



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

T =
V =
W =
X =
Y =

Dear _____ :

This is in reference to your ruling request concerning the proposed reorganization (Reorganization) as described below.

Facts:

T is an organization described in section 501(c)(3) of the Internal Revenue Code and is not a private foundation as described in section 509(a)(2). T operates a variety of programs including the operation of a group home for dependent and neglected children who are in need of group care. T provides services to unwed mothers, foster home care for other dependent and neglected children; adoptive placement for children, and everything else necessary or desirable in connection with the care and or placement of any such children and the promotion of the welfare of children.

V, W, X, and Y are organizations described in section 501(c)(3) of the Code and are not private foundations because they are described in section 509(a)(3). Under the Reorganization, V will become the parent holding company of T, W, X, and Y. T's bylaws have been amended to make V its sole member, and V will become the sole member of W, X and Y. V will appoint the board of directors of T, W, X, and Y and approve certain extraordinary corporate transactions such as mergers, dissolution and liquidation.

The Reorganization will provide flexibility to cope with the increasingly competitive environment to deliver services and allocate resources and plan effectively for the future by pulling together new and existing affiliates into a planned and coordinated system. V will now have a system-wide perspective that will enable it to study and respond to the community's needs in a more effective manner than could be achieved by any of its affiliates acting alone. Other goals will be to promote better use of specialized services and expertise by avoiding unnecessary duplication and realizing economies of scale through the sharing of assets, services, and or personnel among the affiliates.

Pursuant to the Reorganization, V will coordinate the efforts of the autonomous providers and other operating entities, which are or will become part of the reorganized corporate structure. V will be responsible for developing a long-range strategic plan for the overall system, focusing on broader system-wide issues to reduce functional overlap and maximize the utilization of available resources.

V will monitor each affiliate's actual and proposed programs to help assure that services are being or will be delivered efficiently. V will focus on whether new organizations should be created or acquired to assume certain functions currently performed by existing affiliates or to add new services to the overall system.

Pursuant to the Reorganization, T will transfer assets to V, W, X and Y. W will operate the care center T currently operates and other similar programs in the future, X will hold all real property, and Y will operate endowments currently that were held by T.

You are requesting the following rulings:

1. The Reorganization and resulting corporate structure will not adversely affect the continued tax-exempt status of T, V, W, X and Y under section 501(c)(3) of the Code.
2. The Reorganization and resulting corporate structure will not adversely affect the continued public charity status of T, V, W, X and Y under section 509(a) of the Code.
3. Any transfer of funds, assets, services and or personnel in connection with the Reorganization and any subsequent sharing of funds, assets, services and or personnel by and amongst T, V, W, X, and Y that are related to the Reorganization will not jeopardize the continued section 501(c)(3) exempt status of the organization providing such funds, assets, services and or personnel.
4. Any payments for transfers of funds, assets, services and/or personnel in connection with the Reorganization and any payments in connection with the subsequent sharing of funds, assets, services and or personnel by and among T, V, W, X, and Y that are related to the Reorganization will not generate unrelated business taxable income under sections 511 through 513 of the Code.

Law:

Section 501(c)(3) of the Code provides, in part, for the exemption from federal income tax of organizations that are organized and operated exclusively for religious, charitable, scientific, or educational purposes, provided no part of their net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in Code section 501(c)(3) in its generally accepted legal sense. The promotion of health has long been recognized as a charitable purpose. See Restatement (Second) of Trusts, sections 368, 372; IV Scott on Trusts, sections 368, 372 (3rd ed. 1967); and Rev. Rul. 69-545, 1969-2 C.B. 117.

Rev. Rul. 69-545, 1969-2 C.B. 117, sets forth standards under which a nonprofit hospital may qualify for recognition of exemption under section 501(c)(3) of the Code. This revenue ruling gave consideration to two separate hospitals, only one of which was determined to qualify for exempt status under section 501(c)(3). By weighing all the relevant facts and circumstances, the revenue ruling analyzed whether both the control and use of the hospitals were for the benefit of the public or for the benefit of private interests. The hospital that qualified for exemption was found to be organized and operated to further the charitable purpose of promoting health by satisfying a community benefit standard that included, among other factors, a board of directors that broadly represented the interests of the community. The hospital that did not qualify for recognition of exemption was found to be operating for the private benefit of those who controlled it rather than for the benefit of the public.

Rev. Rul. 67-149, 1967-1 C.B. 131, holds that an organization providing only financial assistance to organizations exempt under section 501(c)(3) of the Code may qualify for exemption under section 501(c)(3).

Rev. Rul. 69-463, 1969-2 C.B. 131, holds that the leasing of its adjacent office building, and the furnishing of certain office services by an exempt hospital to a hospital based medical group is not unrelated trade or business under section 513 of the Code where the medical group performs important health services for the hospital.

Rev. Rul. 78-41, 1978-1 C.B. 148, concludes that a trust created by a hospital to accumulate and hold funds to pay malpractice claims against the hospital qualified for exemption under section 501(c)(3) of the Code as an integral part of the hospital. The hospital provided the funds for the trust, and the banker-trustee was required to make payments to claimants at the direction of the hospital. The organization conducted an activity that the hospital could perform itself.

Section 509(a)(1) of the Code provides that the term "private foundation" means a domestic or foreign organization described in section 501(c)(3) other than an organization described in section 170(b)(1)(A) (other than in clauses (vii) and (viii)).

Section 511 of the Code imposes a tax on the unrelated business taxable income of organizations exempt from federal income tax under section 501(c).

Section 512(a)(1) of the Code defines the term "unrelated business taxable income" as gross income derived by an organization from any unrelated trade or business regularly carried on by it, less the deductions directly attributable to such business activity.

Section 513(a) of the Code defines the term "unrelated trade or business" as any trade or business the conduct of which is not substantially related (aside from the need of the organization for income or funds or the use it makes of the profits derived) to the exercise or performance by an organization of the purpose or function constituting the basis for its exemption.

Section 1.513-1(a) of the regulations defines "unrelated business taxable income" to mean gross income from any unrelated trade or business regularly carried on. Section 1.513-1(b) states that the phrase "trade or business" includes activities carried on for the production of income and which possess the characteristics of a trade or business within the meaning of section 162 of the Code. Finally, section 1.513-1(c) of the regulations explains that "regularly carried on" has reference to the frequency and continuity of the conduct of an activity and the manner in which the activity is pursued.

Section 1.513-1(d)(2) of the regulations provides that a trade or business is "related" to exempt purposes only where the conduct of the business activity has a causal relationship to the achievement of any exempt purpose, and is "substantially related" for purposes of section 513 of the Code, only if the causal relationship is a substantial one. Thus, for the conduct of a trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes.

Rationale:

Since after the Reorganization, T will continue to provide and arrange for services for at-risk, abused, neglected and abandoned children, its current tax-exempt status under section 501(c)(3) of the Code and classification as an organization described in section 509(a)(2) will not be adversely affected by the Reorganization.

The restructuring of T and the transfer of assets to V, W, X, and Y pursuant to the Reorganization will not adversely affect their exempt status as organizations described in section 501(c)(3) of the Code. V, W, X and Y will perform the same functions that T formerly performed or could have performed in furtherance of its exempt purposes, which are charitable as described in section 1.501(c)(3)-1(d)(2) of the regulations, and the promotion of health as described in Rev. Rul. 69-545. See also Rev. Rul. 78-41 and Rev. Rul. 67-149. The activities performed by V, W, X and Y support T's exempt purposes and would not jeopardize their statuses as supporting organizations under section 509(a)(3).

The transfer of assets and/or funds pursuant to the Reorganization will be one-time transfers and therefore, will not possess the characteristics of a trade or business "regularly carried on" within the meaning of sections 1.513-1(b) and 1.513-1(c) of the regulations. Following the Reorganization, the sharing of services and facilities, whether or not a fee is

charged, and transfers of cash and assets among the exempt organizations will be substantially related to the exercise or performance of their exempt purposes and will, therefore, not constitute unrelated trade or business activities within the meaning of section 513 of the Code and sections 1.513-1(a) and 1.513-1(d)(2) of the regulations. Each organization will be merely supplying a related charitable organization with a service or facility necessary for, and in furtherance of, the performance of its own exempt functions under section 501(c)(3). See Rev. Rul. 69-463.

Based on all the facts and circumstances described above, we rule as follows:

1. The Reorganization and resulting corporate structure will not adversely affect the continued tax-exempt status of T, V, W, X and Y under section 501(c)(3) of the Code.
2. The Reorganization and resulting corporate structure will not adversely affect the continued public charity status of T, V, W, X and Y under section 509(a) of the Code.
3. Any transfer of funds, assets, services and/or personnel in connection with the Reorganization and any subsequent sharing of funds, assets, services and or personnel by and among T, V, W, X and Y that are related to the Reorganization will not jeopardize the continued section 501(c)(3) exempt status of the organization providing such funds, assets, services and/or personnel.
4. Any payments for transfer of funds, assets, services and/or personnel in connection with the Reorganization and any payments in connection with the subsequent sharing of funds, assets, services and/or personnel by and among T, V, W, X, or Y that are related to the Reorganization will not generate unrelated business taxable income under sections 511 through 513 of the Code.

This ruling 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.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

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

Sincerely,

Steven B. Grodnitzky
Manager, Exempt Organizations
Technical Group 1

Enclosure
Notice 437