



Department of the Treasury
Internal Revenue Service
Tax Exempt and Government Entities
PO Box 2508
Cincinnati, OH 45201

Date:
05/08/2023
Employer ID number:

Tax years:
All
Person to contact:

Release Number: 202331004
Release Date: 8/4/2023
UIL Code: 501.00-00,
501.04-00, 501.04-02,
503.00-00

Dear :

This letter is our final determination that you don't qualify for exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a) as an organization described in IRC Section 501(c)(4). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

You must file the federal income tax forms for the tax years shown above within **30 days** from the date of this letter unless you request an extension of time to file. For further instructions, forms, and information, visit www.irs.gov.

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection after deleting certain identifying information, as required by IRC Section 6110. Read the enclosed Letter 437, Notice of Intention to Disclose - Rulings, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Letter 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

If you have questions about this letter, you can call the contact person shown above. If you have questions about your federal income tax status and responsibilities, call our customer service number at 800-829-1040 (TTY 800-829-4933 for deaf or hard of hearing) or customer service for businesses at 800-829-4933.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements

Enclosures:
Letter 437
Redacted Letter 4034
Redacted Letter 4038

cc:



Department of the Treasury
 Internal Revenue Service
 PO Box 2508
 Cincinnati, OH 45201

Date: February 21, 2023

Employer ID number:

Person to contact:

Name:

ID number:

Telephone:

Fax:

Legend:

B = company

C = state

D = date

E = individual

G = county

H = company 2

J = date 2

K = company 3

L = company 4

UIL:

501.00-00

501.04-00

501.04-02

513.00-00

Dear _____ :

We considered your application for recognition of exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a). We determined that you don't qualify for exemption under IRC Section 501(c)(4). This letter explains the reasons for our conclusion. Please keep it for your records.

Issues

Do you qualify for exemption under IRC Section 501(c)(4)? No, for the reasons stated below.

Facts

Organizational Documents:

Articles of Incorporation:

You were formed under the nonprofit public benefit corporation law of the state of C on D.

Article V of your Articles of Incorporation ("Articles") states that your purposes are: (i) offering pharmacy and medical health benefit coverage and related health benefits to the general public, governmental entities,

and employer groups through multiple accessible channels, and to carry on other social welfare activities associated with this purpose; (ii) addressing the pharmacy, medical and related health benefit needs of the uninsured and underinsured; (iii) providing pharmacy, medical and related health benefits in underserved communities and to small employers with limited access to pharmacy and related health benefits; and (iv) promoting the general health of the community and engaging in any activities that are reasonably related to or in furtherance of the foregoing social and welfare and community purpose.

Article IX of your Articles provides that upon dissolution, your assets remaining after payment of debts and liabilities will be distributed to a nonprofit fund, foundation or corporation which is organized and operated exclusively for tax-exempt purposes as set forth in Code Sections 501(c)(3) or 501(c)(4).

Bylaws:

Your Bylaws that you submitted for review state that they were adopted on J.

Article 3.2 of your Bylaws states your specific purpose is the same as stated in Article V of your Articles of Incorporation above.

Article 4.1 of your Bylaws states that the initial number of directors constituting the Board shall be people. Upon reaching various revenue milestones, the number of directors will increase as follows:

ANNUAL REVENUE MILESTONE*	NUMBER OF DIRECTORS	E FAMILY APPOINTEES	EMPLOYEE DIRECTORS	NUMBER OF NOMINATING COMMITTEE MEMBERS

* Revenue = "net revenue" calculated per GAAP

Article 4.3 provides that the Nominating Committee shall appoint a simple majority of directors to the Board, who shall be leaders within a community served by the Corporation with experience in health or charitable services, representatives of non-profit organizations that qualify as public charities described in Section 509(a)(2) or (3) of the Code or representatives [sic] governmental units described in Section 170(c)(1) of the Code.

Article 4.3 further provides that the remaining director positions ("E Family Directors") shall be appointed by E, and following his death or incapacity, by a majority vote of his spouse and his direct adult descendants (E, his

spouse, and his direct adult descendants are collectively referred to as the "E Family"). In the event of a tie, the most senior E Family member's vote shall prevail. The E Family representation shall be capped at four (4) as the Board expansion milestones are met. Upon the passing of E and his wife, the E Family representatives shall be apportioned equally between their children and the choice of the representative will belong to the line. For clarity, the E Family appointees can be non-family members, employees of B, a strategic partner or consultant, or any other person deemed appropriate by the E Family. If there is no direct descendant of the E Family, these positions will be equally apportioned to the Nominating Committee and B's Employees with any odd number being apportioned to B's Employees. The E Family shall adopt processes for selection of E Family appointees consistent with the guidelines above.

The President and CEO shall each be eligible to serve as a director. At specified revenue milestones, one additional board member position shall be filled with an employee of the corporation elected by a majority vote of the employees.

E Family Directors may serve an unlimited number of terms, while directors appointed by the nominating committee or elected by the employees may serve a maximum of terms.

Article 4.4 provides that not more than percent (%) of the persons serving on the Board of Directors at any time may be "interested persons." An "interested person" is (a) any person currently being compensated by the Corporation for services rendered to it within the previous () months, whether as a full- or part-time employee, independent contractor or otherwise; or (b) any brother, sister, ancestor, descendant, spouse, brother-in-law, sister-in-law, daughter-in-law, mother-in-law, or father-in-law of any such person.

Article 4.6 provides that the E Family, by simple majority vote may remove and replace any director at large at any time, with or without cause.

Article 4.8 provides that members of the Board shall serve without compensation but shall be reimbursed for travel and lodging expenses in accordance with policies established by the Board.

Article 6.6 provides that the Chief Executive Officer may be removed without cause by a majority vote of the Directors or for cause by a simple majority vote. Article 6.7 provides similarly if the President is not the CEO.

Article 7.2.2. provides that the Nominating Committee shall be comprised of one (1) representative from each of () public charities ("Sponsoring Organization") and the Chief Executive Officer of the Corporation shall be a non-voting member of the Nominating Committee. Each Sponsoring Organization shall remain eligible to appoint a representative to the Nominating Committee so long as it remains exempt under Section 501(c)(3) of the Code and meets the requirements of a public charity under Section 170(b)(1)(A)(iii), (iv), (v) or (vi) of the Code. The Chief Executive Officer (or the President if there is none) shall chair the Nominating Committee. A Sponsoring Organization may be removed upon a majority vote of the Board, provided that at all times there shall be no less () Sponsoring Organizations. Additional or replacement Sponsoring Organizations meeting the requirements of this Section 7.2(c) may be designated from time to time by a () majority vote of the Board. The Nominating Committee shall appoint a simple majority of the members of the Board. The number of voting members on the Nominating Committee shall be governed by

these Bylaws and shall not be subject to change, except by amendment to these Bylaws as prescribed in Article 12.

Officers:

E serves as President, CEO, and a director. E's spouse also serves as a director. There is also an individual serving as Treasurer and Secretary as well as three (3) additional directors. You state that one of your directors is the CEO of a client organization which is exempt under IRC Section 501(c)(3). You state that you will follow a conflict-of-interest policy.

Conversion from For-Profit:

You state you will acquire certain assets and business of B, a state of C Benefit Corporation. B has been in operation as a for-profit enterprise for over 17 years. Such acquisition will occur on or about days after the issuance of a favorable determination letter that you meet the requirements under IRC Section 501(c)(4). The terms of the acquisition will be based upon a determination of the fair market value of the assets and business by an independent appraiser and upon approval of the independent members of your Board of Directors.

Under the Term Sheet between B and you, B will transition all of its operations to you. Therefore, B's sole function will be to provide transition and support services to you. B will cease providing services to the public as this function will transition to you.

You will acquire certain aspects of the assets and business of B. This will be embodied in a series of agreements involving licensing of intellectual property, leasing of certain equipment and one or more agreements transitioning such aspects of the business of B. You state that the terms of such agreements will be set at fair market value, in the manner described above and under terms approved by the independent members of the Board of Directors. These agreements include:

- Leasing of furniture, moveable fixtures, computers and software at fair rental value with an option to purchase some or all of such leased property at the initial 3-year lease period, renewable for -year periods at adjusted fair rental value.
- Licensing of all B's intellectual property under an exclusive license for a period of years, with perpetual rights of renewal. The license fee will be established for the initial license period by an independent appraiser and adjusted at the time of each renewal terms based on an updated independent appraisal. The intellectual property includes a number of patents and software developed by B as well as a number of proprietary products that it provides.
- Sublease of physical office space to B to be used by B's employees.
- Assumption of B's client contracts, network contracts, and client service contracts after an independent review to confirm that they are at arm's length and provide for reasonable compensation.
- Assumption of B's contracts with third-party manufacturers.

You included a schedule of projected financial expenses marked as a response to Part VI, Line 19. It is unclear if this relates to line 19 of Part V of your application where you entered "see attached itemized financial data."

Your projected expenses indicate significant continued financial arrangements with your intended predecessor organization including:

Expense			
Payroll Related services Personnel use for Foundation activities allocated from related party			
Consultant services allocated from related party			
Travel and Meal (inclusive of allocated portion from related party)			
Professional Services (inclusive of allocated portion from related party)			
Information Technology Services allocated portion from related party			
Other Expenses (inclusive of allocated portion from related party)			
Administrative Service Fee charged from related party			
Totals:			

Operations:

You claim that you will benefit the community and promote social welfare by reason of (i) enrollment that is open to individuals and small employer groups, (ii) serving low income, high risk, medically underserved and elderly persons, and (iii) providing prescription medications at demonstrably lower costs than the typical PBM.

Overview of sector:

You claim you will provide an alternative solution in the pharmacy benefit space occupied by traditional pharmacy benefit managers (PBMs).

Pharmacy Benefit Managers are third party companies that function as intermediaries between insurance providers and pharmaceutical manufacturers. PBMs create formularies, negotiate rebates (discounts paid by a drug manufacturer to a PBM) with manufacturers, process claims, create pharmacy networks, review drug utilization, and occasionally manage mail-order specialty pharmacies. PBMs work in conjunction with drug manufacturers, wholesalers, pharmacies, and health insurance providers but play no direct role in the physical distribution of prescription drugs, only handling negotiations and payments within the supply chain. When a new drug is available, the manufacturer negotiates with wholesalers who then sell and distribute drugs to pharmacies. PBMs negotiate agreements with drug manufacturers on behalf of insurers and are paid rebates by drug manufacturers. Pharmacy Services Administrative Organizations (PSAOs) negotiate reimbursements with PBMs on behalf of pharmacies. PBMs then pay pharmacies on behalf of health insurance providers for drugs dispensed to patients. PSAOs and PBMs are both third party companies with different functions and purposes.

PSAOs represent and offer services to independent pharmacies and PBMs represent health insurers. (Source: NAIC.com – National Association of Insurance Commissioners).

You appear to provide both PBM and PSAO services, as well as other similar services.

You state:

Pharmacy benefits and health management of patient use of prescription medications is a critical aspect of health care delivery that has not been adequately addressed by other non-profit healthcare organizations. The U.S. Dept. of Health & Human Services (HHS) estimates that prescription drug spending in the U.S. was approximately \$457 billion in 2015, or 16.7 percent of overall personal health care services. Furthermore, HHS indicates that prescription expenditures are rising and are projected to rise faster than overall health care spending. The traditional PBM industry core business model is focused on driving utilization of prescription drugs, whereas [your] unique pharmacy services administration (“PSA”) model emphasizes appropriate prescription drug use (for example, inappropriate prescription drug use is curtailed, thereby improving the health of the patient and reducing prescription drug costs).

You state that you will use a proprietary Acquisition Cost Index (patent pending) and your network of approximately _____ pharmacies nationwide to set the cost of prescriptions that eliminates hidden spreads and can pass along rebates to the individual and group subscribers in a manner that is unlike traditional PBMs.

You state that you believe healthcare is a social good and will provide discounted pharmaceutical products and services to the community served. These discounts will be made accessible by your unique Medical Benefit Manager (“MBM”) class-of-trade, which will act as a certification of integrity and transparency of cost of care and encourage pharmaceutical manufacturers to work with you in ways that may not be available to traditional MBMs (e.g., providing discounts on drugs, devices, tests, and other products under the medical benefit). This broad access to discounts from industry will allow you to craft integrated healthcare solutions with clients that differentiates clients’ plans from traditional health plans. These MBM products and services will encompass pharmacy services (prescription dispensing), claims adjudication, listing of drugs available and at what cost. You will strive to provide functionality that allows the community (including enrollees and Plan Sponsors) to administer their prescription drug benefits in an improved fashion (primarily resulting from processes pioneered by you that deliver greater integrity, transparency, and compliance with applicable federal safe harbor regulations).

You further state that unlike the current traditional Pharmacy Benefit Manager (PBM), your MBM solution will allow pharmacy benefits to be delivered with true transparency related to acquisition cost of prescription drugs, transfer of pharmaceutical manufacturer discounts directly to the enrollee or Plan Sponsor without diversion (i.e., re-classification by PBM to divert part of the savings to additional compensation to the PBM), eliminate potential conflicts-of-interest that arise from PBM’s ownership of their own pharmacies (you have no ownership in any pharmacy), and providing the tools to administer benefits to lower inappropriate prescription drug use (unlike the traditional PBM that focuses on driving up prescription drug utilization).

You state you will be operated exclusively for the promotion of social welfare of the community. You state you will focus your efforts on “reaching the uninsured and underinsured” by offering affordable access to pharmacy benefits through: retail pharmacy networks offering your services to uninsured (or under-insured) individuals, state and local government-sponsored programs for the uninsured, non-profit hospitals that are designated as

“disproportionate share hospitals” (those serving a significantly disproportionate number of low-income patients), and other similar programs benefiting the community as a whole. You further state you will also provide unique administrative tools that will allow eligible patients to access special government and non-governmental drug pricing programs such as 340B, Group Purchasing Organization (GPO) and Federal Supply Schedule (FSS) at lower costs. You state that this is in keeping with the need to develop innovative ways of making prescription drugs affordable.

You state you will offer pharmacy and other health benefit coverage through an “arranger model,” arranging for provision of pharmacy health services to enrollees through your proprietary national network of approximately pharmacies. You defined your “proprietary network” of pharmacies to be those with whom you have contracted and who offer a negotiated discount to enrollees in your network, with the claims being administered at these negotiated rates by you.

You further state that as your programs expand, you intend to utilize other for-profit or non-profit organizations to interface with program sponsors (employers, government agencies, etc.) in their respective geographic areas which will serve as the marketing arm for your PSA services. These licensing agreements will be reviewed by an independent advisor to confirm the compensation is reasonable in the market.

You state your control will be by the community. A majority of the Board of Directors will be selected by a Nominating Committee appointed by public charities and your Bylaws provide more detail as described above.

You state, through programs such as your current project with the G county’s Dept. of Health Services, you will provide pharmacy benefits to indigent members of the community. You claim you will also pursue expansion of programs offering individual benefits through your network of pharmacies, similar to your initial program with H (described below), through which uninsured and underinsured individuals can access affordable pharmacy benefits. You state you will not decline coverage to any individual of the public based on health condition, nor will you discriminate on the basis of race, ethnicity, country of origin, gender, or gender identity or expression.

You claim while you will offer your services to small and large employers, particularly tax-exempt organizations and governmental employers, that percent or more of your services will be providing a community benefit based on IRS guidance. You state based on your projected enrollees, the percentage of your PSA services provided to individuals and groups of individuals is as follows:

Category of Enrollee	Percentage of your PSA Services
Individuals who receive your PSA benefits directly through a retail pharmacy program:	%
Individuals who receive your PSA benefits through governmental and charitable organizations programs:	%
Individuals who are employees of governmental and charitable organizations and their dependents and receive your pharmacy benefits through their employer’s group health plan:	%
Individuals who receive your PSA benefits through Medicare:	%
Individuals who receive your PSA benefits through Medicaid:	%
Individuals who are enrollees of small employer groups of 50 or fewer participants and receive your benefits through their employer’s group health plan:	%

You project that your enrollment in each of these categories will increase approximately percent a year, with a higher increase in critical access and sole community health systems, although, overall it appears that you project that the relative percentage of individuals receiving PSA benefits through each category will remain proportionately about the same.

You state that your social welfare purpose is demonstrated by the fact that you will operate in many service areas that include medically underserved, low income, rural and high-risk persons. You state that approximately percent of the individuals receiving your PSA services are in "at-risk" categories (i.e. indigent (%), indigent Medicare enrollees (%) or Medicaid enrollees (%)). You support these conclusions by using data on the areas served and information on the percentage of individuals in these types of categories from data provided through the Service Center.

You claim that the above-referenced activities are fully aligned with your purpose, which is to promote social welfare through offering affordable pharmacy health benefit coverage to individuals in the general public and to individuals who are part of employer groups through multiple, easily accessible channels. You state that all members of the public may access health coverage from you through available programs. In addition to providing a community benefit by going directly to the public, you argue that a community benefit is provided by your provision of health plan coverage to the employees and dependents of a significant number of small employers, governmental entities, and public charities.

You state your commitment to ensuring that services are available to the entire community is evidenced by your marketing/community relations budget and marketing materials. You state that you will be focused heavily on expanding your pharmacy health care offerings in the individual market and to programs geared to indigents and/or underinsured individuals. Substantially all of your marketing budget and marketing personnel will be devoted to promoting your services to programs that benefit the community as a whole. You attached sample marketing materials including a promotion for H pharmacy benefits (discussed below) and materials with titles such as " ?" with the heading paragraph:

Your materials mention various products and services available to your clients, including some described in your application materials as among your intellectual property and proprietary products that will be leased from your for-profit predecessor to you:

-
-
-
-

-
-
-
-

Another flyer suggests clients can “ ”. The materials also provide examples of “clients” such as hospital systems that benefitted from employing B including substantial cost savings and improved customer service.

You provided a copy of a broker contract which describes brokerage services to be provided to you to find suitable clients for your pharmacy benefit administration systems and claims processing services.

You also provided examples of newsletters provided to your intended predecessor’s clients with industry and medication information as well as educational materials in slideshow format with medication topics marked.

You state you expect your marketing activities to result in significant growth in the categories of individuals, charitable and county and local government programs, Critical Access and Sole Community Health Systems, Federally Qualified Health Clinics, , cities and school districts, and small employer group plans in the coming years.

In order to make your coverage more affordable for members of the public, you will strive to keep the cost for pharmacy benefits low compared to for-profit alternatives. You do this by keeping both profit and administrative expenses low and through effective use of automation and technology. You will operate in a “virtual” manner whereby, instead of employees coming in to work, the work is allocated to employees. This will relieve you of any geographic restriction on recruiting the best people (resulting in high service levels), while providing for competitive advantage through low infrastructure costs. You will also develop much of the proprietary technology and systems itself which eliminates dependence on others at extra cost (e.g., claims, network, rebates, pedigree programs (340B, GPO, FSS), analytics, etc.).

You claim that additionally, you will provide benefits to the community beyond health care benefits through funding programs for the promotion of health and other charitable purposes. You state you have designated approximately percent of your budget for such purposes. You have not specified which programs are covered by this budget.

Program with H:

You state that you offer access to your services to individuals through programs such as your program with H. You state that your contractual arrangement with H allows individuals who are uninsured or underinsured, through the contracts you have negotiated with pharmaceutical manufacturers, to obtain their prescriptions at costs comparable to and in many instances more favorable than those available to a participant under a group health plan. This results in a reduction from the retail cost of prescription medications of up to %. For example, you have negotiated an % rebate for insulin prescriptions with the pharmaceutical manufacturer. A certain vial of insulin has a wholesale acquisition cost of \$; with your discount, the patient pays \$. You state that this requires a significant financial commitment by H in that it must allow the patient to realize the savings upon purchase and then H must await receipt of the pharmaceutical manufacturers rebate to fully recoup its cost for the prescription. H currently has approximately in-store pharmacies throughout the country.

You further state that through your provider network, approximately _____ of your _____ pharmacies are also enrolled in this unique program with H throughout the country. You state that you supported H in allowing these other pharmacies to participate in the rebate pricing arrangements negotiated by you, resulting in approximately _____ additional pharmacies that are able to provide similar discounts with a membership to H's membership prescription program, greatly expanding the number of uninsured and underinsured individuals who are able to obtain their prescriptions substantially below the retail costs they would otherwise pay. You anticipate that the number of pharmacies participating will greatly increase over time.

You provided a copy of a flyer from H reading as follows:

The H Member Prescription Program is a prescription savings program for you and your family. It allows Members who have no prescription drug insurance or whose insurance does not cover all of their prescription medication to be the beneficiaries of H's commitment to member service, value, quality and product confidence. H is committed to passing on savings to the member and is able to do that by monitoring expenses, taking lower markups and negotiating manufacturer/supplier discounts and passing those savings back to H members.

How It Works

To Join

Enroll at any participating H pharmacy. There is no additional charge for H members to participate in the Program. This program is NOT insurance. The program is a value-added benefit of H membership that provides eligible H members and their eligible dependents the ability to obtain lower prices for certain prescriptions on the Program's Preferred Drug List.

Savings

Savings are estimated up to _____ % off and calculated at the time of sale. View some examples of savings that you and your family can begin taking advantage of immediately. The amount of any price reduction is determined at the time of purchase and may change from time to time. Contact your local H Pharmacist for current Program pricing information.

The flyer you provided shows information and links about your company at the bottom. However, information currently available on H's website only on one page describes the benefits as provided by H and "powered by" your predecessor organization. Otherwise, the information provided by H on its member pharmacy benefits markets the program as provided by H internally.

You provided a copy of a contract between you and H titled "Participating Pharmacy Provider Services" which appears to describe PSA services. The contract describes pharmacy services to be provided by H to eligible members of plan sponsors, for whom you manage pharmacy benefits. To be reimbursed for drugs dispensed, H must submit Claims for payment, whereupon you will pay the Pharmacy on behalf of the Plan Sponsors. Exhibit A describes how you are compensated under the contract such as a flat fee per drug product dispensed by the pharmacy less the amount paid by the customer for drugs on your Acquisition Cost Index (ACI) or a fee of _____ percent plus \$ _____ for drugs not on the ACI list, as well as small charges per claim for claim processing. Also attached is a list of specialty drugs and reimbursement terms.

General internet research also indicates the availability of similar non-insurance pharmacy discount cards available to members of the public at retail pharmacy outlets which are offered by your direct competitors (e.g. K offered by L which also advertises it may be used at pharmacies nationwide) as well as other companies claiming to lower the cost of prescription drugs by methods such as eliminating hidden costs.

Law

IRC Section 501(c)(4) purposes generally

IRC Section 501(c)(4) provides for the exemption from federal income tax of organizations not organized for profit but operated exclusively for the promotion of social welfare. Further, exemption shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

Treasury Regulation Section 1.501(c)(4)-1(a)(1) states a civic league or organization may be exempt as an organization described in IRC Section 501(c)(4) if it is not organized or operated for profit and it is operated exclusively for the promotion of social welfare.

Treas. Reg. Section 1.501(c)(4)-1(a)(2)(i) 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 people 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.

Treas. Reg. Section 1.501(c)(4)-1(a)(2)(ii) provides that promotion of social welfare doesn't include carrying on a business with the general public in a manner similar to organizations which are operated for profit.

Revenue Ruling 54-394, 1954-2 C.B. 131, provides that a nonprofit community television antenna organization whose only activity was to provide television reception for its members was held not to be exempt as a social welfare organization since the benefits were only available to their members who were not the community in general.

Rev. Rul. 68-46, 1968-1 C.B. 260, concluded that a war veterans' association did not qualify for exemption under IRC Section 501(c)(4) because it was primarily engaged in renting a commercial building and operating a public banquet and meeting hall.

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 under IRC Section 501(c)(4). The revenue ruling stated "Because the organization's primary activity is carrying on a business by managing low- and moderate-income housing projects in a manner similar to organizations operated for profit, the organization is not operated primarily for the promotion of social welfare. The fact that these services are being performed for tax-exempt corporations does not change the business nature of the activity."

Rev. Rul. 70-535 denied exemption based on the following facts and circumstances:

- The organization managed low- and moderate-income housing projects for a number of other exempt organizations.
- They received all of their income from management fees and these funds were used for management service expenses.

- This was their primary activity and was no different from the same type of services provided by for-profit corporations.
- The fact this service was provided for other nonprofit organizations did not change the business nature of the activities.

Therefore, exemption for the organization was denied because the conduct of a business was the organization's primary purpose.

Rev. Rul. 76-441, 1976-2 C.B. 147, explained that an otherwise qualifying nonprofit organization that purchases or leases at fair market value the assets of a former for-profit school and employs the former owners, who are not related to the current directors, at salaries commensurate with their responsibilities is operated exclusively for educational and charitable purposes. However, an organization that takes over a school's assets and its liabilities, which exceed the value of the assets and include notes owed to the former owners and current directors of the school, is serving the directors' private interests and is not operated exclusively for educational and charitable purposes.

Commissioner v. Lake Forest, Inc., 305 F.2d 814 (4th Cir. 1962), stated that while a social welfare organization necessarily benefits private individuals in the process of benefiting the community as a whole, even when the benefits are confined to a particular group of individuals, the organization may be exempt if the general community derives a substantial benefit. Conversely, an organization that benefits a large number of people will not necessarily be organized for social welfare purposes within the meaning of IRC Section 501(c)(4) because numbers are not necessarily determinative of social welfare objectives. Social welfare is the well-being of persons as a community and classification depends upon the character - as public or private - of the benefits bestowed, of the beneficiary, and of the benefactor. The court also concluded that Lake Forest did not meet the dictionary definition of "social" or "welfare," stating:

It does not propose to offer a service or program for the direct betterment or improvement of the community as a whole. It is not a charitable corporation in law or equity, for its contribution is neither to the public at large nor of a public character. Lake Forest does, of course, furnish housing to a certain group of citizens but it does not do so on a community basis. It is a public-spirited but privately-devoted endeavor. Its work in part incidentally redounds to society but this is not the "social welfare" of the tax statute.

Contracting Plumbers Cooperative Restoration Corp. v. United States, 488 F.2d 684, 686 (2nd Cir. 1973), *cert. denied*, 419 U.S.827 (1974), states that if an organization has at least one substantial non-exempt purpose, exemption under IRC Section 501(c)(4) will be precluded even though the organization may have other significant exempt purposes.

Harding Hospital, Inc. v. United States, 505 F.2d 1068 (1974), held that a hospital that was a successor to a for-profit corporation was not entitled to tax exemption in part because net earnings inured to private individuals where doctor members of one association treated 90 to 95 percent of patients, that association leased office space, equipment and business office services from hospital at rentals that did not adequately compensate hospital and hospital paid annual salary to the association of doctors for hospital supervision.

In Ruekwald Foundation, Inc. v. Commissioner, T.C. Memo 1974-298, the court held that an organization's purpose and leasing of equipment and real estate that was owned by its founder was prohibited inurement. The organization did not demonstrate it conducted any exempt activities.

In Santa Cruz Building Association v. United States, 411 F. Supp.871 (E.D. Mo.1976), the district court stated, in reference to claims to exemption under IRC Section 501(c)(4), that "[o]rganizations primarily engaged in profit making and non-social welfare activities cannot take an exemption under this section."

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 IRC 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).

Application of law

You have not established that you are operated exclusively for social welfare purposes within the meaning of IRC Section 501(c)(4). Treas. Reg. Section 1.501(c)(4)-1(a)(1) states that an organization may be exempt as an organization described in Section 501(c)(4) if it is not organized or operated for profit and is operated exclusively for the promotion of social welfare. The promotion of social welfare includes being primarily engaged in promoting in some way the common good and general welfare of the people of the community (Treas. Reg. Section 1.501(c)(4)-1(a)(2)(i)). It further states that an organization is not operated primarily for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations which are operated for profit.

Social welfare organizations are not precluded from engaging in business activities as a means of financing their social welfare programs. However, the regulations provide that an organization is not operated exclusively for the promotion of social welfare if its primary activity is carrying on a business with the general public. In Rev. Rul. 68-46 an organization that provides services for a fee was not exempt under IRC Section 501(c)(4) because its primary activity was carrying on a business in a manner similar to organizations operated for profit. In the same manner, your primary activity appears to be carrying on a pharmacy benefit administration business, and not promoting social welfare. This type of pharmaceutical business activity is commonly conducted to produce a profit.

While you state that your primary activity is to provide an "alternative solution" in the pharmacy benefit space occupied by traditional pharmacy benefit managers (PBMs) you still appear to carry on a business with the general public in a similar manner, but with the goal to offer these services at a lower price point and in a socially conscious manner.

You will be a successor of a long running for-profit organization for which it will transfer certain assets and business to you after you obtain a favorable determination under IRC Section 501(c)(4). You will purchase the assets of the existing company from its founder at fair market value. Your application and responses to our inquiries indicate that you will assume responsibility under the existing contracts of the for-profit entity with pharmacies and other businesses and continue to provide generally the same pharmacy benefit management and administrative services to these clients as the existing organization. You will also license various intellectual

property, including various proprietary services which your application states are essential to your business model from the intended predecessor organization at fair market value. Your financial statements project that you will incur significant future expenses payable to your predecessor, most significantly allocated personnel costs, but also over a million in administrative fees per year.

You state that your business model is focused on greater transparency and other methods such as virtual operations to provide pharmaceuticals at a lower cost, and while this may have admirable goals, your submissions do not demonstrate that your operations will be significantly distinguishable from your existing for-profit competitors in a manner that appears to be in furtherance of social welfare within the meaning of IRC Section 501(c)(4). You have not established how providing pharmacy benefit management, administrative, and similar services for lower fees, even if this results in lower prices for individual consumers, is an activity engaged in primarily for social welfare purposes even if affordability of drugs is a problem for society at large. See, for example, Santa Cruz Building Association v. United States.

You will continue to use proprietary methods and products developed by the for-profit predecessor under a license of intellectual property to provide similar products and services as your competitors, but at a lower cost and with more consideration towards your ethical goals. You are still paid on the basis of negotiated fees under the terms of your various contractual arrangements, which you will assume from your predecessor. Your marketing materials indicate that you are directly competing for the same business as your for-profit competitors at a lower price and with better service. Your marketing materials you submitted in support of your application promote your ability to save clients money and time by use of your superior and proprietary products and services. You also submitted a broker contract under which a broker would find and solicit appropriate clients for your services. You do not negotiate to provide the products below cost to a charitable sector or otherwise, but rather provide the same products and services as other pharmacy benefit managers at lower costs, which are then passed on to the end consumer.

You state you will focus your efforts on “reaching the uninsured and underinsured” by offering affordable access to pharmacy benefits through: retail pharmacy networks offering your services to uninsured (or under-insured) individuals, state and local government-sponsored programs for the uninsured, non-profit hospitals that are designated as “disproportionate share hospitals” (those serving a significantly disproportionate number of low-income patients), and other similar programs benefiting the community as a whole.

You do not provide services exclusively for government or exempt organizations, but even if you did, this is not in and of itself a social welfare purpose. See Rev. Rul. 70-535, which 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 under IRC Section 501(c)(4). It stated that because the organization's primary activity is carrying on a business by managing low- and moderate-income housing projects in a manner similar to organizations operated for profit, the organization is not operated primarily for the promotion of social welfare. The fact that these services are being performed for tax-exempt corporations does not change the business nature of the activity.

Your arguments also appear to be similar to the organization in B.S.W. Group, Inc. v. Commissioner, even though that organization was seeking exemption under IRC Section 501(c)(3). That 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. It 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). This is similar to the prohibition on exemption under Section 501(c)(4) for organizations that are carrying on a business with the general public in a manner similar to organizations which are operated for profit (Treas. Reg. Section 1.501(c)(4)-1(a)(2)(ii)).

You emphasize your program through H and other retail pharmacies that enables individuals to access your discounted pharmaceutical prices as a way that you directly provide individuals with access to affordable pharmaceuticals. However, the materials you submitted as well as materials available to the public on the internet indicate that individuals must have an H membership in order to access the pharmaceutical discounts. You have not demonstrated how H membership corresponds to the uninsured or underinsured individuals you state your program is targeted to reach.

Further, H appears to advertise the pharmacy benefit program that you administer to its members as a benefit and encourages its members to transfer their prescriptions to H pharmacies in order to enjoy the discounts as a service that it provides to its members. The contract you provided, which presumably you would assume responsibility for after receiving a favorable ruling, provides for pharmacy benefit administrative services and claims processing services for negotiated fees.

It further appears that H markets pharmacy benefit services similar to you (“powered by” your predecessor organization) to other employers’ clients under the name “H Health Services.” Presumably this is under licensing agreements such as those that you state you intend to pursue with both for-profit and non-profit entities in the future in order to expand the reach of your activities.

You have not demonstrated how any of these activities further a social welfare purpose, or further how this arrangement does not provide a private benefit to H in the form of increased membership and/or clients for its health services line of business. Exemption under IRC Section 501(c)(4) is also precluded to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

You have also not demonstrated how assuming the business arrangements of your intended predecessor organization will further social welfare purposes, or how the continuing license, rental and other arrangements do not provide inurement to the founder who will retain ownership of your for-profit predecessor, even if the licenses and other arrangements are provided at fair market value. The fact that arrangements are at fair market value does not preclude a finding of inurement, rather all facts and circumstances must be taken into account. See, for example, Harding Hospital, Inc. v. United States, Ruekwald Foundation, Inc. v Commissioner, and Rev. Rul. 76-441.

Your founder will be bought out of the business at fair market value, but then continue to have a dedicated client and source of income for the patented and proprietary services and products developed by the for-profit company owned by the founder. You project you will incur over \$ _____ annually in administrative fees to the for-profit as well as nearly another \$ _____ allocated costs to your predecessor. Further, while your founder will not have majority control of the board, he or his family members will have a minority interest for life, while other members of the board are term limited. The E family members can also terminate any director at large with or without cause at any time.

Moreover, it appears that individuals generally receive access to your discounted prices through your business activities as a third-party administrator for health plan sponsors, even if the plan sponsors include government

or charitable employers, small employers, or Medicare and Medicaid. Providing services exclusively to a body of members is not a social welfare activity. See, for example, Rev. Rul. 54-394. Like the organization in Contracting Plumbers Cooperative Restoration Corp. v. United States, you are a middleman who receives your service fees from the for-profit companies, such as H, and the pharmaceutical companies when your members purchase the medications from them.

Like the organization in Commissioner v. Lake Forest, Inc., your benefits are generally confined to a particular group of individuals, even if the group of individuals is large. The benefits of more affordable drug prices may incidentally redound to society, but such “public-spirited but privately-devoted” endeavors are not “social welfare” within the meaning of IRC Section 501(c)(4). It is also unclear what community you purport to serve as you both discuss the individual counties you service for plan sponsors as well as local government and charitable entities, but then also state that your community is nationwide.

You state that through your program such as that sponsored by the G county’s Dept. of Health Services you offer pharmacy benefits to indigent members of the community who are uninsured. It’s unclear if this program is in furtherance of social welfare as you did not state if the indigent individuals still have to pay the retail prices as stated on your proprietary Acquisition Cost List or if the cost is subsidized by the government programs. Even if these programs are in furtherance of social welfare, you only project these programs to comprise about percent of your enrollees and to maintain a similar percentage of your overall enrollees in the future.

You indicated that a further percent of your enrollees receiving your pharmacy administrative services through Medicare and a further percent of your enrollees receive your pharmacy services through Medicaid. You have not specifically demonstrated why providing your services to these individuals is a social welfare purpose other than stating that they are “at risk” populations. Even if such activities are in furtherance of social welfare purposes, these are not your primary activities. You project that a similar percentage of your overall enrollees will continue to fall into these categories in the future.

Your non-exempt activities are more than insubstantial and thus prevent you from exemption under IRC Section 501(c)(4).

Your position

You state you believe healthcare is a social good and will provide discounted pharmaceutical products and services to the community you serve. These discounts will be made accessible by your unique Medical Benefit Manager (“MBM”) class-of-trade, which will act as a certification of integrity and transparency of cost of care and encourage pharmaceutical manufacturers to work with you in ways that may not be available to traditional PBMs (e.g., providing discounts on drugs, devices, tests, and other products under the medical benefit). This broad access to discounts from industry will allow you to craft integrated healthcare solutions with your clients that truly differentiate clients’ plans from traditional health plans. These MBM products and services will encompass pharmacy services (prescription dispensing), claims adjudication, listing of drugs available and at what cost. You claim you will strive to provide functionality that allows the community (including enrollees and Plan Sponsors) to administer their prescription drug benefits in an improved fashion (primarily resulting from processes pioneered by you that deliver greater integrity, transparency, and compliance with applicable federal safe harbor regulation).

You state you will offer pharmacy and other health benefit coverage through an arranger model, similar to an HMO and arranging for provision of pharmacy health services to enrollees through your proprietary national

network of approximately pharmacies. You defined your “proprietary network” of pharmacies to be those with whom you have contracted and who offer a negotiated discount to enrollees in your pharmacy network, with the claims being administered at these negotiated rates by you.

You cite GCM 39829 and now withdrawn examination guidelines from the 1999 Internal Revenue Manual as sources regarding when “health service providers” may be exempt under IRC Section 501(c)(4). You cite the factors of whether enrolment is open to individuals and small groups and whether the health service provider services low income, high risk, medically underserved, or elderly persons.

You further cite ICH Health Plans, Inc. v. Commissioner, T.C. Memo 2001-246, aff’d, 325 F.3d 1188 (10th Cir. 2003), which involved an HMO denied exemption under IRC Section 501(c)(3), with the denial upheld by the courts, as ICH Health Plans was later granted tax exemption under Section 501(c)(4). You state you are like ICH Health Plans in that slightly over half of your enrollees are individuals or families, percent of your enrollees are indigent, you provide services to Medicaid and Medicare enrollees, and you are community controlled.

You also state that you are different from the organization in Vision Service Plan, Inc. v. US, 2006-1 USTC ¶50,173 (E.D. Cal 2005), aff’d, 2008-1 USTC ¶50,160 (9th Cir. 2008), cert. denied, 129 S.Ct. 898 (2009), which was denied exemption under IRC Section 501(c)(4) by both the IRS and the Courts. You state that you are different from Vision Service Plan because it only offered vision services and was not controlled by tax-exempt organizations and its services and benefits were only open to its members.

Our response to your position

You are not an arranger HMO, or other HMO like ICH Health Plans.¹

¹ Further IRS administrative rulings issued to another entity regarding its exempt status are applicable only to that entity and not precedential guidance applicable to other applications for exemption, each of which is decided on the particular facts and circumstances.

“Health maintenance organizations issue contracts under which they agree to provide or arrange for a comprehensive set of medical services for subscribers in exchange for periodic payments that do not vary with the extent or type of services provided. HMOs provide medical care to subscribers through selected physicians, hospitals, and other providers who are affiliated with the HMO in one manner or another. Subscribers are “locked in” to the HMO-affiliated providers, and receive no benefits for nonemergency services obtained from outside providers without prior HMO authorization. It is this limitation, along with an increased emphasis on preventive care, that distinguishes HMOs from traditional health care insurance.” GCM 39829. Stated differently, HMOs are voluntary prepaid health plans which provide individuals (or groups) with a vehicle to prepay medical expenses. The individual (or group) pays a fixed fee with the understanding that when the need for hospitalization or other medical services arises the prepaid health care plan will either cover the costs or provide the needed services. Arranger HMOs directly arrange services for members through contracted arrangements with providers at their own facilities. Further, not all HMOs qualify for exemption under IRC Section 501(c)(4). See, for example, Rev. Rul. 86-98 (holding that a physician-controlled IPA that contracted with HMOs did not qualify under Section 501(c)(4) because it operated primarily to benefit the physicians); see also GCM 38894, EE-75-78 (Sept. 3, 1982) (same result).

You do not operate a prepaid health plan, nor do you provide or arrange for health care, nor do you utilize your own facilities. You provide third party administrative services which facilitate fulfillment of prescription drugs and similar medical items prescribed by unrelated providers using your contracted network of retail pharmacies, which presumably largely consist of for-profit entities. Your proprietary business model facilities offering the prescribed products at lower prices to the end consumer, which may be a laudable goal; however, the products are still being purchased at a negotiated price. You do not arrange for the products to be provided below cost but rather charge less fees than the middleman. For individuals to access your services through a plan sponsor, you arrange payment of that price through the plan sponsor. For individuals who access your services through an H membership or otherwise access your discounts at a retail pharmacy, the individual pays the negotiated price directly.

While you may be structured to provide for majority control of your board by organizations exempt under IRC Section 501(c)(3), like Vision Service Plan you provide a specific service and you have not demonstrated how your primary purpose is other than to provide these services through plan sponsors or contractual arrangements for members of entities like H.

You state that you provide your services through local government and charitable entities to indigent persons and to Medicare and Medicaid enrollees, however, even if these were found to be social welfare activities, these are not your primary services based on your projected enrollments. Further, the enrollees are the indirect beneficiaries of the lower prices that you negotiate on behalf of the plan sponsors for the Medicare and Medicaid enrollees, who compensate you for your administrative services and the costs of the prescribed drugs at the negotiated rates.

Conclusion

Even though you are organized as a nonprofit corporation, you are not and will not be operated exclusively for the promotion of social welfare. Therefore, you do not qualify under IRC Section 501(c)(4).

If you agree

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on

your income tax filing requirements.

If you don't agree

You have a right to protest if you don't agree with our proposed adverse determination. To do so, send us a protest within 30 days of the date of this letter. You must include:

- Your name, address, employer identification number (EIN), and a daytime phone number
- A statement of the facts, law, and arguments supporting your position
- A statement indicating whether you are requesting an Appeals Office conference
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization or your authorized representative
- The following declaration:

For an officer, director, trustee, or other official who is authorized to sign for the organization:

Under penalties of perjury, I declare that I have examined this request, or this modification to the request, including accompanying documents, and to the best of my knowledge and belief, the request or the modification contains all relevant facts relating to the request, and such facts are true, correct, and complete.

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, Power of Attorney and Declaration of Representative, with us if they haven't already done so. You can find more information about representation in Publication 947, Practice Before the IRS and Power of Attorney.

We'll review your protest statement and decide if you gave us a basis to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't given us a basis for reconsideration, we'll send your case to the Appeals Office and notify you. You can find more information in Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court later because the law requires that you use the IRC administrative process first (IRC Section 7428(b)(2)).

Where to send your protest

Send your protest, Form 2848, if applicable, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Mail Stop 6403
PO Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Mail Stop 6403
Cincinnati, OH 45202

You can also fax your protest and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that they received it.

You can get the forms and publications mentioned in this letter by visiting our website at www.irs.gov/forms-pubs or by calling 800-TAX-FORM (800-829-3676). If you have questions, you can contact the person listed at the top of this letter.

Contacting the Taxpayer Advocate Service

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or if you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit www.taxpayeradvocate.irs.gov or call 877-777-4778.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements

cc: