



**Department of the Treasury  
Internal Revenue Service  
Tax Exempt and Government Entities**

**Date:** May 9, 2022

**Taxpayer ID number:**

**Form:**

**Tax periods ended:**

Release Number: 202249019  
Release Date: 12/9/2022  
UIL Code: 501.03-00

**Person to contact:**  
**Name:**  
**ID number:**  
**Telephone:**  
**Fax:**

**CERTIFIED MAIL - RETURN RECEIPT REQUESTED**

**Why we are sending you this letter**

This is a 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)(3), effective . Your determination letter dated , is revoked.

Our adverse determination as to your exempt status was made for the following reasons: You have failed to establish that you are operated exclusively for an exempt purpose within the meaning of IRC Section 501(c)(3), and that no part of your earnings inures to the benefit of private individuals or shareholders.

Organizations that are not exempt under IRC Section 501 generally are required to file federal income tax returns and pay tax, where applicable. For further instructions, forms and information please visit [www.irs.gov](http://www.irs.gov).

Contributions to your organization are no longer deductible under IRC Section 170.

**What you must do if you disagree with this determination**

If you want to contest our final determination, you have 90 days from the date this determination letter was mailed to you to file a petition or complaint in one of the three federal courts listed below.

**How to file your action for declaratory judgment**

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of IRC Section 7428 in one of the following three venues: 1) United States Tax Court, 2) the United States Court of Federal Claims or 3) the United States District Court for the District of Columbia.

Please contact the clerk of the appropriate court for rules and the appropriate forms for filing an action for declaratory judgment by referring to the enclosed Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status. You may write to the courts at the following addresses:

United States Tax Court  
400 Second Street, NW  
Washington, DC 20217

U.S. Court of Federal Claims  
717 Madison Place, NW  
Washington, DC 20439

U.S. District Court for the District of Columbia  
333 Constitution Ave., N.W.  
Washington, DC 20001

Processing of income tax returns and assessments of any taxes due will not be delayed if you file a petition for declaratory judgment under IRC Section 7428.

We'll notify the appropriate state officials (as permitted by law) of our determination that you aren't an organization described in IRC Section 501(c)(3).

**Letter 6337 (12-2020)**  
Catalog Number 74808E

**Information about the IRS Taxpayer Advocate Service**

The IRS office whose phone number appears at the top of the notice can best address and access your tax information and help get you answers. However, you may be eligible for free help from the Taxpayer Advocate Service (TAS) if you can't resolve your tax problem with the IRS, or you believe an IRS procedure just isn't working as it should. TAS is an independent organization within the IRS that helps taxpayers and protects taxpayer rights. Contact your local Taxpayer Advocate Office at:

Or call TAS at 877-777-4778. For more information about TAS and your rights under the Taxpayer Bill of Rights, go to [taxpayeradvocate.irs.gov](http://taxpayeradvocate.irs.gov). Do not send your federal court pleading to the TAS address listed above. Use the applicable federal court address provided earlier in the letter. Contacting TAS does not extend the time to file an action for declaratory judgment.

**Where you can find more information**

Enclosed are Publication 1, Your Rights as a Taxpayer, and Publication 594, The IRS Collection Process, for more comprehensive information.

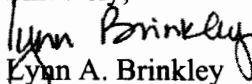
Find tax forms or publications by visiting [www.irs.gov/forms](http://www.irs.gov/forms) or calling 800-TAX-FORM (800-829-3676).

If you have questions, you can call the person shown at the top of this letter.

If you prefer to write, use the address shown at the top of this letter. Include your telephone number, the best time to call, and a copy of this letter.

Keep the original letter for your records.

Sincerely,



Lynn A. Brinkley  
Acting Director, Exempt Organizations Examinations

Publication 892



**Department of the Treasury  
Internal Revenue Service  
Tax Exempt and Government Entities**

**Date:**  
February 2<sup>nd</sup>, 2022  
**Taxpayer ID number:**

**Form:**

**Tax periods ended:**

**Person to contact:**

**Name:**  
**ID number:**  
**Telephone:**  
**Fax:**  
**Address:**

**Manager's contact information:**

**Name:**  
**ID number:**  
**Telephone:**  
**Response due date:**  
March 4<sup>th</sup>, 2022

**CERTIFIED MAIL – Return Receipt Requested**

:

**Why you're receiving this letter**

We enclosed a copy of our audit report, Form 886-A, Explanation of Items, explaining that we propose to revoke your tax-exempt status as an organization described in Internal Revenue Code (IRC) Section 501(c)(3).

**If you agree**

If you haven't already, please sign the enclosed Form 6018, Consent to Proposed Action, and return it to the contact person shown at the top of this letter. We'll issue a final adverse letter determining that you aren't an organization described in IRC Section 501(c)(3) for the periods above.

After we issue the final adverse determination letter, we'll announce that your organization is no longer eligible to receive tax deductible contributions under IRC Section 170.

**If you disagree**

1. Request a meeting or telephone conference with the manager shown at the top of this letter.
2. Send any information you want us to consider.
3. File a protest with the IRS Appeals Office. If you request a meeting with the manager or send additional information as stated in 1 and 2, above, you'll still be able to file a protest with IRS Appeals Office after the meeting or after we consider the information.

The IRS Appeals Office is independent of the Exempt Organizations division and resolves most disputes informally. If you file a protest, the auditing agent may ask you to sign a consent to extend the period of limitations for assessing tax. This is to allow the IRS Appeals Office enough time to consider your case. For your protest to be valid, it must contain certain specific information, including a statement of the facts, applicable law, and arguments in support of your position. For specific information needed for a valid protest, refer to Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status.

Fast Track Mediation (FTM) referred to in Publication 3498, The Examination Process, generally doesn't apply now that we've issued this letter.

4. Request technical advice from the Office of Associate Chief Counsel (Tax Exempt Government Entities) if you feel the issue hasn't been addressed in published precedent or has been treated inconsistently by the IRS.

If you're considering requesting technical advice, contact the person shown at the top of this letter. If you disagree with the technical advice decision, you will be able to appeal to the IRS Appeals Office, as explained above. A decision made in a technical advice memorandum, however, generally is final and binding on Appeals.

**If we don't hear from you**

If you don't respond to this proposal within 30 calendar days from the date of this letter, we'll issue a final adverse determination letter.

**Contacting the Taxpayer Advocate Office is a taxpayer right**

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 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](http://www.taxpayeradvocate.irs.gov) or call 877-777-4778.

**For additional information**

You can get any of the forms and publications mentioned in this letter by visiting our website at [www.irs.gov/forms-pubs](http://www.irs.gov/forms-pubs) or by calling 800-TAX-FORM (800-829-3676).

If you have questions, you can contact the person shown at the top of this letter.

Sincerely,

Sean E. O'Reilly  
Director, Exempt Organizations  
Examinations

Enclosures:  
Form 886-A  
Form 6018

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

**Issue**

Does the \_\_\_\_\_ (the Program) qualify for tax exemption under Internal Revenue Code section 501(c)(3) by serving a public rather than private interest, where no net earnings inure to the benefit of any private shareholder or individual?

**Facts**

The Program was incorporated in the State of \_\_\_\_\_ on \_\_\_\_\_ as a nonprofit public benefit corporation. Article III of the Articles of Incorporation states its specific purpose is “\_\_\_\_\_.” Article V states the Program is “organized and operated exclusively for scientific or educational purposes within the meaning of IRC Section 501(c)(3).” Article VII states “the property of this corporation is irrevocably dedicated to scientific or educational purposes and no part of the net income or assets of this corporation shall ever inure to the benefit of any director, officer or member thereof or to the benefit of any private person.”

The Program submitted Form \_\_\_\_\_, *Application for Recognition Under Section 501(c)(3) of the Internal Revenue Code*, to the Internal Revenue Service (IRS) on \_\_\_\_\_. On Part II Line 1, the Program described its activities as such:

“

”

On Part II Line 2, the Program listed its sources of financial support in order of size as: 1. Contributions and gifts, and 2. \_\_\_\_\_.

On Part II Line 4b, the Program wrote “none” for annual compensation of the organization’s governing body.

On Part II Line 12a, the Program checked “no” for the organization requiring payment from the recipients of provided benefits, services, or products. On Part II Line 12b, the Program checked “no” for the organization limiting its benefits, services, or products to specific individuals or classes of individuals.

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

On Part III Line 9i, the Program selected it is not a private foundation because it qualifies under Section 509(a)(2) as normally receiving not more than one-third of its support from gross investment income and more than one-third of its support from contributions, membership , and gross receipts from activities related to its exempt functions.

Attached to the Form was a proposed budget detailing the following:

Table 1 – Proposed Budget on Form		
Budget		
<b>Income</b>		
Gifts and contributions	\$	
		\$
<b>Disbursements</b>		
Written material, preparation, production and printing		
Distribution and mailing		
Secretarial and office expense		
Legal and accounting		
Net accumulation:		
Second Year Budget		
<b>Income</b>		
Gifts and contributions		
<b>-Disbursements</b>		
Written material, preparation, production and printing		
Distribution and mailing		
Secretarial and office expense		
Legal and accounting		
Educational Activities		
Net accumulation:		

The Program included in its application for exemption a copy of its Bylaws. Article IV, Dedication of Assets, states “no part of the net earnings of the Corporation shall inure to the benefit of, or be distributable to its members, trustees, officers, directors or other private persons, except that the Corporation shall be authorized and empowered to pay reasonable compensation for services rendered and to make payments and distributions in furtherance of the purposes set forth in the purpose clause hereof.”

In response to a request for additional information, the Program provided the following descriptions of its activities in a letter dated :

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

“

The are considered nominal compared to charged by for-profit programs;”

“The procedure for an individual who would like to participate but cannot afford the is as follows. The individual applies to the Program. There is then a telephone screening to determine whether the Program is appropriate for that individual. If it appears appropriate, the individual is asked to come in for an . The evaluation is to determine if the Program is likely to be helpful to the . At that time finances are discussed to evaluate what portion of the cost, if any, the can afford to pay;”

In this same response, the Program provided the following information about compensation:

“The statement of revenue and expenses previously submitted for salary because at the present time there are . Everyone involved is their time. at such time as it can be afforded, only will be hired. No officer or board member will be ;”

“There are salaried employees or other compensated individuals;” and

“

or is an of the organization.”

The Program filed the Form , *Return of Organization Exempt From Income Tax*, for the year ended on . On Part I Line 1, the Program described its mission to “provide services to individuals who have .” On Part I Lines 3 and 4, the Program left how many voting members and how many independent voting members are part of the governing body. On Part I Line 5, the Program listed person employed during the calendar year.

The Program filed the Form for the year ended on . On Part I Line 1, the Program described its mission to “provide services to individuals with .” On Part I Line 3, the Program listed voting members of the governing body, and left Line 4 for the number of independent voting members of the governing body. On Part I Line 5, the Program listed individuals employed during the calendar year, and on Line 6 listed volunteers.

On Part III Line 1 of both Forms (for and ), the Program described its organization as follows:

“

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

.”

On Part IV Line 28a of both Forms , the Program checked “yes” to being party to a business transaction with a current or former officer, director, trustee, or key employee.

On Part VI Line 1a of both Forms , the Program listed voting members of the governing body. On line 2, the Program checked “yes” to any officer, director, trustee, or key employee having a family relationship or a business relationship with any other officer, director, trustee, or key employee. On line 3, the Program checked “yes” to the organization delegating control over management duties customarily performed by or under the direct supervision of officers, directors, or trustees, or key employees, to a management company or other person.

On Part VII Section A of Form for year ended , the Program listed the following officers, directors, and trustees:

Table 2 – List of Officers, Directors, and Trustees on Form for				
Name and Title	Average Hours per Week	Position		Reportable compensation
		Individual trustee or director	Officer	
, Pres		X	X	
Pres		X	X	
, Secy		X	X	

On Part VII Section B for the year ended , the Program listed the following independent contractor:

Table 3 – List of Independent Contractors on Form		
Name and business address	Description of services	Compensation
		\$

On Part VII Section A of Form for year ended , the Program listed the following officers, directors, and trustees:



Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

Table 4 – List of Officers, Directors, and Trustees on Form for				
Name and Title	Average Hours per Week	Position		Reportable compensation
		Individual trustee or director	Officer	
, President Treasurer		X	X	\$
Pres		X	X	
, Secretary		X	X	

On Part VII Section B for the year ended , the Program listed no independent contractors that received more than \$ in reportable compensation from the organization.

In , the assigned agent began an examination of the Program's books and records for the year ended .

The Program's accountant, , provided Balance Sheets as of and which showed the following accounts:

Table 5 – Balance Sheets		
Assets		
Cash –	\$	\$
Other Current Assets – Suspense		-
Accumulated Depreciation – Furniture	-	-
Furniture and Equipment – Other		
<b>Total Assets</b>		
Liabilities and Equity		
Credit Card Pay	-	
<b>Total Liabilities</b>	-	
Unrestricted Net Assets		
Net Income		-
<b>Total Liabilities and Equity</b>		

provided Profit & Loss Statements for through and which showed the following:

Table 6 – Profit and Loss Statements		
Income		
	\$	\$
<b>Total Income</b>		
Expense		
Bank Charges		
Account Fees		

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

Depreciation		
Dues		
Advertising		
Outside Services		
Payroll Expenses		
Rent		
Salaries		-
Tax and Licenses		
<b>Total Expense</b>		
<b>Net Income</b>		-

provided a contract between it and the , Professional Corporation ( )  
for a of \$ /hour, with a minimum of hours/week. The agreement was signed by the Secretary at the  
time, , on for the following services:

- Supervision of all , including independent contractors and trainees
- Overseeing the running of the Program to ensure that the highest quality of care is being provided; this shall include ongoing evaluation with the staff
- Collaboration with any other professionals working with the (e.g. , )
- Management of the bookkeeping, including deposits, expenses and balancing the budget
- Preparation of all tax information
- Organize and direct training for in the community who are interested in learning more about the treatment of population

The assigned agent conducted an interview on with , President and CFO, and , the accountant and Power of Attorney to the organization. and provided the subsequent information.

The organization's primary purpose is to provide for adults and adolescents on treating . runs the whole organization—directs and hires the independent contractors; does the financials, bookkeeping, and tax filings; reviews charts, supervises the contractors, and works with insurance companies as needed. also organizes community outreach programs such as—hosting community classes on for adolescents and adults on treating ; going to schools in the area to present to the students; speaking to students on how to diagnose and treat ; and training and staff on how to treat . , is the organization's Vice President, and , recently join the Board as the Secretary. The Board meets once a year, unless something comes up during the year, then another meeting would be held to discuss. None of the Board members receive compensation or other benefits.

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

The organization only receives income from . The collect the , then collects the cash and checks and deposits them into the organization's bank account. is responsible for preparing the bank deposits, but the are the ones that collect the from the prepares and signs outgoing checks and is the only in the organization authorized to sign the check. prepares annual bank reconciliation reports. For someone to be reimbursed for business expenses, they would submit a receipt to , though the organization does not generally reimburse anyone for expenses does get reimbursed for the telephone bill, and was once reimbursed for the accounting fee when it was paid for with personal card instead of the organization's card.

The organization is billed by the Professional Corporation ( ) for consultations and expertise. is trained in and has years of experience. The contract between the organization and the was signed by the Vice President. The was set for the services provided, based on what they thought the organization could afford to pay.

The organization charges on a based on the . The end is from \$ -\$ a session, up to \$ -\$ a . In most paid around \$ .

The organization does not have a specific policy in place for when a no longer has the ability to pay, but there is a code of ethics that the cannot abandon their . Thus, if a lost their job, the would continue to treat them and make sure they have the resources they need. However, this is based on the individual ; does not dictate how or when the must continue to that .

On , the assigned agent sent an Information Document Request to the Program to request supporting documentation for sampled transactions from the general ledger. provided the following invoices:

Table 7 – Invoice from		for services provided	
Date	Service		Amount Charged
			\$



Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

The assigned agent asked \_\_\_\_\_ and \_\_\_\_\_ on \_\_\_\_\_ about what the difference is between the Program and a for-profit private practice. \_\_\_\_\_ explained that the organization is different from a for-profit because the community service and reduced \_\_\_\_\_. \_\_\_\_\_ was unsure how the organization is structured differently from a for-profit.

On \_\_\_\_\_, the assigned agent sent the Program a memorandum of the notes taken during the prior interviews and requested comments. \_\_\_\_\_ responded via fax on \_\_\_\_\_ with additions to some of the prior responses given:

“

”

### **Law**

Section 501(c)(3) provides in part tax-exemption to corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, or similar purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(a)-1(c) of the Income Tax Regulations (Regulations) defines “private shareholder or individual” as referring to persons having a personal and private interest in the activities of the organization.

Regulations Section 1.501(c)(3)-1(a)(1) states that in order to be exempt as an organization described in Section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational or operational test, it is not exempt.

Regulations Section 1.501(c)(3)-1(c)(1) states that an organization is operated exclusively for charitable purposes if it engages primarily in activities which accomplish one or more of such exempt purposes specified in IRC Section 501(c)(3).

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number ( <i>last 4 digits</i> )	Year/Periods ended

Regulations Section 1.501(c)(3)-1(c)(2) states that an organization is not operated exclusively for charitable purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

Regulations Section 1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized exclusively for any of the purposes specified in Section 501(c)(3) unless it serves public, rather than private interests. Thus, it is necessary for the organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such interests.

Regulations Section 1.501(c)(3)-1(d)(1)(iii) states that private benefit must not be substantial relative to the public benefit, in a facts and circumstances test that requires public benefit from the organization's activities outweigh any individual benefit.

Regulations Section 1.501(c)(3)-1(d)(2) provides that the term "charitable" is used in Section 501(c)(3) in its generally accepted legal sense. The promotion of health has long been recognized as a charitable purpose.

Revenue Ruling (Rev. Rul.) 56-185, 1956-1 C.B. 202 provides in part that an organization is not exempt merely because it operates a hospital devoted to the treatment and care of patients. This ruling also sets forth general requirements, among other things, relevant to when a hospital is exempt under Section 501(c)(3):

1. It must be organized as a nonprofit charitable organization for the purpose of operating a hospital for the care of the sick. A nonprofit hospital chartered only in general terms as a charitable corporation can meet the test as being organized exclusively for charitable purposes.
2. It must be operated to the extent of its financial ability for those not able to pay for the services rendered and not exclusively for those who are able and expected to pay. It is normal for hospitals to charge those able to pay for services rendered in order to meet the operating expenses of the institution, without denying medical care or treatment to others unable to pay. It must not refuse to accept patients in need of hospital care who cannot pay for such services.
3. It must not restrict the use of its facilities to a particular group of physicians and surgeons, such as a medical partnership or association, to the exclusion of all other qualified doctors.
4. Its net earnings must not inure directly or indirectly to the benefit of any private shareholder or individual. This includes use by or benefit to its members of its earnings by way of a **distribution of profits**, the payment of excessive rents or excessive salaries, or the use of its facilities to serve their private interests.

Rev. Rul. 69-266, 1969-1 C.B. 151 provides in part that an organization formed and controlled by a medical doctor to conduct research programs consisting of examining and treating patients who are charged prevailing fees for services rendered is not exempt.

Rev. Rul. 69-383, 1969-2 C.B. 113 provides in part that a revenue-sharing arrangement for compensation on the basis of a fixed percentage of departmental income will not necessarily preclude exemption, so long as there was an arms' length transaction, and the compensation is not excessive when compared to amounts received by specialists with similar responsibilities.

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

Rev. Rul. 69-545, 1969-2 C.B. 117 provides in part that the “promotion of health” is considered to be a charitable purpose in the general law of charity.

Rev. Rul. 70-186, 1970-1 C.B. 128 provides that private benefit must be a **necessary by-product** of the activity that benefits the public at large and accomplishes exempt purposes. In other words, the benefit to the public cannot be achieved without necessarily benefitting certain private individuals.

Airlie Foundation, Inc v. Commissioner of Internal Revenue (CIR), 70 T.C. 352 (1978) provides in cases where an organization’s activities could be carried out for either exempt or nonexempt purposes, courts must examine the manner in which those activities are carried out in order to determine their true purpose.

Birmingham Business College, Inc. v. Commissioner, 276, F.2d 476 provides in part that those in control of an organization may not withdraw its earnings under the guise of salary payments.

Church by Mail, Inc. v. CIR, 765 F.2d 1387 (9<sup>th</sup> Cir. 1985) found that a substantial, if not principal purpose of the organization was to generate income for the private benefit of its reverends and their families, who were private persons.

Federation Pharmacy Services, Inc. v. CIR, 625 F. 2d 804 (8th Cir. 1980), dealt with a nonprofit pharmaceutical service providing pharmacy services to the general public. It provided special discount rates for handicapped and seniors in its area, although it was not committed to providing any drugs below cost or free to indigents. Although its services did improve health in the area, it did not qualify for exemption because it was **primarily a commercial venture operated in competition** with other area pharmacies.

IHC Health Plans, Inc. v. CIR, 325 F.3d 1188 (2003) provides in part that to justify charitable exemption, taxpayer health-care provider must make its services available to all in community plus provide additional community benefits, which either further function of government-funded institutions or provide service that would not likely be provided within community but for the subsidy, and additional public benefit conferred must be sufficient to give rise to strong inference that public benefit its primary purpose for which organization operates. The court also provides that the fact that an activity is normally undertaken by commercial for-profit entities does not necessarily preclude charitable tax exemption, particularly where taxpayer entity offers its services at or below-cost. The court also provides that in determining whether charitable exemption is justified, taxpayer organization which does not extend some of its benefits to individuals unable to make the required payments generally **reflects commercial activity** rather than charitable one.

Lorain Ave. Clinic v. CIR, 31 TC 141 provides in part that the presence of a **percentage compensation agreement** will destroy the organization’s exemption under section 501(c)(3) of the Code where such arrangement transforms the principal activity of the organization into a joint venture between it and a group of physicians.

Lowry Hospital Ass’n. v. CIR, 66 TC 850 provides in part that a close relationship between an exempt hospital and a doctor or group of doctors may indicate private inurement, where the exempt hospital is part

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

and parcel of the doctors' personal medical practice and personal financial affairs. The two operations were so integrally interwoven in their daily operation that only the faintest outlines of a separable operating charity may be perceived.

Maynard Hospital Inc. v. CIR, 52 T.C. 1006 (1969) provides in part that it is doubtful whether an organization's operation can be "exclusively" for charitable purposes within the meaning of section 501(c)(3) when its income is being accumulated to increase directly the value of the interests of the stockholders which they expect to receive beneficially.

Northwestern Municipal Ass'n v. United States, 99 F.2d 460, 463 provides in part that the phrase "net earnings", as used in Section 501(c)(3), may include "more than the term net profits as shown by the books of the organization or the difference between the gross receipts and disbursements in dollars."

People of God Community v. CIR, 75 T.C. 127 (1980) provides in part that where a percentage compensation arrangement when no upper limit exists, a portion of the organization's earnings is simply being passed on to the individual. The Court noted that the prohibition against inurement and the prohibition against benefit to private interests do overlap.

Sonora Community Hospital v. CIR, 46 T.C. 51 (1966) provides in part that the mere fact that an organization maintains a hospital does not in and of itself justify the conclusion that it was operated exclusively for charitable purposes. While the diagnosis and cure of disease are indeed purposes that may furnish the foundation for characterizing an activity as "charitable," something more is required. The court adds that of course, a "charitable" hospital may impose charges or fees for services rendered, and indeed its charity record may be comparatively low depending upon all the facts, but a serious question is raised where its charitable operation is virtually inconsequential.

### **Taxpayer's Position**

The taxpayer has not provided a position.

### **Government's Position**

Organizations exempt from federal income tax under Section 501(c)(3) may not allow its net earnings to inure to the benefit of any private shareholder or individual. The Program is not organized and operated exclusively for charitable purposes as its net earnings inures to be benefit of the President and the evidenced by their structure, compensation arrangement, and governing body composition.

### **Structure**

The Court provided in that in determining whether charitable exemption is justified, an organization which does not extend some of its benefits to individuals unable to make the required payments ( ) generally reflects a commercial activity rather than charitable one. The Program does not have specific policies or procedures in place for determining the amount of charged to a . The Program does not have a charity care or similar policy for treating or who become unable to pay while undergoing treatment. The Program does not dictate how much a should be charged, but instead leaves the decision to the individual . The Program



Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

originally provided that it is not a suitable treatment option for                      unable to pay, then later stated it does consider offering services for free and has done so in the past. For these reasons, the Program is like                      , where its operation reflects a commercial activity rather than a charitable one.

In                      , the Court held that the diagnosis and cure of disease is not enough to justify exemption, and while an organization may impose charges and                      for services rendered, a serious question is raised where its charitable operation is virtually inconsequential. The Program wrote in its tax-exemption application that                      are charged                      on an individual basis solely dependent upon the                      s ability to pay, which are considered nominal compared to                      charged by for-profit programs. However, the Program did not provide any evidence to show how its                      were determined to be                      than comparable for-profit entities, such as research or surveys of similar                      in the region. The Program charges                      on a sliding scale based on the                      ability to pay, from \$ - \$                      a session, but does not have any policies to dictate how the                      determine the amount to charge a                      . stated that in                      , most                      paid around \$                      per session, which is at the high end of its range of \$ - \$                      .

The Program has taken little measures to ensure                      are charged based on their ability to pay, and that charity care is provided to                      . Like                      , the Program's charitable operation is virtually inconsequential. The Court acknowledged that reasonable                      may be imposed but providing medical services with little/no consideration for                      does not alone justify tax exemption. The Program has provided little evidence to show a charitable operation beyond the diagnosis and treatment of                      .

Like                      and                      , the amount charity care provided and consideration for                      by the Program is virtually nonexistent, making it indistinguishable from a for-profit program. The Program has not adequately established that its charitable operation is a significant part to be considered substantially different from a for-profit enterprise to justify exemption.

### Compensation of

The Court held in                      that the presence of a percentage compensation agreement will destroy an organization's tax exemption where such arrangement transforms the principal activity of the organization into a joint venture between it and a group of physicians. The Program bears striking similarities with                      , mainly that                      organizations did not fix the charges to be made to                      but left the matter of determining the amounts of charges to be collected to the associated                      . Neither organization's President knew upon what basis or method the individual                      fixed their charges.

Moreover, both the                      and the Program compensated their respective                      based on a percentage of the individual                      collected. This system for fixing the salaries of the individual                      constituted a competitive system with incentives for increasing the extent of the services rendered by the                      and the                      charged for such services. Of course, employees may receive reasonable compensation for their services, but where the method for fixing compensation for services is

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

predominantly one which compensates the individual based on the ratio of their and activity to the whole, so that each is in competition with the other, the operation is one for profit.

Most importantly, both the and the Program distributed substantially all of their net earnings to the associated . The Program indicated on both its Forms and its Profit and Loss Statements for and that it derives % of its income from , and payments to the make up over % of its expenses:

Table 8 – Income and Expense Sources				
Income		Percentage of Income		Percentage of Income
	\$	%	\$	%
<b>Total Income</b>	<b>\$</b>	<b>%</b>	<b>\$</b>	<b>%</b>
Expenses		Percentage of Total Income		Percentage of Total Income
Outside Services	\$	%	\$	%
Payroll Expenses	\$	%	-	-
Salaries	\$	%	-	-
<b>Total Expenses</b>	<b>\$</b>	<b>%</b>	<b>\$</b>	<b>%</b>

As the Court explained, because the compensation arrangements allow and incentivize charges to the , the distribution of substantially all net receipts to the inures to their benefit, which is expressly prohibited for tax-exempt organizations.

Additionally, the Court held in *People of God Community v. CIR* that where a percentage compensation arrangement when no upper limit on earnings exists, a portion of the organization's earnings is simply being passed on to the individual. The Program stated that the highest percentage a can receive from collected is %, and there is no cap or upper limit on the amount of income a can receive. Thus, like the *People of God Community*, the Program's earnings are being passed on to the individuals to their private benefit. The Court also clarified that the prohibition on inurement extends to the founders and other controlling individuals that have a personal stake in the organization's receipts. In the Program, the have complete control over the organization's gross earnings and are distributed substantially all of it through this compensation arrangement.

In *Maynard Hospital Inc. v. CIR*, the Court explained it is doubtful whether an organization's operation can be "exclusively" for charitable purposes within the meaning of section 501(c)(3) when its income is being accumulated to directly increase the value of the interests of the stockholders which they expect to receive beneficially. Though the Program's are not stockholders, they have a personal financial interest in the Program's success due to the compensation arrangement. Thus, they are incentivized to accumulate the

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

Program's earnings to directly increase their personal distributions, causing doubt that the Program is operated "exclusively" for charitable purposes.

In *Birmingham Business College, Inc. v. CIR*, the Court found that those in control of an organization may not withdraw its earnings under the guise of salary payments. Again, the Program's directly controlled the amount of gross receipts collected and received substantially all of it as compensation. The Program mirrors Birmingham Business College, as both organizations had controlling individuals influencing the gross earnings, and later receiving those earnings as compensation.

It is not meant to be implied that all contingent compensation arrangements made by charitable organizations will preclude tax-exempt status. In fact, Rev. Rul. 69-383 provides in part that a revenue-sharing arrangement for compensation based on a fixed percentage of departmental income will not necessarily preclude exemption, so long as there was an arms' length transaction, and the compensation is not excessive when compared to amounts received by specialists with similar responsibilities. However, the record fails to show the Program engaged in arms' length transactions with each , and determined the compensation not to be excessive, as there is no cap or upper limit to the amount of compensation a could receive. The record also fails to show what research or information was gathered to determine a reasonable compensation amount, such as a compensation study or survey.

Lastly, Regulations Section 1.501(c)(3)-1(d)(1)(ii) states that it is necessary for the organization to establish that it is not organized or operated for the benefit of private interests. The fact that the Program compensates its based on a percent of the they collect, where each sets their own to be charged, does not establish that it is organized or operated for public, rather than private, interests.

### Governing Body Composition

Regulations Section 1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized exclusively for any of the purposes specified in Section 501(c)(3) unless it serves public, rather than private interests. Thus, it is necessary for the organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or their family, shareholders of the organization, or persons controlled, directly or indirectly, by such interests.

The Program's Board consists of the founder, , and . The contract between personal corporation, the , and the Program was authorized by the Vice President, . The bills the Program for services provides, and the payment is authorized by the Program's Board, . The Program does not have a conflict-of-interest policy. The collect cash and checks from the , and is responsible for collecting the money, and preparing the bank deposits. also prepares and authorizes the outgoing checks and other payments and is the only in the organization authorized to sign the checks. Based on these facts, the Program has not established that it is *not* organized or operated for the benefit of private interests, which is required by IRC Section 501(c)(3) for tax exemption.

Rev. Rul. 70-186 provides that private benefit must be a necessary by-product of the activity that benefits the public at large and accomplishes exempt purposes. In other words, the benefit to the public cannot be

Form <b>886-A</b>	Department of the Treasury – Internal Revenue Service <b>Explanations of Items</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Periods ended

achieved without necessarily benefitting certain private individuals. In contrast to this Revenue Ruling, there is little evidence to suggest any private benefit conferred to \_\_\_\_\_ and the \_\_\_\_\_ is a necessary by-product of the charitable operation, such as a conflict-of-interest policy, internal controls policy, arms'-length transactions, or other safeguards to prevent misuse of assets and personal enrichment.

### **Net Earnings Inure to the Benefit of Private Interests**

As discussed above, the Program's charity care operation and consideration for \_\_\_\_\_ is virtually inconsequential, making it indistinguishable from a for-profit enterprise. This Program is not designed or suitable for \_\_\_\_\_ or \_\_\_\_\_ who later become \_\_\_\_\_ while receiving \_\_\_\_\_, calling into question how the Program can be considered charitable. Additionally, the \_\_\_\_\_ are incentivized by their compensation arrangement to increase the \_\_\_\_\_ charged to the \_\_\_\_\_ and the extent of the services rendered to the \_\_\_\_\_, going against the Program's assertion that it is charitable and serves \_\_\_\_\_. This compensation arrangement also allows for the Program's net earnings to inure to benefit of the \_\_\_\_\_.

Lastly, the Program's organizational structure creates doubt that it is organized exclusively to serve public, rather than private, interests, as the Board is comprised almost entirely of \_\_\_\_\_ family, where little/no evidence has been presented to show how private benefit is discouraged or prevented.

The record fails to show the Program is organized and operated *exclusively* for charitable purposes, where no part of the net earnings inure to the benefit of any private individual, and thus does not qualify for tax exemption under IRC Section 501(c)(3).

### **Conclusion**

\_\_\_\_\_ does not qualify for tax exemption under section 501(c)(3) because it serves private rather than public interests, where the net earnings inure to the benefit of private individuals.

Since the Program will no longer have tax-exempt status beginning \_\_\_\_\_, they are liable for filing Form \_\_\_\_\_, *U.S. Corporation Income Tax Return*, as of that date.