

SUPPORTING ORGANIZATION REFERENCE GUIDE

IRC 509(a)(3) Foundation Status Classification

By Janet E. Gitterman

Overview

Purpose

The purpose of this article, with the accompanying guide sheet, is to provide a primer to aid in the processing of IRC 501(c)(3) exemption applications requesting non-private foundation status under IRC 509(a)(3). Such requests may be submitted as initial applications for tax exemption or as reclassifications from private foundation status.

This article is a concise presentation of information useful to determination agents. For a comprehensive review of the topic, refer to Exempt Organizations CPE Volume, FY 2003, *Article B, Public Charity or Private Foundation Status Issues under IRC 509(a)(1)-(4), 4942(j)(3), and 507*, pp. B-116 – B-145. This article does not address the subject of abusive supporting organizations that involve control by disqualified persons, or impermissible private benefit.

Exhibit 1, “*Supporting Organization*” *Exemption Application - Guide Sheet for IRC 509(a)(3) Foundation Status Classification*, is for the agent’s use in identifying issues specific to processing such applications. A “Q” followed by a number, (Q#) in the block labels (left side of page) refers to questions in the guide.

Continued on next page

Overview, Continued

In This Article This article contains the following topics:

Topic	Page
Overview	1
IRC 509(a)(3) Supporting Organization	3
Threshold Requirement: Complying With Requirements of IRC 501(c)(3)	4
Determining Eligibility for 509(a)(3) Status: Four Tests	5
Test 1: Relationship Test	7
“Operated in Connection With” - Responsiveness Sub-Test	10
“Operated in Connection With” – Integral Part Sub-Test	13
Test 2: Organizational Test	15
Test 3: Operational Test	17
Test 4: Control Test	18
Special Health Care Issues <ul style="list-style-type: none">• Hospital Systems• Hospital System: Upside-Down Relationship• 509(a)(3) Supporting another 509(a)(3)	20
Unusual Situations <ul style="list-style-type: none">• Supported Organizations Described in IRC 501(c)(4), (5), or (6)• Non-exempt Charitable Trusts and IRC 509(a)(3)	25
Exhibit 1: “ <i>Supporting Organization</i> ” <i>Exemption Application - Guide Sheet for IRC 509(a)(3) Foundation Status Classification</i>	28

IRC 509(a)(3) Supporting Organization

**Basis For
Exclusion From
Private
Foundation
Status**

An organization described in IRC 501(c)(3) is a private foundation unless it is a public charity described in IRC 509(a)(1), (2), (3), or (4). Unlike organizations excepted from private foundation status under IRC 509(a)(1) or 509(a)(2) because they receive broad public support or they are inherently public (e.g. churches, hospitals, schools, or governmental units) and IRC 509(a)(4) (public safety testing organizations), those organizations covered by the IRC 509(a)(3) exception neither receive broadly based public support nor are they inherently public charities.

**Supporting
Organization**

Rather, IRC 509(a)(3) excludes “supporting organizations” from private foundation classification because of their close relationship to publicly supported organizations classified as IRC 509(a)(1) or 509(a)(2) organizations.

**Supported
Organization**

The IRC 509(a)(1) or 509(a)(2) publicly supported organizations are commonly called “supported organizations.” The supported organization may be foreign or domestic. Rev. Rul. 74-229, 1974-1 C.B. 142.

**Requesting IRC
509(a)(3) Status**

IRC 509(a)(3) classification is most commonly requested as part of an IRC 501(c)(3) exemption application. However, 509(a)(3) classification may also be submitted as a request for a determination by:

- A charitable trust, under Rev. Proc. 72-50, 1972-2 C.B. 830;
 - A private foundation terminating under IRC 507; or
 - A public charity seeking reclassification of its foundation status under IRC 509(a).
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Threshold Requirement: Complying With Requirements of IRC 501(c)(3)

Threshold Requirement

A threshold requirement to the IRC 509(a)(3) supporting organization determination requested as part of an IRC 501(c)(3) exemption application, is whether the applicant is organized and operated exclusively for charitable purposes, and so is eligible for exemption from federal income tax under section 501(c)(3). The organization and operations of the applicant organization must comply with IRC 501(c)(3) requirements.

Stand Alone Exemption

A supporting organization may qualify under IRC 501(c)(3) based on its activities which, standing alone, further exempt purposes. For example, an organization may make grants directly to another IRC 501(c)(3) organization or to students for educational scholarships on behalf of another IRC 501(c)(3) organization.

Integral Part Doctrine: Derivative Exemption

Alternatively, a supporting organization may qualify based on the integral part doctrine by performing an essential activity on behalf of an organization, described in IRC 501(c)(3), by which it is controlled. For example, an organization that was formed and is controlled by a conference of churches to make mortgage loans to churches that are members of the conference, is qualified for exemption under IRC 501(c)(3) even though such activities, standing alone, would not justify exemption. Rev. Rul. 75-282, 1975-2 C.B. 201. Also, see Rev. Ruls. 78-41, 1978-1 C.B. 148, and 81-19, 1981-1 C.B. 353.

Determining Eligibility For IRC 509(a)(3) Status: Four Tests

Four Tests

Since the IRC 509(a)(3) private foundation exception rests on the theory that control or close supervision by an IRC 509(a)(1) or 509(a)(2) organization over the supporting organization will help prevent manipulation for private benefit that is possible in a private foundation, the statute requires the supporting organization to meet four tests:

Test 1: Relationship Test under IRC 509(a)(3)(B).

It must be operated, supervised or controlled by or in connection with one or more organizations described in IRC 509(a)(1) or 509(a)(2).

Test 2: Organizational Test under IRC 509(a)(3)(A).

It must be organized exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more organizations described in IRC 509(a)(1) or 509(a)(2).

Test 3: Operational Test under IRC 509(a)(3)(A).

It must be operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more organizations described in IRC 509(a)(1) or 509(a)(2).

Test 4: Disqualified Person Control Test under IRC 509(a)(3)(C).

It must not be controlled directly or indirectly by one or more disqualified persons (as defined in IRC 4946) other than foundation managers and other than one or more organizations described in IRC 509(a)(1) or 509(a)(2).

501(c)(4), (5) or (6)

Organizations described in IRC 501(c)(4), (5) or (6), which would be described in section 509(a)(2) if they were 501(c)(3) organizations are deemed to be included in section 509(a)(2) for purposes of these tests. See **Unusual Situations** for more detail.

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Determining Eligibility For IRC 509(a)(3) Status: Four Tests, Continued

Processing the Request

In processing a request for an IRC 509(a)(3) supporting organization, it is the relationship test that is the first that should be reviewed, despite its secondary order in both the statute and regulations. This is because the particular relationship between the supporting organization and the supported organization(s) will indicate the ease or difficulty of meeting the other tests of IRC 509(a)(3).

Each permitted relationship has particular requirements as to governing body composition, language in the governing documents, and other details of organization and operation. The “operated in connection with” relationship also requires analysis of additional sub-tests: responsiveness and integral part.

Each of the tests and sub-tests will be covered individually in this article.

Test 1: Relationship Test

Relationship Test Under IRC 509(A)(3)(B)

To be classified as a supporting organization under IRC 509(a)(3) an organization must meet one of three relationships with a supported organization described in IRC 509(a)(1) or (2). The three permitted relationships are:

Q1

1. “Operated, supervised or controlled by” one or more supported organizations, or
2. “Supervised or controlled in connection with” one or more supported organizations, or
3. “Operated in connection with” one or more supported organizations

The first two relationships depend upon the supervision and control of the supporting organization by the supported organization(s). Thus, the supporting organization’s governing board must be appointed by, or be substantially similar to, the governing board of the publicly supported organization(s).

The third relationship seeks to establish that the supporting organization is responsive to the publicly supported organization(s) and that the publicly supported organization(s) maintain significant involvement in the activities of the supporting organization.

A supporting organization may also meet the requirements of the relationship test if it has the required relationship with a supported organization that is a governmental unit described in IRC 509(a)(1) and 170(b)(1)(A)(v). A governmental unit includes the United States government; a state or a political subdivision of a state, such as a city, town or county; and a federal, state or local court.

Note: Compliance with the relationship test may be established through a provision in the supporting organization’s articles of organization or by-laws, by resolution of its governing board, or through some other evidence of a fixed right by the supported organization(s) to appoint or elect officers, directors, or trustees of the supporting organization. For example, a supporting organization established that it met the “operated, supervised or controlled by” relationship because its bylaws provide that publicly supported organizations elect a majority of its trustees. Treas. Reg. 1.509(a)-4(g)(2) at Example (2).

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Test 1: Relationship Test, Continued

“Operated, Supervised or Controlled by”
Treas. Reg. 1.509(a)-4(g)

“Operated, supervised or controlled by” is akin to a parent-subsidiary relationship between supported and supporting organization. The supported public charity must be the parent entity. This relationship test requires a substantial degree of direction over the policies, programs, and activities of a supporting organization by one or more publicly supported organizations. Thus, a majority of the officers, directors, or trustees of the supporting organization must be appointed or elected by one or more of the supported organizations.

“Supervised or Controlled in Connection With”
Treas. Reg. 1.509(a)-4(h)

“Supervised or controlled in connection with” is akin to a brother-sister relationship. The regulations require common supervision and control by the persons supervising or controlling both the supported and supporting organizations. Thus, a majority of the persons who control or manage the supported organization(s) must also control or manage the supporting organization. The “same persons” does not mean representatives or appointees of the supported organization(s).

Control or management of the two organizations must be vested in the very same people, though these persons need not occupy the same office or position in both the supported and supporting organizations. G.C.M. 39508 (May 27, 1986).

An organization seeking IRC 509(a)(3) status will not be considered to be “supervised or controlled in connection with” a publicly supported organization solely by reason of its making payments to the publicly supported organization, even if the publicly supported organization has enforceable rights under state law. Treas. Reg. 1.509(a)-4(h)(2).

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Test 1: Relationship Test, Continued

**“Operated in
Connection
With”
Treas. Reg.
1.509(a)-4(i)**

The **“operated in connection with”** relationship requires that the supporting organization also meet two sub-tests:

- A responsiveness sub-test and
- An integral part sub-test

Organizations that were supporting or benefiting IRC 509(a)(1) or 509(a)(2) organizations before November 20, 1970 are eligible for an exception that takes into account facts and circumstances related to the historic and continuing relationship in determining whether the responsiveness and integral part sub-tests are met. Treas. Reg. 1.509(a)-4(i)(1)(ii) and (iii) and 1.509(a)-4(i)(4).

“Operated in Connection With” - Responsiveness Sub-Test

Responsiveness Sub-Test
Q2

This sub-test is designed to ensure that the supporting organization is responsive to the needs or demands of the supported organization(s). The supporting organization must comply with one of two alternative sub-tests of responsiveness.

Responsiveness Sub-Test #1: Part 1

Responsiveness sub-test #1 is a two-part analysis. It first requires the supporting organization demonstrate that one of the following arrangements exists:

- One or more of its officers, directors, or trustees are elected or appointed by the officers, directors, trustees, or membership of the supported organization(s);
- One or more members of the governing bodies of the supported organization(s) are also officers, directors, or trustees of, or hold other important offices in, the supporting organization; or
- The officers, directors, or trustees of the supporting organization maintain a close and continuous working relationship with the officers, directors, or trustees of the supported organization(s).

Treas. Reg. 1.509 (a)-4(i)(2)(ii).

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“Operated in Connection With” - Responsiveness Sub-Test, Continued

**Responsiveness
Sub-Test #1:
Part 2**

Once the arrangement is shown, the supporting organization faces an additional hurdle. It must demonstrate that, by reason of such arrangement, the officers, directors, or trustees of the supported organization(s) have a significant voice in:

- The investment policies of the supporting organization,
- The timing of grants,
- The manner of making grants,
- The selection of recipients by the supporting organization, and
- In otherwise directing the use of the income or assets of the supporting organization.

However, a mere working relationship between representatives of the organizations that involves only the selection of grantees may not satisfy this test because the supported organization does not have a significant voice in directing the use of the supporting organization's income or assets. Rev. Rul. 75-437, 1975-2 C.B. 217; Lapham Foundation, Inc. v. Commissioner, T.C. Memo 2002-293 (2002).

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“Operated in Connection With” - Responsiveness Sub-Test, Continued

Responsiveness Sub-Test #2 (Alternative Responsiveness Sub-Test) This sub-test is for trusts that do not satisfy the responsiveness test described for Sub-Test #1.

Responsiveness sub-test # 2 requires that:

Q3

- The supporting organization is a charitable trust under state law,
- Each specified supported organization is a named beneficiary under the trust's governing instrument, and
- The beneficiary organization has the power to enforce the trust and compel an accounting under state law.

With respect to the requirement that the beneficiary organization have the power to enforce the trust and compel an accounting, the supporting organization must produce authority under state law that the beneficiary organization(s) have such power. Further, it must be ascertained that beneficiary organization(s) will be aware they have an interest that can be enforced. Treas. Reg. 1.509(a)-4(i)(2)(iii); Roe Foundation Charitable Trust v. Commissioner, T.C. Memo 1989-566 (1989).

Additional Facts and Circumstances

For an organization that was supporting or benefiting one or more supported organizations before November 20, 1970, additional facts and circumstances, such as an historic and continuing relationship between organizations, also may be taken into consideration to establish compliance with either of the above responsiveness tests. Treas. Reg. 1.509(a)-4(i)(1)(ii).

“Operated in Connection With” – Integral Part Sub-Test

Meeting the Integral Part Sub-Test

Q4

An organization claiming the "operated in connection with" relationship will meet the integral part sub-test if it maintains significant involvement in the operations of one or more supported organizations and these organizations, in turn, are dependent upon the supporting organization for the type of support it provides.

The supporting organization can engage in activities on behalf of the supported organization(s) or it can provide financial grants for the use of one or more supported organizations. There are two alternative integral part sub-tests, depending upon the type of support provided:

1. Supporting organization engages in activities
 2. Supporting organization makes grants
-

Integral Part Sub-Test: Supporting Organization Engages in Activities

There is an integral part sub-test for supporting organizations engaging in activities. To satisfy this sub-test, two requirements must be met:

1. The activities engaged in for or on behalf of the supported organization(s) must be activities that perform the functions of, or carry out the purposes of, such organization(s); and
2. These activities, but for the involvement of the supporting organization, would normally be engaged in by the supported organization(s) themselves.

The general rule is that this sub-test only applies in situations where the supporting organization actually engages in activities to benefit the supported organizations, for example, performing publishing and printing functions for a college, as opposed to simply making grants to the supported organizations or to grantees benefited by the supported organizations. G.C.M. 38417 (June 20, 1980).

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“Operated in Connection With” – Integral Part Sub-Test,

Continued

Integral Part Sub-Test: Supporting Organization Makes Grants

The supporting organization that does not engage in activities, but provides financial support must meet the following integral part sub-test:

1. The supporting organization pays substantially all of its income to or for the use of one or more supported organizations. (Rev. Rul. 76-208, 1976-1 C.B. 161, holds that "substantially all," in this context, means at least 85 percent of the supporting organization's income);
2. The amount of support received by one or more of the supported organizations must be sufficient to insure the attentiveness of the organization or organizations to the operations of the supporting organization (this is known as the "attentiveness requirement"); and
3. A significant amount of the total support of the supporting organization must go to those supported organizations that meet the attentiveness requirement.

Even if the payment by the supporting organization is not sufficiently large and significant in terms of amount in comparison with the total support measured, it will meet this test if the absence of the amount would interrupt a particular substantial activity or program of the recipient. The payment must be earmarked for a particular substantial program or activity by the supported or the supporting organization for this test to be met.

Where the payment is made to or for the use of a particular department of a recipient, such as the pediatric ward of a hospital, then the total support of the ward can be substituted for the total support of the supported organization to determine whether it is sufficiently large to ensure attentiveness. In all cases, a substantial amount must be paid to an “attentive charity.” Treas. Reg. 1.509(a)-4(i)(3)(iii) and refer to CPE 2003 Article B, pp. 127-136 for more coverage of this topic.

Test 2: Organizational Test

**Organizational
Test – Treas.
Reg. 1.509(a)-
4(c) and (d)**

Q5

This test requires that the supporting organization have specific appropriate language in its articles of organization (governing instrument). IRC 509(a)(3)(A) requires that a supporting organization must be organized and at all times operated exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in IRC 509(a)(1) or 509(a)(2).

Permitted purposes in the governing document of a supporting organization may:

- Contain some or all of the specific purposes of the IRC 509(a)(1) or 509(a)(2) organization(s) that it supports, or
- State simply that it is formed “for the benefit of,” or “to perform the functions of,” one or more specified organizations described in IRC 509(a)(1) or 509(a)(2), or
- Be similar to, but no broader than, the purposes set forth in the governing instrument of the IRC 509(a)(1) or 509(a)(2) organization by which it is controlled or closely involved.

If the supporting organization is operated, supervised, or controlled by an IRC 501(c)(4), (5), or (6) organization which is deemed to be an IRC 509(a)(2) organization, the supporting organization’s articles must require it to carry on religious, charitable, scientific, literary, or educational activities within the meaning of IRC 170(c)(2) to meet the organizational test.

The supporting organization’s governing document may not expressly empower the organization to engage in activities that are not in furtherance of such purposes. The document also may not expressly empower the organization to support or benefit any organization other than the specified publicly supported organization(s).

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Test 2: Organizational Test, Continued

Organizational Test and Relationship Test Satisfying the organizational test depends on which relationship is met.

“Operated, Supervised or Controlled By” or “Supervised or Controlled in Connection With” An organization that meets the “operated, supervised or controlled by” or “supervised or controlled in connection with” relationship may specify the supported organization by name, class, or purpose. For example, a supporting organization that is “supervised or controlled in connection with” an IRC 509(a)(1) hospital that provides health care to residents of S city may state in its organizing instrument that it is formed to provide financial support to publicly supported organizations that provide health care to residents of S city.

“Operated in Connection With” An organization that meets the “operated in connection with” relationship must specify the publicly supported organization(s) by name in its organizing instrument. However, where an historic and continuing relationship between the supporting and supported organizations has created a substantial identity of interest between the organizations, this problem can be overcome by examining all the facts and circumstances.

“Operated in Connection With” An organization that meets the “operated in connection with” relationship must state in its governing document that it is formed “for the benefit of” or “to perform the functions of” one or more specified organizations described in IRC 509(a)(1) or 509(a)(2), although these exact words do not need to be used.

Test 3: Operational Test

**Operational
Test – Treas.
Reg. 1.509(a)-
4(e)**

The operational test is concerned with permissible beneficiaries and permissible activities.

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**Benefits and
Activities as
Support**

The supporting organization must engage only in activities that support or benefit the specified IRC 509(a)(1) or 509(a)(2) supported organization(s). Such activities may include making payments to or for the use of, or providing services or facilities for individual members of the charitable class benefited by the specified publicly supported organization(s).

A supporting organization is not required to pay over its income to supported organizations, but may carry on its own independent programs, designed to support or benefit the specified supported organization(s).

**Permissible
Beneficiaries**

A supporting organization may support or benefit additional organizations other than the supported organization(s) it was formed to support or benefit, including organizations described in IRC 509(a)(3), but only when the additional organizations are “permissible beneficiaries” with respect to the IRC 509(a)(1) or 509(a)(2) supported organizations.

An organization is a permissible beneficiary if it is described in IRC 501(c)(3), is other than a private foundation under IRC 509(a), and is operated, supervised or controlled directly by or in connection with the specified supported organization(s), or is described in IRC 511(a)(2)(B) (colleges and universities that are government agencies or instrumentalities).

Although a supporting organization may support a permissible beneficiary that is classified under IRC 509(a)(3), the supporting organization cannot name the other IRC 509(a)(3) organization in its organizing instrument. Only “publicly supported” organizations described in IRC 509(a)(1) or 509(a)(2) can be named in the supporting organization’s governing instrument.

Test 4: Control Test

**Control Test -
IRC
509(a)(3)(C)**

A supporting organization may not be controlled directly or indirectly by one or more disqualified persons. This control test requires a two-pronged examination:

Q7

1. Who are disqualified persons?
2. What constitutes prohibited direct or indirect control over a supporting organization by disqualified persons?

The question of control by disqualified persons arises most frequently with supporting organizations that claim to be “operated in connection with” publicly supported organizations.

**Disqualified
Persons**

For purposes of this test of control, disqualified persons include the following persons described in IRC 4946:

- A substantial contributor to the supporting organization. A substantial contributor is a person who has given more than \$5,000 to the supporting organization if this amount is also more than 2 percent of the total amount given by the end of the taxable year.
 - A creator of a trust that is a substantial contributor to a supporting organization.
 - An owner of more than 20 percent of the combined voting power of a corporation, profits interest of a partnership, or beneficial interest of a trust or unincorporated enterprise, which is a substantial contributor to a supporting organization.
 - A family member of one of the above persons.
 - A corporation, partnership or trust in which one of the above persons owns more than 35% of the combined voting power, profits interest, or beneficial interest, respectively.
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Test 4: Control Test, Continued

**Vote/Veto
Power - Treas.
Reg. 1.509(a)-
4(j)(1)**

In determining control, one must look at whether disqualified persons may, by aggregating their votes or positions of authority, require the supporting organization to act or can prevent it from acting. The general rule is that control will be found where disqualified persons have either 50 percent of the voting power or a veto power over the supporting organization's activities.

Example

If the balance of disqualified persons is three of five board members, the supporting organization would not pass the disqualified person control test.

On the other hand, if two of five board members of a supporting organization are disqualified persons, the organization would not be considered to be controlled directly by disqualified persons unless the disqualified persons have veto power over the supporting organization's operations or activities. In addition, one must consider whether disqualified persons indirectly control the supporting organization. See below.

**Foundation
Manager**

Public charities described in IRC 509(a)(1) or 509(a)(2), or foundation manager(s) can control the supporting organization even though they are otherwise disqualified persons. However, for purposes of the control test, a foundation manager who is a disqualified person for some other independent reason, such as being a substantial contributor, will be treated as a disqualified person even if appointed or designated as a foundation manager by the publicly supported beneficiary organization.

**Indirect
Control**

IRC 509(a)(3)(C) forbids both direct and indirect control by disqualified persons. Treas. Reg. 1.509(a)-4(j)(1) states that all the facts and circumstances will be considered in determining whether a disqualified person does in fact control a supporting organization, including:

- The nature, diversity, and income yield of the supporting organization's holdings,
- The length of time particular stocks, securities, and other assets are retained, and
- The manner of exercising its voting rights with respect to stocks in which members of its governing body have some interest.

Rev. Rul. 80-207, 1980-2 C.B. 193 (example of impermissible indirect control under IRC 509(a)(3)).

Special Health Care Issues

Hospital Systems

Hospital systems are frequently structured with multiple entities comprised of hospitals, clinics, ancillary service providers, and an organization that functions as the parent of the other entities, making policy and coordinating long range planning for the system. Since this parent organization is not itself a hospital nor does it have broad public support, it can only escape private foundation status by qualifying under IRC 509(a)(3) as a supporting organization.

Relationship of Parent Organization to Hospital

The “operated, supervised or controlled by” relationship is satisfied when the publicly supported organization stands in the relationship of “parent” to the supporting organization. However, in a typical hospital system, the hospital and its tax-exempt affiliates are subsidiaries of the parent, a supporting organization.

Since neither the hospital nor any of its tax-exempt affiliates stand in the relationship of parent to the parent (supporting) organization, the “operated, supervised or controlled by” relationship cannot be satisfied. Thus, the parent organization must satisfy either the “supervised or controlled in connection with” or the “operated in connection with” relationship test.

Hospital System: Upside-Down Relationship

At first glance, it appears that the parent organization cannot be an IRC 509(a)(3) supporting organization because, as the overall governing entity of the tax-exempt hospital system with the authority to appoint the governing board of the hospital and its affiliates, the supporting organization controls the public charities it is meant to support.

This is sometimes called an “upside-down relationship” because the supporting organization is actually in control of the supported organization(s). However, this relationship can be structured to allow the parent organization to qualify as a supporting organization under IRC 509(a)(3).

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Special Health Care Issues, Continued

**Meets
“Supervised or
Controlled in
Connection
With” Test**

Most upside-down relationships that qualify under IRC 509(a)(3)(B) will do so because the IRC 509(a)(3) supporting organization (parent organization) meets the “supervised or controlled in connection with” test. In order to meet this relationship test, the by-laws or articles of organization of the supporting organization will specify that a majority of persons who control it must also control or manage the supported organization(s).

**Meets
“Operated in
Connection
With” Test -
Public charity
Must Be
Named**

If the supported and supporting organizations share less than a majority of their officers and board members in common, the “operated in connection with” relationship test may apply. This relationship test requires that the supporting organization meet two sub-tests (responsiveness and integral part).

In this situation, all of the facts and circumstances must be considered in determining whether the supporting organization can and will be responsive to the demands of the supported organization(s) within the hospital system, and will be an integral part of, or maintain a significant involvement in, their operations. In addition, the supported organization(s) must be specifically named in the governing documents of the supporting organization.

While the organizational structure shows the IRC 509(a)(3) parent entity in the “Upside-Down” relationship to be in control, the supported 509(a)(1) or 509(a)(2) health care organization(s) maintain influence and authority because of the common control and/or named beneficiary requirements of the relationship tests.

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Special Health Care Issues, Continued

509(a)(3) Supporting Another 509(a)(3)

In another unusual circumstance, an IRC 509(a)(3) entity can be formed as a subsidiary of another 509(a)(3) organization. This structure looks like one supporting organization supporting a second supporting organization. On its face, this arrangement does not appear to meet the requirement of an IRC 509(a)(3) entity supporting one or more 509(a)(1) or 509(a)(2) organizations. This situation is occasionally seen in the hospital system setting.

An organization seeking 509(a)(3) status through its relationship with another 509(a)(3) entity will have to support one or more IRC 509(a)(1) or 509(a)(2) organizations, but will do so through the other 509(a)(3) entity.

Example

A health care system is headed by a 509(a)(3) supporting organization (“Parent”) as described above in the “upside-down” relationship. Parent forms a 509(a)(3) subsidiary entity (“Supporting sub”). Parent is the parent and sole member of Supporting sub, the hospital, and other publically supported entities within the health care system that have been recognized as described in IRC 501(c)(3).

Supporting sub will support and benefit the hospital and other publicly supported entities within Parent’s health care system that have been recognized as described in IRC 501(c)(3). Supporting sub’s bylaws:

- Specify that Parent is authorized to elect the governing board of Supporting sub;
- Provide that no less than a majority of the members serving on its governing board must be individuals who also serve on hospital’s governing board; and,
- Provide that Supporting sub and Parent have identical boards.

Supporting sub will hold title to a building which houses an ambulatory care clinic operated by the health system’s 501(c)(3) hospital (“hospital”). Supporting sub, on behalf of Parent, will also provide janitorial and maintenance services for the clinic building.

The articles of organization of both Parent and Supporting sub identify the supported organization(s) by class. Supporting sub’s governing document does not state that it was formed to support or benefit Parent or otherwise specify Parent as an organization it will support or benefit, since Parent is not an IRC 509(a)(1) or 509(a)(2) organization. Neither Supporting sub nor Parent is controlled, directly or indirectly, by disqualified persons.

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Special Health Care Issues, Continued

Threshold Requirement: Integral Part Doctrine

Supporting sub qualifies as organized and operated exclusively for charitable purposes and is eligible for exemption from federal income tax under IRC 501(c)(3) based on performing an essential activity (holding title to and providing repair and maintenance for the clinic building) on behalf of a supported organization (hospital).

Test 1: Relationship Test

A majority of the members of Supporting sub’s governing board also serve on the governing board of hospital. Thus, Supporting sub meets the requirements of the “operated, supervised, or controlled in connection with” relationship.

To meet the requirements of the “operated in connection with” relationship, a 509(a)(3) must meet the “responsiveness test” and the “integral part test.” It must also specify by name, rather than by class or purpose, the publicly supported organization(s) it will support.

Supporting sub’s articles of organization identify the publicly supported organizations it will benefit by class rather than by name. Thus, regardless of whether Supporting sub meets the responsiveness and integral part tests, it does not meet the requirements of the “operated in connection with” relationship.

Test 2: Organizational Test

Since supporting sub is “supervised or controlled in connection with” a hospital, Supporting sub’s Articles may specify the supported organization by class. Therefore, the organizational test is satisfied.

Test 3: Operational Test

Supporting sub meets the operational test because Parent is a permissible beneficiary since it is an organization described in IRC 501(c)(3), and is other than a private foundation.

Test 4: Disqualified Person Control Test

Supporting sub is not controlled, directly or indirectly, by disqualified persons.

Continued on next page

Special Health Care Issues, Continued

**Recap:
509(a)(3)
Supporting
Another
509(a)(3)**

An organization seeking 509(a)(3) status must satisfy the requirements of the relationship test, the organizational, and operational tests. Further, it cannot be controlled, directly or indirectly, by disqualified persons. In addition to these requirements, an organization seeking 509(a)(3) status through another 509(a)(3) must satisfy the following requirements:

- It cannot name the 509(a)(3) it supports in its Articles. Instead, it must specify the publicly supported organization(s) it was formed to benefit. The publicly supported organization(s) must be specified by name or, under certain circumstances, by class or purpose.
 - It must establish that it meets the relationship test based on its relationship with the publicly supported organization(s) it will benefit rather than the other 509(a)(3) organization.
 - The 509(a)(3) it will support must be a “permissible beneficiary” as described at Treas. Reg. 1.509(a)-4(e)(1).
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Unusual Situations

Supported Organizations Described in IRC 501(c)(4), (5), or (6)

Q8

Under Treas. Reg. 1.509(a)-4(k), an organization may qualify as a supporting organization if it meets the relationship test by being “operated, supervised or controlled by,” “supervised or controlled in connection with,” or “operated in connection with” an IRC 501(c)(4), (5) or (6) organization, provided it otherwise meets the requirements of IRC 509(a)(3). This situation may arise when a business league or social welfare organization organizes and operates a fund for charitable activities described in IRC 501(c)(3). The IRC 501(c)(4), (5) or (6) organization must meet the public support requirements of IRC 509(a)(2) as if it were an IRC 501(c)(3) organization.

Example

An organization was formed for educational and charitable purposes and is controlled by a civic league exempt under IRC 501(c)(4). The organization grants scholarships to students graduating from local high schools to attend college. The civic league elects five of the organization’s seven trustees and the remaining two trustees are the president and treasurer of the league. None of the trustees are disqualified persons with respect to the organization, except in their capacity as trustees.

The civic league meets the public support requirements for classification as an organization described in IRC 509(a)(2). In this situation, the scholarship organization qualifies for exemption because it is organized and operated exclusively for exempt purposes. It also qualifies as a supporting organization based on its relationship with an IRC 501(c)(4) organization. Rev. Rul. 76-401, 1976-2 C.B. 175.

Non-exempt Charitable Trusts and IRC 509(a)(3)

A trust classified as a non-exempt charitable trust under IRC 4947 may request a determination letter that it meets the requirements of IRC 509(a)(3) even though it neither has obtained nor seeks exemption under IRC 501(c)(3). Rev. Proc. 72-50, 1972-2 C.B. 830, as superseded in minor part by Rev. Proc. 76-34, 1976-2 C.B. 657.

Continued on next page

Unusual Situations, Continued

**Supported
Organization is
a Foreign
Organization**

Under Rev. Rul. 74-229, 1974-1 C.B. 142, a domestic charitable organization, organized and operated in support of a foreign organization described in IRC 501(c)(3), may qualify as an IRC 509(a)(3) supporting organization.

Caution: A domestic organization that derives its IRC 509(a)(3) status through its relationship with a foreign organization may be disqualified from receiving charitable contributions that qualify as tax deductible under IRC 170 depending upon the degree of control exercised by the domestic supporting organization over the charitable contributions it receives. See Rev. Rul. 63-252, 1963-2 C.B. 101, amplified by Rev. Rul 66-79, 1966-1 C.B. 48. Accordingly, determination agents should coordinate this type of case with EO Technical if they have any question about control by the domestic supporting organization over its funds.

Example

“American Friends of the B Museum” is a domestic organization organized and operated to raise funds to support the educational and cultural activities of the B Museum of Antiquities in a foreign country.

The organization and operation of the museum comply with the requirements for tax-exempt status under IRC 501(c)(3). The museum is supported through grants from the Republic of R, the country where it is located; donations from general public; admissions from the thousands of visitors annually to its museum and archeology sites; and from the sale and licensing of replicas of items in its collection.

The B Museum of Antiquities, a foreign organization, has applied for and been granted tax-exempt status under IRC 501(c)(3) as a public charity under section 509(a)(2).

“American Friends of the B Museum” raises money on behalf of the B Museum of Antiquities, but carries on no independent public or charitable activity beyond supporting the museum. Two of its seven board members are also board members of the B Museum. Its Articles of Incorporation state that it is organized and operated to support educational and cultural activities of the B Museum of Antiquities in the Republic of R.

Continued on next page

Unusual Situations, Continued

Example
(continued)

The “American Friends of the B Museum” provides reports of its fundraising activities to the B Museum; at the same time, the B Museum reports to the American Friends on current and planned activities and funding needs. The two common board members facilitate this two-way communication. The American Friends organization develops a three to five year contribution plan to support specific educational and archeological programs during that time period. This assists the supporting organization in soliciting contributions and in overseeing the uses of the funds it raises for the B Museum.

Based on these facts, the “American Friends of the B Museum” would qualify as tax-exempt under IRC 501(c)(3) and as a supporting organization under IRC 509(a)(3).

“SUPPORTING ORGANIZATION” Exemption Application

Guide Sheet for IRC 509(a)(3) Foundation Status Classification

INSTRUCTIONS – This guide sheet is designed to assist in the processing of an IRC 501(c)(3) exemption application or determination request where classification as a supporting organization under IRC 509(a)(3) must be determined. A supporting organization must meet a “relationship test,” an “organizational test,” an “operational test,” and a “control test” under IRC 509(a)(3)(A), (B), and (C). All items should be completed. A “Yes” response generally indicates that a favorable conclusion is warranted, whereas, a “No” response generally indicates that a problem exists. See the accompanying reference guide for assistance in completing this guide sheet. Contact EO Technical for additional help.

	Yes	No
1. Relationship test under IRC 509(a)(3)(B). The organization must meet either a, b or c below or it does not qualify as an organization described in IRC 509(a)(3). If the answer to either a or b is “Yes,” go to item 5.		
a. Is the organization “operated, supervised or controlled” by a 509(a)(1) or (2) organization?		
b. Is the organization “supervised or controlled in connection with” a 509(a)(1) or (2) organization?		
c. Is the organization “operated in connection with” a 509(a)(1) or (2) organization because it meets either item 2 (the responsiveness test) or item 3 (alternative responsiveness test) below, and item 4 (the integral part test) below?		
2. Responsiveness test: The organization must meet either a, b or c below, and item d below.		
a. Do the officers, directors, trustees or members of the 509(a)(1) or (2) supported organization(s) elect or appoint one or more of the officers, directors or trustees of the organization?		
b. Are one or more members of the governing bodies of the 509(a)(1) or (2) supported organization(s) also officers, directors or trustees or hold other important offices of the supporting organization(s)?		
c. Do officers, directors or trustees of the organization maintain a close and continuous working relationship with the officers, directors or trustees of the 509(a)(1) or (2) supported organization(s)?		
d. By reason of the relationship described above, does the 509(a)(1) or (2) supported organization(s) have a significant voice in the supporting organization’s investment policies, the timing of grants, the manner of making grants, and the selection of recipients of grants?		
3. Alternative responsiveness test: If the responsiveness test in item 2 above is not met, the organization must meet each of items a, b and c below.		
a. Is the supporting organization a charitable trust under state law?		
b. Is each specified 509(a)(1) or (2) organization a named beneficiary under the charitable trust’s governing instrument?		
c. Do the specified 509(a)(1) or (2) supported organizations have the power to enforce the trust and compel an accounting under state law?		
4. Integral part test: The organization must meet either a or b below.		
a. Does the organization engage in activities for or on behalf of the 509(a)(1) or (2) organization(s) which perform the functions of or carry out the purposes of the supported organization and which the supported organization would otherwise normally undertake?		
b. (1) Does the organization make payments of substantially all (at least 85%) of its income to or for the use of the 509(a)(1) or (2) organization(s)? If “Yes,” either (2) or (3) need to be met. (2) Are the payments sufficiently significant to assure the attentiveness of the recipient organization(s) because the payments equal at least 10% or more of the 509(a)(1) or (a)(2) organization(s) total annual support? OR		

