



GOV. EMPLOYERS AND
NON-EMPLOYERS
ENTITIES
SIGN

Yellow
DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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Return to Manager, EO Determinations - Cit

DATE: [REDACTED]

SURNAME: [REDACTED]

ate: JAN 29 2002

[REDACTED]

Contact Person: [REDACTED]

Identification Number: [REDACTED]

Contact Number: [REDACTED]

Employer Identification Number: [REDACTED]

ar Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were formed in [REDACTED] for charitable purposes within the meaning of section 501(c)(3) of the Code. You plan on constructing a health care facility for use as a hospital, clinic, or health care facility to provide extended care, outpatient, or long-term rehabilitation services to patients who have sustained physical, cognitive and/or neuropsychological deficits. You plan on using a multidisciplinary approach to rehabilitation with a team of specialists, licensed in their respective fields and led by physicians skilled in therapeutic techniques, to ensure that that patient's rehabilitation needs are met in the most effective and efficient manner.

The health care facility will be constructed on [REDACTED] acres of land that you have purchased. You have not provided any contracts for the purchase of the [REDACTED] acres of land and you have not listed the property as an asset on your balance sheet. You have not provided any details on how the health care facilities will be financed.

You currently are not operational. You have no medical staff. You do not plan on having an emergency room and thus individuals in need of emergency care will be transferred to a local hospital. You have not provided any details as to whether there is another hospital in your community that is nearby your facility that will operate an emergency room.

You have not provided any details concerning your charity care policy. Furthermore, you do not plan on providing a portion of your services or facilities to be used for charity patients.

You have a 5-member board of directors. Three of the five board members may be [REDACTED], [REDACTED], and [REDACTED]. [REDACTED] is paid an annual salary of \$[REDACTED] and [REDACTED] is paid an annual salary of \$[REDACTED]. You have not provided

by details as to the relationships amongst the directors and information as to whether there are any conflicts of interest among the directors.

You have entered into an agreement with [REDACTED] to utilize medical rehabilitation programs owned by [REDACTED]. The agreement is for \$ [REDACTED], and if you sublicense the program, then you will pay [REDACTED] 50% of any sublicense fee.

You have entered into a ten year arrangement with [REDACTED] ([REDACTED]). [REDACTED] will provide client health care services, management services and turnkey commercial services to you. [REDACTED] is the President of [REDACTED]. The arrangement with [REDACTED] does not provide the fee that you will pay to [REDACTED]. There is a \$ [REDACTED] termination fee that will be paid if the arrangement is broken within the first five years and a \$ [REDACTED] fee if the arrangement is broken between years 5 through 10.

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

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

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in Code section 501(c)(3) in its generally accepted legal sense. The promotion of health has long been recognized as a charitable purpose. See Restatement (second) of Trusts, sections 368, 372 (1959); 4A Scott and Fratcher, The Law of Trusts, sections 368, 372 (4th ed, 1989); and Rev. Rul. 69-545, 1969-2 C.B. 117. It also includes relieving the burdens of government, and relief of the poor and distressed and underprivileged.

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279, 283 (1945), the Court stated that "the presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

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

Rev. Rul. 83-157, 1983-2 C.B. 94, holds that a hospital that otherwise met the requirements of Rev. Rul. 69-545 was not required to operate an emergency room when a state health planning agency had made a determination that additional emergency facilities would be unnecessary and duplicative.

Section 5.02 of Rev. Proc. 90-27, 1990-1 C.B. 514, provides that exempt status will be recognized in advance of operations if proposed operations can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere restatement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt, a record of actual operations may be required before a ruling or determination letter will be issued. In those cases where an organization is unable to describe fully its purposes and activities, a refusal to issue a ruling or determination letter will be considered an initial adverse determination from which administrative appeal or protest rights will be afforded.

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

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

In Harding Hospital, Inc. v. United States, 505 F.2d 1068 (6th Cir. 1974), a nonprofit hospital with an independent board of directors executed a contract with a medical partnership composed of seven physicians. The contract gave the physicians a virtual monopoly over the care of the hospital's patients and the stream of income they represented while also guaranteeing the physicians thousands of dollars in payments for various supervisory activities. The court held that the benefits derived from the contract constituted sufficient private benefit to preclude exemption.

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the court concluded that an organization that trained campaign workers for the benefit of the Republican Party was not exempt under section 501(c)(3) of the Code due to the greater than incidental private benefit to the Party. The court noted that section 501(c)(3) organizations may benefit private interests only incidentally. Conferring more than incidental benefits on private interests is a nonexempt purpose.

To be described in section 501(c)(3) of the Code, an organization must be organized and operated exclusively for exempt purposes. An organization will be regarded as operated exclusively for exempt purposes only if it engages primarily in activities which accomplish those exempt purposes. An organization does not operate exclusively for exempt purposes if more

[REDACTED]

than an insubstantial part of its activities does not further exempt purposes. Section 501(c)(3)-1(c)(1) of the regulations. Also, see Better Business Bureau v. United States, supra.

You plan on constructing health care facilities in order to operate a hospital, clinic or health care facility. You have not provided details as to financing the facility or listed the purchased 75 acres of land on your balance sheet. You have not provided any information as to any contract purchase for land where the health care facilities will operate.

You have not shown that you are operating for charitable purposes by satisfying the immunity benefit standard as described in Rev. Rul. 69-545. You do meet the community benefit standard since you do not plan on maintaining an emergency room or provide emergency services, no portion of your facilities will be used for individuals who are unable to pay, and your board of directors has not been shown to be representative of the community that it serves. Moreover, three of the five directors are related to each other, which indicates that your board is not representative of the community. Furthermore, you have not provided any information that you do not need an emergency room because it would be duplicative as described in Rev. Rul. 83-157.

An organization is not operated exclusively for exempt purposes unless it serves a public rather than a private interest. An organization must establish that it does not operate for the benefit of private interests such as designated individuals, the creator or his family or persons controlled, directly or indirectly, by such private interests. See section 1.501(c)(3)-1(d)(1) of the regulations. For the reasons explained below, you have failed to satisfy the requirements of section 1.501(c)(3)-1(d)(1).

The information in the file supports the conclusion that you are operating for the private benefit of [REDACTED]. Evidence showing that you are operating for the private benefit of [REDACTED] includes the fact that you were created by [REDACTED] you established a salary for [REDACTED] without [REDACTED] entering into a conflicts of interest policy, the majority of your directors are related to each other and to [REDACTED] and you have entered into two contracts with companies controlled by [REDACTED]. Therefore, [REDACTED] has significant control over and derives significant benefit from your operations. See Harding Hospital, Inc. v. United States, supra and American Campaign Academy v. Commissioner. The benefits provided to [REDACTED] therefore violate the prohibition against private inurement contained in section 501(c)(3) of the Code.

Furthermore, you have not explained your activities in sufficient detail to support a favorable determination of exempt status under section 501(c)(3) of the Code. You have stated that you want to operate a health care facility, but have not provided specific details explaining how you will operate as an organization described in section 501(c)(3). Therefore you have failed to establish a basis for exemption under section 501(c)(3). See Section 5 of Rev. Proc. 80-27, supra.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

[REDACTED]

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this ruling. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax-Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

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

Internal Revenue Service
[REDACTED], T.E.G.E.A.T.A.
1111 Constitution Ave, N.W.
Washington, D.C. 20224

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

Sincerely,

(signature) Marvin Friedlander
Marvin Friedlander
Manager, EO Technical
Group 1