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Date 4-22-86

Surname [REDACTED]

MAR 10 1986

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(c)(3) of the Internal Revenue Code.

The information submitted indicates that you are an organization which was conceived of by the [REDACTED] to serve as a vehicle for more efficient and cost effective conduct of the management and administration of both corporations and others of a similar nature. Both [REDACTED] and [REDACTED] are recognized as exempt from federal income tax under section 501(c)(3) of the Code.

You were incorporated on [REDACTED]. Article IIB. of your Articles of Incorporation indicates that the specific purpose for which you were organized is "to provide nursing therapy and support services for the sick within the State of [REDACTED]; to provide administrative, management and other non-direct support services and counsel to nonprofit agencies within the State of [REDACTED] engaged in health care or health-care related services." In an amendment filed with the State of [REDACTED] on [REDACTED] of your Articles of Incorporation was amended to provide that you are organized and operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Internal Revenue Code.

Your services are provided to health-care providers for a fee which is determined based on the actual cost incurred by you in providing such services. Each provider must bear its proportionate share of the costs to you for providing services. You have indicated that this will result in savings to the providers and enable them to more successfully fulfill their objectives. Services include bookkeeping, billing, accounting and purchasing services, as well as recommendations as to personnel changes, personnel tracking and other general management and administrative duties.

To receive services from you an organization must be a health-care provider which abides by Title [REDACTED] of the [REDACTED] Administrative Code, [REDACTED], relating to licensing and certification of health facilities and referral agencies issued by the [REDACTED] State Department of Health Services pursuant to the Health Insurance for Aged Act of 1965-Title 18 of the Social Security Act. You do not show as a requirement that the health-care provider must be an organization recognized as exempt from federal

income tax under section 501(c)(3) of the Code, nor do you indicate any additional requirements that must be met by a health-care provider to receive services from you.

Your Board of Directors consists of the members of the Boards of Directors of [REDACTED], [REDACTED], and [REDACTED], the health-care providers for which you currently provide services. However, there is no provision in your by-laws that your Board of Directors is restricted to members of the Boards of Directors of health-care providers for which you provide services. No Board member of either [REDACTED], [REDACTED], or [REDACTED] serves on the Board of either of the other organizations.

You have indicated that your financial support will be derived from voluntary contributions from individuals and organizations and from payment for services rendered or contracted for. You have planned no fundraising programs as it is anticipated that the services you provide will generate sufficient funds to cover operating expenses. The financial information submitted shows revenues to be solely from the three health-care providers receiving services.

You operate with your own separate staff. Your staff roster includes an Executive Director, Director of Finance, Director of Community Services, Director of Administrative Services, Director of Community Relations, Accountant, Administrative Assistant, Executive Secretary, two Bookkeepers, Secretary and Receptionist.

You have indicated that your activities consist solely of providing management and administrative services. You enter into agreements with health-care providers to provide administrative and management services to such providers. You have entered into a contract with [REDACTED], a non-profit public benefit corporation, which was effective [REDACTED], to assume the exclusive management and administrative control of its day-to-day affairs. (The information submitted does not specify whether [REDACTED] is recognized by the Internal Revenue Service as a section 501(c)(3) organization.) You have also entered into oral agreements with [REDACTED] and [REDACTED] which were effective [REDACTED]. You have indicated that you had no assets prior to [REDACTED] and your obligations with respect to the agreement of [REDACTED] were met by [REDACTED] which undertook management of [REDACTED] until [REDACTED]. Management personnel were paid by [REDACTED] and transferred to you on [REDACTED].

The fees to be paid by [REDACTED] and [REDACTED] are determined based on time studies of management staff. Expenses are determined based on actual cost and allocated to each provider based on square footage, number of employees, or usage. Your agreement with [REDACTED] provided that you would receive as compensation for your services: \$ [REDACTED] for [REDACTED], \$ [REDACTED] for [REDACTED], \$ [REDACTED] for [REDACTED], \$ [REDACTED] for [REDACTED], \$ [REDACTED] each month for [REDACTED] through [REDACTED]; and after [REDACTED], the fees charged [REDACTED] will be based on actual cost, computed in the same manner as for [REDACTED] and [REDACTED].

Section 501(c)(3) of the Code provides for the exemption of organizations organized and operated exclusively for charitable purposes.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c) provides that an organization will be regarded as operated exclusively for one or more exempt purposes only if it engages in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense. Such term includes: relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments or works; lessening the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency.

Section 1.501(c)(3)-1(e)(1) of the regulations provides that, in general, an organization may meet the requirements of section 501(c)(3) of the Code although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513. In determining the existence or non-existence of such primary purpose, all the facts and circumstances must be considered, including the size and extent of the trade or business and the size and extent of the activities which are in furtherance of one or more exempt purposes. An organization which is organized and operated for the primary purpose of carrying on an unrelated trade or business is not exempt under section 501(c)(3).

Revenue Ruling 71-529, 1971-2 C.B. 234, states that a nonprofit organization that provides assistance and management of endowment and investment funds for participating colleges and universities (all exempt under section 501(c)(3)) for a charge substantially below the cost to the provider qualifies for exemption under section 501(c)(3) of the Code. The Revenue Ruling concludes that the organization performs an essential function for charitable organizations and by performing the function at a charge that is substantially below the cost it incurs, it is performing a charitable activity. Most of the operating expenses were paid for by grants from independent charitable organizations.

Revenue Ruling 72-369, 1972-2 C.B. 245, states that an organization formed to provide managerial and consulting services at cost to unrelated 501(c)(3) exempt organizations does not qualify for exemption under section 501(c)(3). The organization entered into agreements with the 501(c)(3) exempt organizations to provide management and consulting services on a cost basis with the objective of improving the administration of the charitable programs of the organizations. The organization's receipts were from services rendered and its disbursements were for operating expenses. The revenue ruling states: "Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable."

An organization is not recognized as exempt merely because its operations are not conducted for the purpose of producing a profit. To satisfy the "operational test," the organization's resources must be devoted to purposes that qualify as exclusively charitable within the meaning of section 501(c)(3) of the Code and applicable regulations.

An organization operated for the primary purpose of carrying on a trade or business ordinarily carried on for profit does not qualify for exemption from taxation under section 501(c)(3) unless the service is provided to a participating section 501(c)(3) organizations at a charge substantially below cost as described in Rev. Rul. 71-529.

Your provision of administrative and management services for participating health-care providers (three unrelated non-profit organizations) and the related functions which you undertake in return for payment, is a trade or business of the type ordinarily carried on for profit. The fact that the charges for services will only cover your expenses is not sufficient to characterize your activities as charitable within the meaning of section 501(c)(3). Your services will be provided at cost and not on a substantially below cost basis as is the case in Rev. Rul. 71-529. Your sole activity of operating a management and administrative services organization is inherently commercial in nature and is not consistent with exemption under section 501(c)(3).

Therefore, we conclude that you are not operated exclusively for one or more of the purposes described in section 501(c)(3) of the Code. You are required to 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 with a full explanation of your reasoning. This statement, signed by one of your principal officers, must be submitted in duplicate 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 a 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 principal officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Procedures.

[REDACTED]

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(f)(2) of the Code provides, in part, that a declaratory judgment or decree under that section shall not be issued in any proceeding unless the Tax Court, Claims Court, or 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 Service.

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to the District Director, San Francisco, California, which is your key district for exempt organization matters. Thereafter, any question about your federal income tax status or the filing of tax returns should be addressed to that office. When sending additional letters with respect to this case to the Internal Revenue Service, you will expedite their receipt by placing the following symbols on the envelope: (P:1:10:1, Room 6514. These symbols do not refer to your case, but rather to its location.

In accordance with section 6104(c) of the Code, the appropriate state officials will be notified of this action.

Sincerely yours,

(signed) [REDACTED]

[REDACTED]
Chief, Exempt Organizations
Rulings Branch

cc: ED, San Francisco
Attn: EO Group

cc: [REDACTED]