

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

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Contact Person:

ID Number:

Telephone Number:

Employer Identification Number:

Legend:

A =
B =
C =

Dear _____ :

This is in response to a letter from your authorized representative requesting a series of rulings on your behalf regarding the tax consequences associated with B providing liability insurance to C, a for profit entity which is a subsidiary of A.

A is exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code and is classified as a nonprivate foundation under section 509(a)(1). A operates a hospital and provides a full range of acute health care services. It participates in a Self Insurance Trust, B, along with several of A's subsidiaries, all of which are section 501(c)(3) entities and which are classified as public charities.

B is exempt under section 501(c)(3) of the Code as is classified as a public charity under section 509(a)(3).

C is a for-profit subsidiary of A that operates a nursing home facility. It desires to participate in the insurance program offered by B. You have stated that B would receive only about 2% of its total gross receipts from the provision of insurance to C. In addition, you have stated that the risks of for-profit entities will not exceed 5% of the total risks insured by the trust.

You have requested the following rulings in connection with the transaction described above:

1. Providing insurance for the risks of C will not jeopardize the exempt section 501(c)(3) status of B.
2. Providing insurance for the risks of C will not jeopardize the section 509(a)(3) public charity status of B.
3. The receipt of insurance premiums by B from C will not be treated as unrelated business taxable income to B under section 512 of the Code.

Section 501(a) of the Code provides an exemption from federal income tax for organizations described in section 501(c)(3), including organizations that are organized and operated exclusively for charitable, educational or scientific purposes.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense.

Section 511(a) of the Code imposes a tax on the unrelated business income of organizations described in section 501(c).

Section 512(a)(1) of the Code defines unrelated business taxable income as the gross income derived by an organization from any unrelated trade or business regularly carried on by it, less the allowable deductions which are directly connected with the carrying on of the trade or business, with certain modifications.

Section 513(a) of the Code defines unrelated trade or business as any trade or business the conduct of which is not substantially related (aside from the need of the organization for funds or the use it makes of the profits derived) to the exercise of the organization's exempt purposes or functions.

Section 1.513-1(d)(2) of the Income Tax Regulations provides, in part, that a trade or business is related to exempt purposes only where the conduct of the business activities has a casual relationship to the achievement of exempt purposes; and it is substantially related for purposes of section 513 of the Code only if the casual relationship is a substantial one. Thus, for the conduct of trade or business from which

a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance

of the services from which the gross income is derived must contribute importantly to the accomplishment of exempt purposes.

Revenue Ruling 69-545, 1969-2 C.B. 117, acknowledges that the promotion of health is a charitable purpose within the meaning of section 501(c)(3) of the Code.

Revenue Ruling 78-41, 1978-1 C.B. 148, provides that a trust created by an exempt hospital for the sole purpose of accumulating and holding funds to be used to satisfy malpractice claims against the hospital, and from which the hospital directs the bank-trustee to make payments to claimants, is operated exclusively for charitable purposes and is exempt from tax under section 501(c)(3) of the Code.

Providing insurance for the risks of C, a for profit entity, does not contribute importantly to the accomplishment of exempt purposes by B under section 1.513-1(d)(2) of the regulations, even though C is a subsidiary of A. Therefore, the income B receives from C for the provision of insurance constitutes unrelated business taxable income within the meaning of section 512 of the Code. However, since the gross receipts received by B from C represent only 2% of B's total gross receipts from the provision of insurance and will not exceed 5% of the total risks insured by B, the amount involved is de minimus and therefore will not jeopardize B's exempt status under section 501(c)(3) nor its classification as a public charity under section 509(a)(3).

Accordingly, based on all the facts and circumstances described above, we rule:

1. Providing insurance for the risks of C will not jeopardize the exempt section 501(c)(3) status of B.
2. Providing insurance for the risks of C will not jeopardize the section 509(a)(3) public charity status of B.
3. The receipt of insurance premiums by B from C will be treated as unrelated business taxable income to B under section 512 of the Code and will be subject to tax under section 511.

These rulings are based on the understanding that there will be no material changes in the facts upon which they are based.

These rulings are directed only to the organization that requested them. Section 6110(k)(3) of the Code provides that they may not be used or cited as precedent.

These rulings do not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described.

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Please keep a copy of these rulings in your permanent records.

Sincerely,

Michael Seto
Manager, Exempt Organizations
Technical Group 1

cc: