

Qualification; individual practice association. An individual practice association that provides health services through written agreements with health maintenance organizations does not qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Code or as a business league under section 501(c)(6).

ISSUE

Does the individual practice association described below qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Internal Revenue Code or as a business league under section 501(c)(6)?

FACTS

M, a nonprofit membership corporation, is an individual practice association (IPA) described in section 1302(5) of the Health Maintenance Organization Act of 1973, 42 U.S.C.A. section 300e-1(5) (1982). M's stated purpose is to arrange for the delivery of health services through written agreements negotiated with health maintenance organizations (HMOs).

M's membership is limited to licensed physicians who are engaged in the active practice of medicine and who are members of a specified county medical society. The activities of M are managed by an executive committee which is elected by the membership of M. The bylaws of M require that a majority of the executive committee be members of M.

M's members generally maintain a private medical practice in addition to performing services for M. All members are required to enter into written service contracts with M which provide:

(1) that the members shall provide their professional services to HMO patients in accordance with a compensation arrangement negotiated between M and the HMOs.

(2) that the members shall, to the extent feasible, share medical and other records, equipment, and professional, technical, and administrative staff, and

(3) that the members will limit referrals of HMO patients, to the extent feasible, to other participating members.

M's primary activities are to serve as a bargaining agent for its members in dealing with HMO's, and to perform the administrative claims services required by the agreements negotiated with the HMOs. M is paid a capitation amount by each HMO based on the number of HMO subscribers entitled to receive medical services. Members bill M for services rendered to the HMO subscribers and accept claims payment for M as payment for

services rendered. Members agree to reimbursement by M on a fee-for-service basis according to a fee schedule established by the board of directors of M. The fee schedule reflects the usual customary fees charged by the member-physicians in their private medical practice.

M initially pays its members eight-five percent of the amount stated in the fee schedule. The remaining fifteen percent is credited to the account of each member on M's books. At the end of each year, the difference between what M has received from the HMOs and what it has paid out to members and for administrative costs is paid to the members in proportion to the amounts credited in their accounts. If the amounts received by M from the HMOs, less administrative costs, are not sufficient to pay the total amounts billed by its members, the members have no further recourse. Members may look to patients for payment only for services not covered by the contracts between M and the HMOs. M has made no provisions for waiving the medical fees charged to patients who are unable to pay for services not covered by the contracts between M and the HMOs.

M's income is derived from its contracts with HMOs and its expenditures are for administrative costs and payments to its members.

LAW AND ANALYSIS

Section 501(c)(4) of the Code provides for the exemption from federal income tax of civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1(a)(2)(i) of the Income Tax Regulations provides that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the community. An organization embraced within this section is one that is operated primarily for the purpose of bringing about civic betterments and social improvements.

Section 501(c)(6) of the Code provides for the exemption of business leagues, not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(6)-1 of the Regulations provides that a business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons.

The main functions of M are to provide an available pool of physicians who will abide by its fee schedule when rendering medical services to the subscribers of an HMO, and to provide its members with access to a large group of patients, the HMO subscribers, who generally may not be referred to nonmember-physicians. M negotiates contracts on behalf of its members with various HMOs, administers the claims received from its members, and pays them according to its reimbursement agreement. These facts indicate that M is akin to a billing and collection service, and a collective bargaining representative negotiating on behalf of its member-physicians with HMOs. In addition, M does not provide to HMO patients access to medical care which would not have been available but for the establishment of M, nor does it provide such care at fees below what is customarily and reasonable charged by members in their private practices.

Thus, M operates in a manner similar to organizations carried on for profit, and its primary beneficiaries are its member-physicians rather than the community as a whole. See Rev. Rul. 75-199, 1975-1 C.B. 160, and the authorities cited therein, and Rev. Rul. 81-58, 1981-1 C.B. 331, which provides examples of mutual, self-interest organizations that do not qualify for exemption under section 501(c)(4) of the Code. Accordingly, M is not operated exclusively for the promotion of social welfare within the meaning of section 501(c)(4).

In addition, because the billing and collection services provide an economy or convenience to M's members relating to the operation of their private medical practices, M is primarily performing particular services for its members. See Rev. Rul. 71-175, 1971-1 C.B. 153. Thus, the organization is rendering particular services for individual persons as distinguished from the improvement of business conditions in the medical profession and public health area generally. Membership in the organization is restricted to physicians who are subject to M's written service contract. Thus, M does not better conditions for all physicians in a particular community, but, instead, is devoted to maximizing fees for its members. See *National Muffler Dealers Association, Inc. v. U.S.*, 440 U.S. 472 (1979). Therefore, M is not operated as a business league within the meaning of section 1.501(c)(6)-1 of the regulations.

HOLDING

The individual practice association described above does not qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Code or as a business league under section 501(c)(6).