



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

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Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

UIL Code:

501.00-00

513.00-00

236286

SE: T: EO: KA: TI

Legend:

X =

Y =

Z =

City a =

City b =

State x =

State y =

Date a =

Dear :

We have considered your request for rulings under sections 501(c)(3), 509 and 513 of the Internal Revenue Code.

Facts

Y was formed as a non-stock, non-profit corporation to establish and operate a blood banking facility in City a, State x. The Internal Revenue Service recognized Y as an organization described in section 501(c)(3) of the Code and as a public charity under section 509(a)(2).

Y solicits the donation of blood from volunteer donors, collects, analyzes and processes the blood and supplies blood products to hospitals and outpatient facilities as well as improving and advancing the science and practice of blood transfusion therapy. Y operates under a license granted by the United States Food and Drug Administration (FDA). To comply with FDA regulations, Y developed appropriate management and information systems, and therefore, developed considerable expertise in such systems.

Y's amended Articles of Incorporation state that its purposes include:

- a) Soliciting and facilitating the donation of human blood by volunteer donors in State x, states contiguous to State x and throughout the United States;
- b) Analyzing and processing donated blood and supplying blood products to hospitals and outpatient treatment facilities in State x, states contiguous to State x and throughout the United States;
- c) Improving and advancing the science and practice of blood transfusion therapy in State x, states contiguous to State x and throughout the United States; and
- d) Managing human blood bank programs in State x, states contiguous to State x and throughout the United States.

X was incorporated as a non-stock, non-profit organization to support the charitable, educational, and scientific activities of Y, of which X is the sole member. The Internal Revenue Service recognized X as an organization described in section 501(c)(3) of the Code and as a supporting organization under section 509(a)(3). X provides various services to Y, including policy-making, long-range strategic planning, accounting, financial reporting, marketing and public relations, human resources, legal and professional, purchasing and billing, and information technology. X is funded through payments from Y for the services X provides to Y. X either distributes or loans its income to Y, or invests in assets that will ultimately be used to benefit Y. X does not hold any significant assets other than its membership interest in and loans to Y. The same people serve on the Board of Directors and are senior officers of both X and Y.

Z is an unrelated non-stock, non-profit corporation that was formed through a collaboration of hospitals in City b, State y to ensure a safe and cost-effective alternative to the American Red Cross as a blood banking facility. The Internal Revenue Service recognized Z as an organization described in section 501(c)(3) of the Code and as a public charity under section 509(a)(2).

On Date a, Y entered into a three-year agreement with Z ("Management Agreement"), under which Y agreed to assist Z in developing and operating a new blood banking facility in City b, State y. Y agreed to manage Z's FDA regulated blood banking and related activities at this facility until Z is able to operate independently under its own FDA license. Because Z does not have its own FDA license to operate a blood banking facility, it operates under Y's license. The Management Agreement provides that, as soon as reasonably practicable, Z will obtain its own FDA license, hire its own staff, and be independently responsible for its operations and activities. Furthermore, to facilitate a transition to independent operation, Y will prepare and submit to the Board of Directors a transition plan that outlines how Z will transition to independent operation.

Under the Management Agreement, Y has total control over all of Z's activities in accordance with FDA regulations. Both parties agree that Z will not take any action or direct Y

to take any action that would jeopardize Y's FDA license. Y represents that if the FDA finds a deviation as part of its inspection of Z, the penalty would be levied against Y's entire blood banking system.

Furthermore, Y represents that it is unaware of any organization other than itself that allows another blood center to operate under its FDA license. In addition, Y states that it does not believe an integrated package of management services provided under an FDA license is commercially available to Z from any source other than Y.

Under the Management Agreement, Y provides Z with various FDA-related management, clinical services and technology services. Y also provides Z with access to all of Y's FDA-mandated regulatory documents and policies and procedures as listed in the Management Agreement. Y receives compensation from Z for providing these services. Y represents that the payment for services by Z has declined since the inception of the contract based upon the continuing reduction of services provided by Y.

X is not a party to the Management Agreement. However, X supports Y in its performance of certain contractual obligations under the Management Agreement such as providing financial and budgetary reporting, accounting, marketing and public relations, purchasing and billing, and human resources services. Accordingly, X will be providing services and receiving compensation attributable to the contract with Z.

Rulings Requested

1. Y's provision of services to Z under the Management Agreement does not adversely affect either X's or Y's current tax-exempt status as an organization described in section 501(c)(3) of the Code.
2. Y's provision of services to Z under the Management Agreement does not constitute an unrelated trade or business to Y, and X's provision of services to Y does not constitute an unrelated trade or business to X, within the meaning of section 513 of the Code.
3. Y's income from the provision of services to Z under the Management Agreement does not adversely affect its current status as a public charity described in section 509(a)(2) of the Code.
4. Y's provision of services to Z under the Management Agreement does not adversely affect X's current status as a supporting organization under section 509(a)(3) of the Code.
5. Y's provision of services to Z under the Management Agreement does not adversely affect the ability of donors to either X or Y to deduct contributions under section 170 of the Code.

Law

Section 170 of the Code provides a deduction for charitable contributions to or for the use of corporations organized under the laws of the United States; and operated exclusively for religious, charitable, scientific, or educational purposes; no part of the net earnings of which inures to the benefit of any private shareholder or individual; if it is used within the United States.

Section 501(c)(3) of the Code describes organizations that are organized and operated exclusively for charitable and other exempt purposes, no part of the net earnings of which inure to the benefit of any private shareholder or individual.

Section 509(a)(2)(A)(ii) of the Code provides, in part, that the term "private foundation" includes a domestic organization described in section 501(c)(3) other than an organization which normally receives more than one-third of its support in each taxable year from gross receipts from the performance of services in an activity which is not an unrelated trade or business (within the meaning of section 513).

Section 509(a)(3) provides that the term "private foundation" means a domestic or foreign organization described in section 501(c)(3) other than an organization which:

(A) is organized, and at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in section 509(a)(1) or (2);

(B) is –

- i. operated, supervised, or controlled by one or more organizations described in section 509(a)(1) or (2),
- ii. supervised or controlled in connection with one or more such organizations, or
- iii. operated in connection with one or more such organizations, and

(C) is not controlled directly or indirectly by one or more disqualified persons (as defined in section 4946) other than foundation managers and other than one or more organizations described in section 509(a)(1) or 2.

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 that 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 are not in furtherance of an exempt purpose.

Section 1.513-1(d)(2) of the regulations states that for the conduct of a 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 those purposes.

Rev. Rul. 66-323, 1966-2 C.B. 216, held that a blood bank organized and operated to provide a community with facilities to collect, store and distribute human blood may be recognized as exempt under section 501(c)(3) of the Code. However, the sale of blood and blood products to commercial laboratories constitutes income from an unrelated trade or business, and is taxable under section 511.

Rev. Rul. 72-369, 1972-2 C.B. 245, held that an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations does not qualify for exemption, because the provision of these services constitute a trade or business ordinarily carried on for profit.

Analysis

Ruling No. 1

Operating a blood banking facility furthers an exempt purpose under section 501(c)(3) of the Code because it promotes the health of the community. Rev. Rul. 66-323, *supra*. Here, Y assists Z in developing and operating a new blood banking facility in City b, State y until Z is able to operate independently under its own FDA license. Y has total control over all of Z's activities in accordance with FDA regulations. Y provides Z with various FDA-related management and clinical services under Y's FDA license, as well as access to all of Y's FDA mandated regulatory documents and policies and procedures. The FDA treats Z as a collection and production site of Y and any deviation from FDA standards would negatively impact Y's entire blood banking system, not just the deviating center. Z will be considered a part of Y's operations until Z is able to operate independently.

Y's establishment and operation of its FDA licensed blood banking facility furthers its tax-exempt charitable purpose of promoting health. The operation of a new FDA licensed blood banking facility in another location will help meet the needs of that community and benefit the public. Therefore, Y's provision of services to Z under the Management Agreement will not adversely affect Y's current tax-exempt status as an organization described in section 501(c)(3) of the Code and section 1.501(c)(3)-1(c)(1) of the regulations.

Since X will continue to support Y in Y's performance of its obligations under the Management Agreement, X will also continue to be described in section 501(c)(3).

Ruling No. 2

We concluded above that Y's operation of Z's blood banking facility furthers an exempt purpose under section 501(c)(3) of the Code because it promotes the health of the community. The FDA-mandated services that Y provides to Z under the Management Agreement constitute a unique package of related services not otherwise available to Z. In particular, these services are distinguishable from the commercial services provided by the organization described in Rev. Rul. 72-369, *supra*, which was formed to provide management and consulting services to unrelated exempt organizations. Accordingly, we conclude further that Y's services to Z under the Management Agreement are substantially related to the achievement of Y's exempt

purposes within the meaning of section 1.513-1(d)(2) of the regulations and do not constitute an unrelated trade or business to Y within the meaning of section 513(a) of the Code.

The exempt purpose of X is to support the charitable, educational, and scientific activities of Y. The various management and administrative services X provides to Y are substantially related to the achievement of X's exempt purpose within the meaning of section 1.513-1(d)(2) of the regulations. Therefore, X's provision of these services to Y does not constitute an unrelated trade or business to X within the meaning of section 513(a) of the Code.

Ruling No. 3

Public support under section 509(a)(2)(A)(ii) of the Code includes gross receipts from the performance of services in an activity that is not an unrelated trade or business (within the meaning of section 513), but only to the extent that the gross receipts from any person in a year do not exceed the greater of \$5,000 or one percent of the organization's support for that year. We concluded above that Y's provision of services to Z under the Management Agreement does not constitute an unrelated trade or business to Y within the meaning of section 513(a) of the Code.

Thus, the fees Y receives from Z for providing services to Z under the Management Agreement constitute public support under section 509(a)(2)(A)(ii), but only to the extent that the fees from Z in any year do not exceed the greater of \$5,000 or one percent of Y's total support for that year.

Ruling No. 4

The Internal Revenue Service recognized X as an organization described in section 501(c)(3) of the Code and as a supporting organization under section 509(a)(3). By X providing various services to Y, X continues to be organized and operated to support or benefit Y. In addition, X continues to be supervised or controlled in connection with Y, an organization described in section 509(a)(2) of the Code. Accordingly, X continues to meet the requirements under section 509(a)(3) as a supporting organization.

Ruling No. 5

We have concluded that Y's provision of services to Z under the Management Agreement does not adversely affect either X's or Y's current tax-exempt status under section 501(c)(3) of the Code. Because X and Y continue to be described in section 170, donors may continue to deduct contributions to X and Y in accordance with the law.

Rulings

1. Y's provision of services to Z under the Management Agreement does not adversely affect either X's or Y's current tax-exempt status as an organization described in section 501(c)(3) of the Code.

2. Y's provision of services to Z under the Management Agreement does not constitute an unrelated trade or business to Y, and X's provision of services to Y does not constitute an unrelated trade or business to X, within the meaning of section 513 of the Code.
3. Y's income from the provision of services to Z under the Management Agreement does not adversely affect its current status as a public charity described in section 509(a)(2) of the Code.
4. Y's provision of services to Z under the Management Agreement does not adversely affect X's current status as a supporting organization under section 509(a)(3) of the Code.
5. Y's provision of services to Z under the Management Agreement does not adversely affect the ability of donors to either X or Y to deduct contributions under section 170 of the Code.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept 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.

Sincerely,

Steven B. Grodnitzky
Manager, Exempt Organizations
Technical Group 1