guests, customers and subtenants of REIT A's office condo unit. Further, REIT A represents that the garage is expected to be used predominantly by the office condo unit's tenants and their guests, subtenants, and customers and will be built for this purpose.

- Parcel 2 contains a residential condo unit (owned by an unrelated party), a retail condo unit (owned by REIT B), and a subsurface three-level parking garage. Certain lower levels of the parking garage are dedicated for the residential condo unit with a separate gated entry. REIT B is entitled to use the remaining parking garage and represents that the number of spaces in its portion of the parking garage is appropriate in size for its tenants and their guests, subtenants, and customers and is expected to be used predominantly by them.

The letter rulings describe that the land-use and environmental permits for the entire mixed-use development project require the garages to be physically interconnected underground. Once physically interconnected, cars will be able to enter and exit either parking garage from the other parking garage without using the surrounding streets. Further, it is anticipated that each parking garage will nonetheless be predominantly used for parking by tenants (and their customers and guests) of the REIT owning such parking garage. However, because there will be free access from each parking garage to the other, it will be possible for cars entering through the entrance to one of the parking garages to park in the other parking garage. Thus, it will be impractical to determine in which parking garage any individual car has been parked. Accordingly, the REITs have determined that the parking garages must be operated essentially as if they were one parking garage, and they intend to engage one independent contractor for the parking garages.

The letter rulings describe further certain activities and operational matters at the parking garages. For example, the garage operator may park cars, but only in order to maximize capacity of the parking garages or for reasons of safety or security. The garage operator may also connect or disconnect electric vehicles from charging stations or move electric vehicles close to or away from charging stations in order to maximize the use of charging stations. No separate fee will be charged to move or park a car or to connect or disconnect an electric vehicle from a charging station. Occasionally, as a courtesy or when necessary, an attendant may provide minor, incidental or emergency service, such as charging a battery or changing a flat tire.

Because of the joint operation, both REITs will need to share public parking revenues (the "Parking Revenues") and expenses of the parking garages and intend to share these items in a manner that replicates as closely as possible the revenue and expenses that each REIT would have if the parking garages were operated separately rather than jointly.

After citing Rev. Rul. 2004-24, the IRS described that:

> *As in Situation 3 [of Rev. Rul. 2004-24], the Parking Garages are appropriate in size for the expected number of tenants, guests, customers and subtenants. Unlike the parking facilities in Situation 3, however, each Parking Garage is connected to the other Parking Garage, so that the Parking Revenues received by [each REIT] may not represent the exact amounts attributable to cars parked in [the respective garage]. Based on Taxpayer's representations that the connection of the Parking Garages is required by the permits for the project, that each Parking Garage will be used for parking predominantly by tenants (and their customers and guests) of the REIT owning such Parking Garage, and that Parking Revenues and expenses will be shared so as to replicate as closely as possible the revenue and expenses that each REIT would have if the Parking Garages were operated separately, the Parking Garages are sufficiently similar to the parking facilities described in Situation 3 of Revenue Ruling 2004-24 that the Parking Revenues should be subject to the same analysis as the parking income received in Situation 3.*

The IRS accordingly ruled each REIT's share of the Parking Revenues will qualify as rents from real property for purposes of section 856(d).

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