TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **200635018**
Release Date: 9/1/2006
Date: June 8, 2006

Contact Person:

501-03-00
501-03-31

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose,* and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: March 27, 2006

501-03-00
501-03-31

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

A =
B =.
C =
D =
E =
F =
G =

Dear :

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

A is a nonprofit corporation, jointly founded and operated by B and C, two for-profit medical practices. A's mission is to improve the quality of oncology care by developing plans of care based on collaborative, consultative, evidence-based process approved by the patients' caregivers. A has represented that it is also a professional review committee created pursuant to D and E.

A is comprised of a cross-section of providers and other individuals involved in the delivery of care to cancer patients. These include physicians (primary care, oncology, surgery, radiology, pathology, other sub-specialists specific to each case), medical ethics experts, hospice providers, insurance company medical directors, nurse case managers and consumers.

Through the collaborative effort of all of these individuals, A recommends a specific plan of care for each cancer patient, after a rigorous peer review process using evidence-based, national treatment guidelines.

A will initially identify the patient according to the national treatment guidelines and begin data collection in preparation for referral of the patient for consideration. Specialized software will be used to organize patient information and A will design and interface a secure "chat room" with functionality to accommodate discussion and facilitate a final recommendation. A's recommendations will be provided to attending physicians and to the patient in an understandable form. To help ensure the highest quality patient care, outcome reporting and analysis will be conducted at each entry point and for the duration of the patient's care.

The eligible patient population will be limited during the early stages of A's development. Initially, B will identify all patients who are insured by F, a for-profit Medicare HMO, and will refer all of F's oncology patients to A. Approximately 4 percent of C's patients are enrolled in F and approximately 22 percent of B's patients are enrolled in F. Three physicians have entered into a participation agreement with A. All of these physicians are officers or directors of either B or C. Physicians who wish to participate in A will enter into a participation agreement. The participation agreement outlines the duties and responsibilities of the physician and A in the case review process.

If the initial effort proves successful in improving the quality of patient care, the patient population will be expanded to include all oncology patients of B and C. Ultimately, A will make the collaborative process available to outside physicians who wish to have their cases reviewed by A's Review Committee, thus expanding the benefits of the team care approach to additional patient populations.

The Review Committee presently consists of a small number of persons who are working to develop the process and systems. When the program becomes operational, all physicians of B (47 physicians) and C (53 physicians) will be asked to participate. At this time the Review Committee has 7 members: one physician of B and one physician of C, one nurse from each practice, two volunteers and a nurse employed by A.

Each case will be assigned a review period during which Review Committee members can provide input as to the recommended plan of care. As time is of the essence in oncology care, all participants will be encouraged to provide comments within the designated review period. If, based on the comments submitted during the review period, there is a consensus among A's Review Committee members regarding the recommended plan of care, A's Care Coordinator will notify the Review Committee members and the treating physician(s). The Care Coordinator will also facilitate the referral/preauthorization process and arrange appointment times to assure that all recommended care is provided in the most expeditious manner possible.

Should individual opinion vary from that of A's Review Committee, an appeal process has been defined and will soon be available to all participants. All appeals will be expected to include medical rationale for any and all variances to the treatment guidelines.

The members of A's Board of Directors are elected by its corporate members, B and C. Each corporate member elects five (5) Board members. The officers of A are officers and directors of B and C. Recently a new member has been added to the Board of Directors of A, the President and CEO of G, a provider of indigent and medically underserved individuals that is an organization described in section 501(c)(3) of the Code.

A proposes that all ten director positions be determined now. The composition of the ten positions would be as follows: B and C would each elect one director; of the remaining eight positions there would be a minimum of four physicians, two of whom must be primary care physicians and two who must be oncologists. These four physician directors would not be required to be doctors in the two member groups. The remaining four positions would either physicians or laypersons from the community. Other than the two directors selected by B and C, it would be self-perpetuating Board. A's offices are located in B's offices. A's Bylaws include a limited conflicts of interest policy.

A's sources of financial support include grants and contributions from governmental units, pharmaceuticals, other organizations described in section 501(c)(3) of the Code and individuals. The funds required to start operations were provided by B and C.

LAW

Section 501(a) of the Internal Revenue Code provides that organizations described in section 501(c)(3) shall be exempt from taxation. Section 501(c)(3) includes corporations organized and operated exclusively for charitable, religious, and educational purposes. Furthermore, section 501(c)(3) requires that no part of the organization's net earnings inure to the benefit of any private shareholder or individual, that no substantial part of its activities is to influence legislation, and that it does not participate in any political campaign on behalf of or in opposition to any candidate for public office. Section 1.501(a)-1(c) of the Income Tax regulations provides that private shareholders or individuals are defined as persons having a personal and private interest in the activities of an organization.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that to be exempt as an organization described in section 501(c)(3) of the Code an organization must be both organized and operated exclusively for purposes specified in section 501(c)(3). If an organization fails to meet either test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that in order for an organization to be considered operated for one or more exempt purposes, it must engage primarily in activities that accomplish one or more exempt purposes specified in section 501(c)(3). An organization will not be so regarded as operated exclusively for one or more exempt purposes if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated for an exempt purpose unless it serves a public rather than a private interest. Even though an organization serves a public interest, it will not qualify for status under section 501(c)(3) of the Code if it also serves a private interest more than incidentally. Therefore, the organization has to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interest.

The private benefit prohibition of section 501(c)(3) applies to all kinds of persons and groups, not just to those "insiders" subject to the stricter inurement proscription. Prohibited private benefit may include an "advantage; profit; fruit; privilege; gain or interest." Retired Teachers Legal Defense Fund v. Commissioner, 78 T.C. 280, 286 (1982).

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the Tax Court held that an organization that as its primary activity operated a school to train individuals for careers as political campaign professionals was not operated exclusively for exempt purposes as described in section 501(c)(3) of the Code because the school's activities conferred impermissible private benefit. The court defined "private benefit" as "nonincidental benefits conferred on disinterested persons that serve private interests."

An organization may provide benefits to private individuals provided those benefits are incidental quantitatively and qualitatively. To be qualitatively incidental, private benefit must be a necessary concomitant of an activity that benefits the public at large; in other words, the benefit to the public cannot be achieved without necessarily benefiting certain private individuals. To be quantitatively incidental, the private benefit must be insubstantial, measured in the context of the overall public benefit conferred by the activity. To illustrate the quantitatively incidental concept, compare Rev. Rul. 68-14, 1968-1 C.B. 243, with Rev. Rul. 75-286, 1975-2 C.B. 210.

For a benefit to be qualitatively incidental, it must be a necessary concomitant of the activity which benefits the public at large. That is, the benefit to the public cannot be achieved without necessarily benefiting certain private individuals. For example, in Rev. Rul. 70-186, 1970-1 C.B. 128, an organization was formed to preserve a lake as a public recreational facility and to improve the condition of the water in the lake to enhance its recreational features. Although the organization clearly benefited the public at large, there necessarily was also significant benefit to the private individuals who owned lake front property. In this ruling, the IRS determined that the private benefit was incidental in a qualitative sense, stating:

> The benefits to be derived from the organization's activities flow principally to the general public through the maintenance and improvement of public recreational facilities. Any private benefits derived by the lake front property owners do not lessen the public benefits flowing from the organization's operations. In fact, it would be impossible for the organization to accomplish its purposes without providing benefits to the lake front property owners.

There is also a quantitative connotation to the term "incidental." For example, in Rev. Rul. 76-152, 1976-1 C.B. 151, a group of art patrons formed an organization to promote community understanding of modern art trends. The organization selected modern art works of local artists

for exhibit as its gallery, which was open to the public, and for possible sale. If an art work was sold, the gallery retained a commission of ten percent and paid the remainder to the artist. In this ruling, the IRS concluded that since ninety percent of all sales proceeds are turned over to the individual artists, such direct benefits are substantial and the organization's provision of these benefits m is not merely incidental to its other purposes and activities.

In Rev. Rul. 60-143, 1960-1 C.B. 192, the social and recreational activities carried on by an alumni association of a university were merely incidental to the association's basic purpose of advancing the interests of the university and thus, did not preclude the association from being described in section 501(c)(3) of the Code. This revenue ruling noted that "an activity which is in fact incidental, secondary or subservient to an organization's exempt purpose or purposes and which, when weighed against the whole of the activities of the organization, is less than a substantial part of the total, will not ordinarily operate to deny exemption."

In Rev. Rul. 75-196, 1975-1 C.B. 155, held that an organization operating a law library whose rules limited access and use to members, or their designees, of a local bar association qualified for exemption as an organization described in section 501(c)(3) of the Code. Although the attorneys who used the library might derive personal benefit in the practice of their profession, the benefit was incidental to the library's exempt purpose and a logical by-product of an educational process.

In Rev. Rul. 68-14, an organization that helped beautify a city was exempt when it planted trees in public areas, cooperated with municipal authorities in tree plantings and programs to keep the city clean, and educated the public in advantages of tree planting.

In Rev. Rul. 75-286, an organization with similar activities did not qualify under section 501(c)(3) of the Code where its members consisted of residents and business operators of a city block and its activities were limited to that block. The facts in Rev. Rul. 75-286 indicate that the organization was organized and operated for the benefit of private interests by enhancing the value of members' property.

In est of Hawaii v. Commissioner, 71 T.C. 1067 (1979), aff'd in unpublished opinion, 647 F.2d 170 (9th Cir. 1981), several for-profit est organizations exerted significant indirect control over est of Hawaii, a non-profit entity, through contractual arrangements. The Tax Court concluded that the for-profits were able to use the non-profit as an "instrument" to further their for-profit purposes. Neither the fact that the for-profits lacked structural control over the organization nor the fact that amounts paid to the for-profit organizations under the contracts were reasonable affected the court's conclusion. Consequently, est of Hawaii did not qualify as an organization described in section 501(c)(3) of the Code.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" as used in section 501(c)(3) of the Code includes its generally accepted legal sense. The promotion of

health is a recognized charitable purpose. Rev. Rul. 56-185, 1956-1 C.B. 202, as modified by Rev. Rul. 69-545, 1969-2 C.B. 117; Rev. Rul. 80-114, 1980-1 C.B. 115; and Rev. Rul. 83-157, 1983-2 C.B. 94.

Rev. Rul. 69-545, 1969-2 C.B. 117, holds that the following factors indicate that the use and control of a hospital are for the benefit of the public and that no part of the income of the organization is inuring to the benefit of any private individual nor is any private interest being served:

1. It is controlled by a board of trustees, which is composed of independent civic leaders.

2. It maintains an open medical staff with privileges available to all qualified physicians including leasing available space in its medical building.

3. It operates an active and generally accessible emergency room.

4. It provides hospital care for all those persons in the community able to pay the cost thereof either directly or through third party reimbursement.

All of the facts and circumstances present in the favorable situation of Rev. Rul. 69-545 do not have to be duplicated in every case involving health care providers. The test for exemption is whether the clinic or other health care provider is organized and operated for the charitable purpose of promoting health. The community benefit standard simply requires an evaluation of all the facts and circumstances in determining whether a particular organization meets the exemption standard. Where the type of health care organization involved does not usually have an open medical staff or an emergency room, other facts and circumstances may still demonstrate that the organization benefits the community as a whole. See Sound Health Association v. Commissioner, 71 T.C. 158 (1978), acq., 1981-2 C.B. 2; Geisinger Health Plan v. C.I.R. 985 F.2d 1210, 3rd Cir. 1993, rev'g 62 T.C.M. (CCH) 1656 (1991); Redlands Surgical Services v. Commissioner, 113 T.C. 47 (1999), aff'd per curium, 242 F.3rd 904 (9th Cir. 2001); IHC Health Plans, Inc. v. Commissioner, T.C.M. (CCH) 2001-246, aff'd per curium, 325 F.3rd ll88 (10th Cir. 2003). In IHC Health Plans, Inc., the court stated:

> "In summary, under section 501(c)(3), a health-care provider must make its services available to all in the community plus provide additional community or public benefits. The benefit must either further the function of government-funded institutions or provide a service that would not likely be provided within the community but for the subsidy. Further, the additional public benefit conferred must be sufficient to give rise to a strong inference that the public benefit is the primary purpose for which the organization operates. In conducting this inquiry, we consider the totality of the circumstances. Geisinger I, 985 F.2d at 1219." 325 F.3rd at 1198.

Although circumstances may differ from case to case and among various types of organizations, each organization must still demonstrate that it provides benefits to a class or persons that is broad enough to benefit the community and it must show that it is operated to serve a public rather than a private interest. Although Rev. Rul 69-545 discusses the community benefit standards to be applied to an exempt hospital, the operation of other health care organizations must meet the requirements applicable to the particular services being provided. Therefore, an organization that provides medical services on an outpatient service basis must be controlled by a Board composed by civic leaders and must provide its services to all.

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279, 283 (1945), the Supreme Court stated that the presence of a single nonexempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. This case is the basis of section 1.501(c)(3)-1(c)(1) of the regulations, which provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. Thus the operational test standard prohibiting a substantial nonexempt purpose is broad enough to include inurement, private benefit, and operations that further nonprofit goals outside the scope of section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities are not in furtherance of an exempt purpose.

RATIONALE

B and C are both for-profit medical practices. Under A's Bylaws, B and C have the power to appoint a majority of A's Board of Directors. Thus, B and C effectively control A. A's provision of healthcare services to patients of B and C enhances these businesses and improves their reputation in the community. Therefore, similar to est of Hawaii, supra, B and C are able to use A as an "instrument" to further their for-profit purposes. Accordingly, A is operated for a substantial non-exempt purpose. The presence of this single non-exempt purpose prevents A from qualifying for exemption, regardless of the number or importance of truly exempt purposes. See Better Business Bureau of Washington, D.C., supra. Thus, under section 1.501(c)(3)-1(c)(1) of the regulations, A is not operated exclusively for a tax-exempt purpose because more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

In addition, A operates primarily for the benefit of B and C, two for-profit medical practices, and F, a for-profit HMO, rather than primarily for the benefit of the community. Therefore, A does not satisfy the community benefit standard described in Rev. Rul. 69-545, supra, and in IHC Heath Plan, Inc., supra. Thus, A is not operated exclusively for a tax-exempt purpose, as required by section 501(c)(3) of the Code and section 1.501(c)(3)-1(a)(1) of the regulations.

Finally, because A operates primarily for the benefit of B, C and F, all for-profit businesses, which enhances these businesses and improves their reputation in the community, A's activities confer more than an incidental level of private benefit on B, C and F, both quantitatively and qualitatively, contrary to the prohibition in section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a

proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

In the event this ruling becomes final, it will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

If you decide to protest this ruling, your protest statement should be sent to the address shown below. If it is convenient, you may fax your reply using the fax number shown in the heading of this letter.

If you do not intend to protest this ruling, and if you agree with our proposed deletions as shown in the letter attached to Notice 437, you do not need to take any further action.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437