Internal Revenue Service

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Date [redacted]

Surname [redacted]

[redacted]

Department of the Treasury

Washington, DC 20224

Contact Person: [redacted]

Telephone Number: [redacted]

In Reference to: [redacted]

Date: [redacted]

Employer Identification Number: [redacted]
Key District: [redacted]

Dear Applicant:

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.

FACTS

You were incorporated on [redacted] as a non-profit membership corporation under the [redacted] Non-Profit Corporation Code.

Your sole member is [redacted] ("[redacted]"). [redacted] is also the sole member of [redacted] ("[redacted]") and [redacted], ("[redacted]."). All of these organizations are exempt under section 501(c)(3) of the Code. [redacted] is a general acute care community hospital located in [redacted], [redacted]. [redacted] operates primary care medical clinics, diagnostic labs and psychiatric practices and performs collection services.

Managed care payers are requiring that hospitals in [redacted] contract on a global capitation basis. Under this arrangement, one fee is paid to one payee for all medical and hospital services provided to the payers' participants or enrollees. To provide this centralized delivery system, hospitals must form contractual alliances with physicians and ancillary health care providers. This arrangement provides a mechanism whereby the managed care payers can contract with and make payment to one entity for both hospital and physician health care. To accomplish this objective, [redacted] formed your organization to act as a supporting organization for [redacted].

[redacted]

You contract with the [redacted], physicians and ancillary care providers to provide a single contracting entity for managed care payers. You seek and negotiate contracts with managed care payers on behalf of the [redacted] and contracting physicians and ancillary care providers. In addition, you provide credentialing of health care providers, medical quality review and improvement activities, and you review and improve the utilization of health care resources.

Your activities consist of credentialing and contracting with physicians and ancillary care providers ([redacted]%), seeking and negotiating contracts with managed care payers and administering these contracts on behalf of [redacted] and the contracting physicians and ancillary care providers ([redacted]%), and performing medical quality review and improvement activities and review and improvement of utilization of health care resources ([redacted]%).

Your Bylaws provide that you have two classes of members: (1) [redacted] and its subsidiaries, and (2) "Clinician Participants." Clinician Participants consist of (1) independent primary care physicians and specialists in private practice who contract with you to provide medical services pursuant to your managed care contracts, (2) primary care physicians and specialists employed by [redacted] or one of its subsidiaries, and (3) independent primary care physicians and specialists in private practice who contract with [redacted] to provide medical services to patients of [redacted].

Your Bylaws provide that your Board of Directors consists of ten persons, of whom six are Clinician Participants in private practice, three are Directors and officers of [redacted] or [redacted], and one is a Clinician Participant who is a primary care physician employed by [redacted] or one of its subsidiaries.

You have proposed amending Article Seven of your Bylaws to provide that the [redacted] Directors and the Clinician Directors would each vote as a class. For any matter being voted upon by the Board of Directors, an affirmative vote of a majority of the members of each class in attendance at a meeting would be required for that class to cast an affirmative vote. In addition, at all times, the [redacted] class would have a [redacted] percent vote and the Clinician class would have a [redacted]% vote. Further, at meetings of the Board, a quorum for the transaction of business would be established under either of two methods: (1) attendance by at least four Clinician Directors and two [redacted] Directors, or (2) attendance by at least three [redacted] Directors. Therefore, since the [redacted] class of Directors always has [redacted] percent of the voting power, this class will always prevail over

[redacted]

the Clinician class of Directors as to every matter that is considered by your Board of Directors.

You have also proposed amending section 4.4 of your Bylaws to provide that any Director may be removed for cause by the affirmative vote of at least [redacted] percent of the total number of seats on the Board, provided that at least two [redacted] Directors vote for removal.

You have represented that [redacted] has amended its Bylaws to include a substantial conflicts of interest policy that applies to your organization as well as to the other [redacted] subsidiaries. This policy supersedes and replaces the conflicts of interest policy that currently appears in Article 12 of your Restated Bylaws.

Under Section 4.1(d) of your Restated Bylaws, [redacted] has reserved substantial powers for itself over your operations.

Under your Bylaws, the Clinician Participants must:

1. Agree to be bound by your Articles of Incorporation, your Bylaws and the Participating Physician Agreement;

2. Participate in all managed care contracts you enter into, in accordance with the Participating Physician Agreement; and

3. Pay the dues and assessments as your Board of Directors may require.

You have entered into contracts with approximately [redacted] health maintenance organizations and preferred provider organizations (collectively, "Third Party Payers") under which the health care providers in your network will provide health care services for the Third Party Payers' members at the capitated or fee-for-service rates set forth in these contracts.

You have established a network of health care providers, including [redacted], [redacted] and [redacted]. The agreements with your Clinician Participants state that they will provide health care services pursuant to the managed care contracts you have entered into with the Third Party Payers. See, e.g., [redacted] section 3.3.

Under your agreements with the Clinician Participants, in order to pay the expenses associated with marketing, administration, billing, collection, contract negotiation,

[redacted]

supplies and other operating matters, each provider agrees to pay you a "Network Fee," which may be based on either (1) a fixed percentage of the compensation you collect on behalf of the provider and/or received by the provider for health care services performed pursuant to your managed care agreements, (2) a flat fee, or (3) a combination of these two. These agreements provide that you may either withhold the fee from the providers' compensation that is paid to you or bill the providers on a monthly basis. See, e.g., Physician Provider Services Agreement, section 3.2. At the present time, the annual Network Fee is $[redacted] for each active physician specialist, $[redacted] for each associate physician specialist, $[redacted] for each primary care physician and $[redacted] for each allied health provider. For the years ended [redacted], [redacted] and [redacted], [redacted], you expect that [redacted] percent of your revenue will be derived from these fees.

You have submitted no evidence that you independently provide health care services for medically underserved persons, such as Medicare or Medicaid beneficiaries or indigent persons, or that your otherwise engage in health care activities that benefit the community as a whole.

LAW

A. Stand Alone Basis for Exemption

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

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order for an organization to be exempt as one described in section 501(c)(3) of the Code, it must be both organized and operated exclusively for one or more exempt purposes. Under section 1.501(c)(3)-1(d)(1)(i)(b) of the regulations, an exempt purpose includes a charitable purpose.

Section 1.501(c)(3)-1(d)(2) of the 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 (1959); 4A Scott and Fratcher, The Law of Trusts, sections 368, 372 (4th ed. 1989); Rev. Rul. 69-545, 1969-2 C.B. 117.

[redacted]

Section 1.501(c)(3)-1(b)(1) of the regulations provides that an organization is organized exclusively for one or more exempt purposes only if its articles of organization (a) limit the purposes of such organization to one or more exempt purposes and (b) do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the regulations 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. 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(e)(1) of the regulations states that 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) of the Code.

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279, 283 (1945), the 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."

In Rev. Rul. 69-545, 1969-2 C.B. 117, the Service established the community benefit standard as the test by which the Service determines whether a hospital is organized and operated for the charitable purpose of promoting health.

Geisinger Health Plan v. Commissioner, 985 F.2d 1210 (3rd Cir. 1993), rev'g 62 TCM 1656 (1991) ("Geisinger II"), held that a prepaid health care organization that arranges for the provision of health care services only to its members benefits its members, not the community as a whole and therefore does not promote health in a charitable sense. Under the community benefit standard, the organization must benefit the community as a whole in addition to its members. In concluding that the organization did not qualify for exemption under section 501(c)(3) on the basis of promoting health, the court of appeals stated that an organization must meet a "flexible community benefit test based on a variety of indicia."

Rev. Rul. 75-197, 1975-1 C.B. 156, held that a nonprofit organization that operates a free computerized donor authorization retrieval system to facilitate transplantation of

[redacted]

body organs upon a donor's death qualifies for exemption under section 501(c)(3) of the Code because by facilitating the donation of organs which will be used to save lives, it is serving the health needs of the community and therefore is promoting health within the meaning of the general law of charity.

Rev. Rul. 77-68, 1977-1 C.B. 142, held that a nonprofit organization formed to provide individual psychological and educational evaluations, as well as tutoring and therapy, for children and adolescents with learning disabilities qualified for exemption under section 501(c)(3) of the Code because it both promoted health and advanced education. Because its services are designed to relieve psychological tensions and thereby improve the mental health of the children and adolescents, it promoted health.

In Rev. Rul. 77-69, 1977-1 C.B. 143, an organization was formed as a Health Systems Agency (HSA) under the National Health Planning and Resources Development Act of 1974. As an HSA, the organization's primary responsibility was the provision of effective health planning for a specified geographic area and the promotion of the development within that area of health services, staffing and facilities that met identified needs, reduced inefficiencies and implemented the HSA's health plan. The revenue ruling concluded that by establishing and maintaining a system of health planning and resources development aimed at providing adequate health care, the HSA was promoting the health of the residents of the area in which it functioned. Therefore, the HSA qualified for exemption under section 501(c)(3) of the Code on the basis that it promoted health.

Rev. Rul. 81-298, 1981-1 C.B. 328, held that a nonprofit organization that provides housing, transportation and counseling to hospital patients' relatives and friends who travel to the locality to assist and comfort the patients qualifies for exemption under section 501(c)(3) of the Code because it promotes health by helping to relieve the distress of hospital patients who benefit from the visitation and comfort provided by their relatives and friends.

In Professional Standards Review Organization of Queens County, Inc. v. Commissioner, 74 T.C. 240 (1980), acq., 1980-2 C.B. 2 ("Queens County PSRO"), the Tax Court held that an organization that reviewed the propriety of hospital treatment provided to Medicare and Medicaid recipients was exempt under section 501(c)(3) of the Code because it lessened the burdens of government and promoted the health of persons eligible for Medicare and Medicaid.

[redacted]

In Rev. Rul. 81-276, 1981-2 C.B. 128, the Service held that a PSRO qualifies for exemption under section 501(c)(3) of the Code because it lessens the burdens of government and promotes the health of the beneficiaries of the Medicare and Medicaid programs.

Federation Pharmacy Services, Inc. v. Commissioner, 72 T.C. 687 (1979), aff'd, 625 F.2d 804 (8th Cir. 1980), held that while selling prescription pharmaceuticals promotes health, pharmacies cannot qualify for recognition of exemption under section 501(c)(3) on that basis alone.

Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), involved an organization that operated restaurants and health food stores with the intention of furthering the religious work of the Seventh-Day Adventist Church as a health ministry. However, the Seventh Circuit held that these activities were primarily carried on for the purpose of conducting a commercial business enterprise. Therefore, the organization did not qualify for recognition of exemption under section 501(c)(3) of the Code.

Rev. Rul. 70-535, 1970-2 C.B. 117, describes an organization formed to provide management, development and consulting services for low and moderate income housing projects for a fee. The revenue ruling held that the organization did not qualify for exemption under section 501(c)(4) of the Code.

Rev. Rul. 54-305, 1954-2 C.B. 127, involves an organization whose primary purpose is the operation and maintenance of a purchasing agency for the benefit of its otherwise unrelated members who are exempt as charitable organizations. The ruling held that the organization did not qualify under section 101(6) of the Code (the predecessor to section 501(c)(3)) because its activities consisted primarily of the purchase of supplies and the performance of other related services. The ruling stated that such activities in themselves cannot be termed charitable, but are ordinary business activities.

Rev. Rul. 69-528, 1969-2 C.B. 127, describes an organization formed to provide investment services on a fee basis only to organizations exempt under section 501(c)(3) of the Code. The organization invested funds received from participating tax-exempt organizations. The service organization was free from the control of the participating organizations and had absolute and uncontrolled discretion over investment policies. The ruling held that the service organization did not qualify under section 501(c)(3) of the Code and stated that providing investment services on a regular basis for a fee is a trade or business ordinarily carried on for profit.

[redacted]

Rev. Rul. 72-369, 1972-3 C.B. 245, deals with an organization formed to provide management and consulting services at cost to unrelated exempt organizations. This revenue ruling held that providing managerial and consulting services on a regular basis for a fee is a trade or business that is ordinarily carried on for profit. The fact that the services in this case were provided at cost and solely for exempt organizations was not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Code.

In Rev. Rul. 77-3, 1977-1 C.B. 140, a nonprofit organization that provides rental housing and related services at cost to a city for its use as free temporary housing for families whose homes have been destroyed by fire is not a charitable organization exempt under section 501(c)(3) of the Code.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the organization entered into consultant-retainer relationships with five or six limited resource groups involved in the fields of health, housing, vocational skills and cooperative management. The organization's financing did not resemble that of the typical section 501(c)(3) organization. It had neither solicited, nor received, any voluntary contributions from the public. The court concluded that because its sole activity consisted of offering consulting services for a fee, set at or close to cost, to nonprofit, limited resource organizations, it did not qualify for exemption under section 501(c)(3) of the Code.

In Christian Stewardship Assistance, Inc. v. Commissioner, 70 T.C. 1037 (1978), a nonprofit corporation that assisted charitable organizations in their fund raising activities by providing financial planning advice on charitable giving and tax planning to wealthy individuals was held not to qualify for exemption under section 501(c)(3) of the Code because its tax planning services were a substantial nonexempt activity enabling the corporation to provide commercially available services to wealthy individuals free of charge.

B. Integral Part Basis for Exemption

Section 502 of the Code states that an organization operated for the primary purpose of carrying on a trade or business for profit is not tax exempt on the ground that all of its profits are payable to one or more tax-exempt organizations.

Section 1.502-1(b) of the regulations provides that a subsidiary organization of a tax exempt organization may be exempt on the ground that the activities of the subsidiary are an integral part of the exempt activities of the parent

[redacted]

organization. However, the subsidiary is not exempt from tax if it is operated for the primary purpose of carrying on a trade or business which would be an unrelated trade or business if regularly carried on by the parent organization.

In Rev. Rul. 78-41, 1978-1 C.B. 148, a trust created by a hospital to accumulate and hold funds to pay malpractice claims against the hospital was determined to be an integral part organization because the hospital exercised significant financial control over the trust. This was because the trustee was required to make payments to claimants at the direction of the hospital, the hospital provided the funds for the trust and the hospital directed where the funds from the trust were to be paid.

Geisinger Health Plan v. Commissioner, 100 T.C. 394 (1993), ("Geisinger III"), aff'd, 30 F.3d 494 (3rd Cir. 1994) ("Geisinger IV"), held that a prepaid health plan did not qualify for exemption under section 501(c)(3) of the Code based on the integral part doctrine of section 1.502-1(b) of the regulations.

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 such organization of the purpose or function constituting the basis for its exemption.

Section 513(a)(2) of the Code provides that the term "unrelated trade or business" does not include any trade or business which is carried on, in the case of an organization described in section 501(c)(3), such as a hospital, by the organization primarily for the convenience of its patients.

Section 1.513-1(a) of the regulations defines "unrelated business taxable income" to mean gross income derived by an organization from any unrelated trade or business regularly carried on by it, less directly connected deductions and subject to certain modifications. Therefore, gross income of an exempt organization subject to the tax imposed by section 511 of the Code is includible in the computation of unrelated business taxable income if: (1) it is income from trade or business; (2) such trade or business is regularly carried on by the organization; and (3) the conduct of such trade or business is not substantially related (other than through the production of funds) to the organization's performance of its exempt functions.

Section 1.513-1(b) of the regulations states that the phrase "trade or business" includes activities carried on for the production of income which possess the characteristics of a trade

[redacted]

or business within the meaning of section 162 of the Code. Section 1.513-1(c) of the regulations explains that "regularly carried on" has reference to the frequency and continuity with which the activities productive of the income are conducted and the manner in which they are pursued.

Section 1.513-1(d)(1) of the regulations states that the presence of the substantially related requirement necessitates an examination of the relationship between the business activities which generate the particular income in question -- the activities, that is, of producing or distributing the goods or performing the services involved -- and the accomplishment of the organization's exempt purposes.

Section 1.513-1(d)(2) of the regulations states 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 an exempt purpose, and is substantially related for purposes of section 513, 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.

Section 1.513-1(d)(4)(i) of the regulations states that gross income derived from charges for the performance of exempt functions does not constitute gross income from the conduct of unrelated trade or business.

RATIONALE

A. Stand Alone Basis for Exemption

Under the regulations, an organization that is organized and operated exclusively for charitable purposes may qualify for exemption under section 501(c)(3) of the Code. The promotion of health has long been recognized as a charitable purpose.

Whether a hospital promotes health in a charitable manner is determined under the community benefit standard of Rev. Rul. 69-545, supra. This standard focuses on a number of factors to determine whether the hospital benefits the community as a whole rather than private interests. The application of the community benefit standard to exempt hospitals and other exempt health care organizations was sustained in Eastern Kentucky Welfare Rights Org. v. Simon, 506 F.2d 1278 (D.C. Cir. 1974), vacated on other

[redacted]

grounds, 426 U.S. 26 (1975); and in Sound Health Association v. Commissioner, 71 T.C. 158 (1978), acq., 1981-2 C.B. 2.

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The Service and the courts have recognized that the promotion of health includes activities other than the direct provision of patient care. See Rev. Rul. 81-298, supra; Rev. Rul. 81-276, supra; Rev. Rul. 77-69, supra; Rev. Rul. 77-68, supra; Rev. Rul. 75-197, supra; and Queens County PSRO, supra.

However, an organization that merely promotes health, without more, is not entitled to recognition of exemption under section 501(c)(3) of the Code. See Living Faith, Inc. v. Commissioner, supra; and Federation Pharmacy Services, Inc. v. Commissioner, supra.

You have contracted with Third Party Payers to arrange for the provision of health care services to their members by a network of various health care providers. These providers consist of Clinician Participants, who are independent physicians engaged in the private practice of medicine; and [redacted] and [redacted], which are related organizations. By arranging for the provision of health care services primarily by unrelated physicians, for members of Third Party Payers, a limited groups of persons not medically underserved, while providing no more than incidental benefits to the community as a whole, you do not satisfy the community benefit standard of Rev. Rul. 69-545, supra. Thus, although your activities promote health, they do not promote health in a charitable manner.

Furthermore, a nonprofit organization that provides ordinary business services for one or more exempt health care organizations does not promote health in a charitable sense. See Rev. Rul. 70-535, supra; Rev. Rul. 54-305, supra; Rev. Rul. 69-

[redacted]

528, supra; Rev. Rul. 72-369, supra; Rev. Rul. 77-3, supra; B.S.W. Group, Inc. v. Commissioner, supra; and Christian Stewardship Assistance, Inc. v. Commissioner, Inc., supra. By providing marketing, administration, billing, collection, contract negotiation, and supplies for unrelated physicians in return for a Network Fee, you are engaged in performing ordinary business services, activities that do not promote health in a charitable manner.

You are also providing services directly for the independent health care providers for which you receive a Network Fee. The provision of these services -- marketing, administration, billing, collection, contract negotiation, supplies and other operating matters -- are ordinary commercial activities. The provision of these services does not constitute the promotion of health in a charitable manner. One hundred percent of your revenue is derived from the performance of these commercial activities. Thus, because these activities are not insubstantial, you are not operated exclusively for a charitable purpose. See section 1.501(c)(3)-1(c)(1) of the regulations and Better Business Bureau of Washington, D.C. v. United States, supra.

In Geisinger II, supra, the court of appeals held that an HMO did not qualify for exemption under section 501(c)(3) of the Code because arranging for the provision of health care services exclusively for the organization's members primarily benefited the members, not the community as a whole. Under the community benefit standard, the organization must benefit the community as a whole in addition to its members. In concluding that the organization did not qualify for exemption under section 501(c)(3) on the basis of promoting health, the court of appeals stated that an organization must meet a "flexible community benefit test based on a variety of indicia." Your activities, taken as a whole, primarily benefit the Third Party Payers and their members, not the community as a whole. Therefore, you do not satisfy the "flexible community benefit test based on a variety of indicia" established in Geisinger II.

Therefore, you do not qualify for exemption under section 501(c)(3) of the Code as a charitable organization on the basis that you promote health.

B. Integral Part Basis for Exemption

Under section 1.502-1(b) of the regulations, one organization may derive its exemption from a related organization exempt under section 501(c)(3) of the Code if the former organization is an integral part of the exempt organization. To

[redacted]

obtain exemption derivatively, two requirements must be met: (1) the two organizations must be "related" and (2) the subordinate entity must perform "essential" services for the parent. Section 1.502-1(b) of the regulations includes the following example of an organization that is considered as providing essential services: a subsidiary which is operated for the sole purpose of furnishing electric power used by its parent organization, a tax-exempt educational organization, in carrying on its educational activities. See also Rev. Rul. 78-41, supra.

Under section 1.502-1(b) of the regulations, a subsidiary organization that is engaged in an activity that would be considered an unrelated trade or business if it were regularly carried on by the exempt parent does not provide an essential service for the parent. The regulations include an example of a subsidiary organization that is operated primarily for the purpose of furnishing electric power to consumers other than its parent organization. However, the subsidiary is not exempt from tax if it is operated for the primary purpose of carrying on a trade or business which would be an unrelated trade or business if regularly carried on by the parent organization.

Thus, if the subsidiary organization were owned by several unrelated exempt organizations and operated for the purpose of furnishing electric power to each of them, it would not be exempt because the business would be an unrelated trade or business if regularly carried on by any one of the tax-exempt organizations. For this purpose, organizations are related only if they consist of a parent and one or more of its subsidiaries, or subsidiaries having a common parent. An exempt organization is not related to another exempt organization merely because they both engage in the same type of exempt activities. See section 1.502-1(b) of the regulations.

(1) Related. The members of your organization are [redacted] and Clinician Participants, both of which elect your Board of Directors. Your Board consists of [redacted] Clinician Participants and [redacted] representatives. However, your Restated Bylaws provide that [redacted] has [redacted]% voting power on all matters considered by the Board; [redacted] has reserved for itself substantial powers over your operations; amendments to your Bylaws may not be made without the approval of [redacted]; and Directors may be removed only with the participation of MedCorp directors. Therefore, because [redacted] has effective control over your organization, it is considered related for purposes of section 1.502-1(b) of the regulations.

(2) Essential Services. Your activities consist of arranging for the provision of health care services by

[redacted]

independent physicians for members of your Third Party Payers. If MedCorp or Medical Center regularly performed these activities, they would constitute an unrelated trade or business because, as explained previously, these activities do not constitute the promotion of health in a charitable manner. In addition, because these activities would not contribute importantly to the accomplishment of either organization's exempt purpose of promoting the health of the community, they would not have a substantial causal relationship, as described in section 1.513-1(d)(2) of the regulations, to the achievement of either organization's exempt purpose. Thus, your activities, if performed by [redacted] or [redacted], would be considered an unrelated trade or business. Therefore, under section 1.502-1(b) of the regulations, your activities are not considered essential services.

Further, in Geisinger III, supra, the Tax Court held that a prepaid health plan created by an exempt hospital system was not an integral part of the system because a substantial portion of the enrollees of the plan, approximately [redacted], were not patients of the exempt hospitals in the system. The Tax Court reasoned that providing services to such a significant number of non-system patients precluded a finding that the plan's activities were devoted to furthering the exempt purposes of the system hospitals.

In Geisinger IV, supra, the Third Circuit Court of Appeals affirmed the Tax Court, stating that the integral part doctrine has two requirements: (1) the subordinate organization must not be engaged in activities that would be unrelated trade or business activities if the parent engaged in these activities directly, and (2) the subordinate organization's relationship to the parent must enhance (or "boost") the subsidiary's ability to accomplish charitable purposes to such a degree that the subsidiary could qualify for exemption on its own merits.

The Third Circuit concluded that the prepaid health plan did not receive any boost from its association with the exempt hospitals in the hospital system. The patients the plan provided to the system, i.e., the plan's enrollees, were the same patients that it served without its association with the hospital system. Thus, the court concluded that the plan did not satisfy the integral part test because it was not rendered "more charitable" by virtue of its association with the exempt hospitals in the system.

There is no evidence that the persons for whom you arrange the provision of health care services, i.e., the Third Party Payers' members, are patients of the [redacted]. Therefore,

[redacted]

under Geisinger III, supra, since your activities do not further the exempt purposes of Medical Center, the integral part doctrine does not apply.

Further, there is no evidence establishing that you received a charitable "boost" from the [redacted]. The patients you provide to the [redacted], the Third Party Payers' members, are the same persons that you would serve without your association with the [redacted]. Therefore, under Geisinger IV, supra, since you are not rendered "more charitable" by virtue of your association with [redacted], the integral part doctrine does not apply.

As a result, you do not qualify for exemption under section 501(c)(3) of the Code based on the integral part doctrine.

CONCLUSION

For the reasons stated above, 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, 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 Practice 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.

[redacted]

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to your key district office. Thereafter, any questions about your federal income tax status should be addressed to that office. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

[redacted]

For your convenience, our FAX number is [redacted] and my E-Mail address is: [redacted]

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

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

[redacted]

Chief, Exempt Organizations

[redacted]