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

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TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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Date: MAY 21 2002

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Dear Sir or Madam:

This letter is in response to your ruling request under sections 501(c)(3) and 512 of the Internal Revenue Code.

FACTS

You have been recognized by the Internal Revenue Service as tax-exempt under section 501(a) of the Code by reason of being described in section 501(c)(3). In addition, you are not a private foundation by reason of being described in sections 509(a)(1) and 170(b)(1)(A)(iii).

Pursuant to an agreement dated a, you sold your general acute care facility ("Hospital") to L, an unrelated third party. The sale was effective on b. After the sale, your primary function was to continue to provide basic medical care to indigent persons through five medical clinics you operate which are strategically located in various parts of your "Service Area" (as defined below). The operation of these clinics enables you to continue to provide healthcare services to

the uninsured and to those who would not otherwise have access to healthcare services through a private physician.

Your "Service Area" consists of your Primary Service Area, which is the geographical area and population residing in the ten zip codes immediately surrounding your principal offices; and your Secondary Service Area, which is the geographical area and population encompassed by all of the zip codes, any part of which are within a ten-mile radius of your principal offices, but excluding the Primary Service Area.

Most of the residents in the Service Area are extremely poor, consisting primarily of minorities many of whom speak little or no English and who have recently immigrated to the United States. Many of these individuals do not have any healthcare insurance or qualify for Medicare or Medicaid. In addition, many residents are unable to obtain adequate healthcare because they are culturally and linguistically isolated, homeless, elderly, HIV-positive, or excluded from traditional avenues of healthcare.

Pursuant to the law of the State of c, the Attorney General approved the terms of the sale. In addition, the Attorney General is required to regulate the use of proceeds from the sale of significant assets by a c nonprofit institution and to approve a plan developed by the selling organization describing the future use of such proceeds. In the case of your organization, the law requires that the proceeds be held and used for the continuing healthcare benefit of the community.

In compliance with c law, you developed a plan (hereafter, the "Plan") which was approved by the Attorney General, establishing the basis upon which you would continue to use the sales proceeds, together with your other investment assets, to provide healthcare to residents of your Service Area.

An integral part of the Plan was that you will earmark funds from which you will make income distributions, on or after d, to fund emergency room care and related inpatient care provided to "Medically Indigent" persons residing in close proximity to the Hospital. Initially, you will earmark $e for this fund, known as the Emergency Medical Services Fund ("EMS Fund").

In consultation with professional investment advisers, it is your policy to invest the resources of the EMS Fund to maximize total return through balancing current income opportunities with long term capital appreciation potentials, in each case consistent with traditional views of prudence and diversity. To this end, the EMS Fund is primarily invested in marketable securities that are readily tradable on established securities exchanges and which yield current dividend or interest income with the possibility of principal appreciation over a long time horizon. Secondarily, to achieve greater diversity, the resources of the EMS Fund may be invested to a limited extent in real property, private equity offerings and other alternative investments that provide higher than traditional total return opportunities where deemed prudent and opportune.

For purposes of the Plan, a "Medically Indigent" person is an adult person or emancipated minor whose family has an annual gross household income at or below 200 percent of the federal income level applicable to him or her based on the size of his or her family, as set forth in the "Poverty Income Guidelines" published in the Federal Register, where

the medical care required does not qualify for reimbursement from any payor, including governmental reimbursement programs.

Under the Plan, you will pay for emergency room medical care provided to Medically Indigent persons by annually distributing the income earned by the EMS Fund to certain general acute care hospitals located within the Service Area who request reimbursement for "Uncompensated Care" that they provided through their basic or comprehensive emergency medical services rooms in the prior year (hereafter, "Eligible Hospitals"). For this purpose, "Uncompensated Care" is the uncompensated emergency room care provided by Eligible Hospitals to Medically Indigent persons residing in the Service Area, plus the uncompensated inpatient care Eligible Hospitals provided to these persons which arose from admissions to the Eligible Hospitals due to emergency room care provided by Eligible Hospitals to such persons. Eligible Hospitals include the Hospital, other for-profit hospitals and nonprofit hospitals.

You intend to notify the Eligible Hospitals in the Service Area that operate a basic or comprehensive emergency room about the existence of the EMS Fund and about the method of applying for disbursements from the EMS Fund.

The income from the EMS Fund available for distribution will be allocated to each requesting Eligible Hospital in the ratio of (a) the number of emergency room visits by Medically Indigent residents of the Service Area to the Eligible Hospital requesting disbursements, to (b) the total number of emergency room visits by Medically Indigent residents of the Service Area to all Eligible Hospitals requesting disbursements. However, no Eligible Hospital requesting disbursements will be entitled to receive an amount greater than the total amount of Uncompensated Care it provided to Medically Indigent persons residing in the Service Area. For purposes of determining recipients and amounts of disbursements from the EMS Fund, you do not intend to discriminate in favor of nonprofit hospitals over the Hospital or any other for-profit Eligible Hospital. In order for an Eligible Hospital to receive disbursements from the EMS Fund, it must provide, on a timely basis, specific information which will allow you to evaluate the request and, if the request is approved, to allocate a share of the income of the EMS Fund. You intend to use all reasonable commercial efforts to pay the amounts allocated to the hospitals no later than December 31st of each year.

If the total amount of disbursements requested by Eligible Hospitals for a year is less than the income of the EMS Fund for that year, you will retain the income of the EMS Fund that exceeds the amount of the disbursements requested and you will add this excess to the principal of the EMS Fund so as to potentially increase the income of the EMS Fund available to Eligible Hospitals in future years.

If the total amount of disbursements requested by Eligible Hospitals for a years exceeds the income of the EMS Fund for that year, the requesting Eligible Hospitals will receive a portion of the amount requested, as determined by the formula described above.

For each of the first three years beginning d, you estimate that the amount of expenditures you will make for the operation of the five medical clinics and for distributions from the EMS Fund to Eligible Hospitals for providing healthcare services to Medically Indigent persons residing in the Service Area will be as follows:

	****	****	****	****	Percent
Medical Clinics	****	****	****	****	81.3%
EMS Fund	****	****	****	****	18.7%
Total	****	****	****	****	100.0%

Approximately f hospitals qualify as Eligible Hospitals, of which approximately g are for-profit hospitals, including the Hospital, and the remaining hospitals are either nonprofit or city or county hospitals. Collectively, the f Eligible Hospitals have approximately h emergency stations or beds, of which i (20.9%) are located in for-profit hospitals, including j (4%) in the Hospital.

For each of the first three years beginning d, you estimate that the EMS Fund will earn approximately $k each year, which you estimate will be distributed as follows:

Hospital	$ ****	12%
Other for-profit hospitals	****	0%
Nonprofit or city/county hospitals	****	88%
Total	$ ****	100%

For each of the first three years beginning d, you estimate that the Eligible Hospitals will provide healthcare services to approximately l Medically Indigent persons, as follows:

Hospital	****	12.2%
Other for-profit hospitals	****	0.0%
Nonprofit or city/county hospitals	****	87.8%
Total	****	100.0%

RULINGS REQUESTED

1. Distributions of income from the EMS Fund to nonprofit and for-profit hospitals, including the Hospital, for reimbursement of Uncompensated Care they provided to Medically Indigent persons residing in the Service Area, pursuant to the Plan described above, will not adversely affect your status as an organization described in section 501(c)(3) of the Code.

2. Pursuant to section 512(b) of the Code, dividends, interest, royalties, rents and capital gains earned by the EMS Fund will be excluded from unrelated business taxable income under section 512(a)(1), except to the extent provided in section 512(b)(4).

APPLICABLE LAW

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

Section 1.501(c)(3)-1(c)(1) of the Income Tax 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). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Under section 1.501(c)(3)-1(c)(2) of the regulations, for an organization to qualify for exemption under section 501(c)(3) of the Code, it must not confer any of its net earnings on persons who have a personal or private interest in the activities of the organization, as defined in section 1.501(a)-1(c) and commonly referred to as "insiders."

Section 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. It further states that "to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized and operated for the benefit of private interests...."

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the Tax Court defined private benefit as: "nonincidental benefits conferred on disinterested persons that serve private interests." Benefits are not incidental if they are both qualitatively and quantitatively incidental. Qualitatively incidental means that the private benefit is a mere byproduct of the public benefit. (See, e.g., Rev. Rul. 70-186, 1970-1 C.B. 128; Rev. Rul. 75-286, 1975-2 C.B. 210. For private benefit to be quantitatively incidental, it must be insubstantial in amount. The private benefit must be compared to the public benefit of the specific activity in question, not the public benefit provided by all the organization's activities.

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. See Restatement (Second) of Trusts, sections 368, 372 (1959); 4A Austin W. Scott and William F. Fratcher, The Law of Trusts, sections 368, 372 (4th ed. 1989).

In evaluating whether a nonprofit hospital qualifies as an organization described in section 501(c)(3) of the Code, Rev. Rul. 69-545, 1969-2 C.B. 117, compares two hospitals. The first hospital discussed is controlled by a board of trustees composed of independent civic leaders. In addition, the hospital maintains an open medical staff, with privileges available to all qualified physicians; it operates a full-time emergency room open to all regardless of ability to pay; and it otherwise admits all patients able to pay (either themselves, or through third party payers such as private health insurance or government programs such as Medicare). In contrast, the second hospital is controlled by physicians who have a substantial economic interest in the hospital. This hospital restricts the number of physicians admitted to the medical staff, enters into favorable rental agreements with the individuals who control the hospital, and limits emergency room and hospital admission substantially to the patients of the physicians who control the hospital. Rev. Rul. 69-545 notes that in considering whether a nonprofit hospital is operated to serve a private interest, the Service will weigh all the relevant facts and circumstances in each case, including the use and control of the hospital. The revenue ruling concludes that the first hospital continues to qualify as an organization described in section 501(c)(3) and the second hospital does not because it is operated for the private benefit of the physicians who control the hospital.

Thus, under Rev. Rul. 69-545, a hospital must satisfy a community benefit standard to qualify for exemption under section 501(c)(3) of the Code. The community benefit standard focuses on a number of factors to determine if a hospital operates to benefit the community as a whole. The community benefit standard applies to other health care provider organizations in addition to hospitals. See Eastern Kentucky Welfare Rights Org. v. Simon, 506 F.2d 1278 (D.C. Cir. 1974), vacated on other grounds, 426 U.S. 26 (1975); and Sound Health Association, 71 T.C. 158 (1978), acq., 1981-2 C.B. 2.

Rev. Rul. 83-157, 1983-2 C.B. 94, held that a nonprofit hospital identical to the hospital in Rev. Rul. 69-545, except it did not operate an emergency room, can still qualify under I.R.C. 501(c)(3) if other significant factors establish that it operates exclusively to benefit the community as a whole.

Section 509(a)(2) of the Code provides that an organization which normally receives more than one-third of its support from various sources, including gross receipts from the performance of services which are in furtherance of the organization's tax-exempt purposes, and which normally receives less than one-third of its support from certain other sources, is excluded from private foundation status. See section 1.509(a)-3 of the regulations.

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 carrying on the trade or business, both computed with the modifications provided in section 512(b). These modifications are the exclusion of dividends and interest, royalties, certain rents, and capital gains. However, under section 512(b)(4), notwithstanding these exclusions, items of gross income (less applicable deductions) relating to debt-financed property (as defined in section 514(b)) are included in unrelated business taxable income.

RATIONALE

To qualify for exemption under section 501(a) of the Code as an organization described in section 501(c)(3) of the Code, a hospital or other health care provider must satisfy the community benefit standard under Rev. Rul. 69-545, supra. To do this, the organization must establish the presence of significant factors demonstrating that it promotes the health of a class of persons that is broad enough so that the community as a whole benefits. As long as a health care provider can establish the presence of these significant factors, it is not required that it establish the presence of all the factors in Rev. Rul. 69-545 for the organization to satisfy the community benefit standard.

Your primary function is to provide basic medical care to indigent persons through five medical clinics you operate in various parts of your Service Area. The operation of these clinics enables you to continue to provide healthcare services to the uninsured and to those who would not otherwise have access to healthcare services through a private physician.

Under the Plan, you will pay for emergency room medical care provided to Medically Indigent persons by annually distributing the income earned by the EMS Fund to certain general acute care hospitals, including the Hospital, located within your Service Area who request reimbursement for Uncompensated Care that they provided through their basic or comprehensive emergency medical services room in the prior year. Once the Plan is implemented, you expect that approximately 81.3 percent of your expenditures will continue to be made for the operation of the five medical clinics and approximately 18.7 percent will be made for distributions under the Plan to for-profit hospitals, including the Hospital. By engaging in these activities, you will continue to benefit the community as a whole in compliance with the community benefit standard in Rev. Rul. 69-545. In addition, you will continue to be engaged primarily in activities which accomplish your charitable purposes and thus will continue to be operated exclusively for charitable purposes under section 1.501(c)(3)-1(c)(1) of the regulations.

Under the Plan, reimbursing the for-profit hospitals, including the Hospital, for expenses they incur in providing emergency services to charitable recipients will not constitute the distribution of net earnings to these hospitals; instead, this activity will further your charitable purposes. Furthermore, none of these hospitals, including the Hospital, are insiders as defined in section 1.501(a)-1(c) of the regulations. Therefore, under the Plan you will not violate the proscription against inurement of net earnings under section 1.501(c)(3)-1(c)(2).

Similarly, under the Plan, your reimbursement of for-profit hospitals, including the Hospital, for expenses they incur in providing emergency services to charitable recipients will confer upon these hospitals benefits which will be both quantitatively and qualitatively incidental. For example, in 2003, you expect that approximately 12 percent of your total expenditures will be made to the Hospital and that approximately 12 percent of the Medically Indigent persons served under the Plan will be served by the Hospital. Thus, you will not be conferring impermissible private benefits upon these hospitals, including the Hospital, and will continue to serve public rather than private interests within the meaning of section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

Therefore, following implementation of the Plan, you will continue to satisfy the requirements for exemption under section 501(a) of the Code as an organization described in section 501(c)(3).

As a result of investing the EMS Fund, you expect to earn dividends, interest, royalties, rents, and capital gains. Under section 512(b) of the Code, dividends, interest, royalties and certain rents are excluded from unrelated business taxable income, except to the extent that these items of gross income (less applicable deductions) relate to debt-financed property (as defined in section 514(a)). Therefore, income earned from investing the EMS Fund, including capital gains, will be excluded from unrelated business taxable income under section 512(a)(1), except to the extent that these items of gross income (less applicable deductions) relate to debt-financed property.

RULINGS

1. Distributions of income from the EMS Fund to nonprofit and for-profit hospitals, including the Hospital, for reimbursement of Uncompensated Care they provided to Medically Indigent persons residing in the Service Area, pursuant to the Plan

described above, will not adversely affect your status as an organization described in section 501(c)(3) of the Code.

2. Pursuant to section 512(b) of the Code, dividends, interest, royalties, rents and capital gains earned by the EMS Fund will be excluded from unrelated business taxable income under section 512(a)(1), except to the extent provided in section 512(b)(4).

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

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.

These rulings are directed only to the organization that requested them and may not be used or cited by others as precedent.

Please keep a copy of this letter in your permanent records.

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

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

(signed) Marvin Friedlander

Marvin Friedlander
Manager, Exempt Organizations
Technical Group 1