BZA Case No. 19659- Federation of State Medical Boards ("FSMB")

List of Documents accompanying Rebuttal:

1. Articles of Incorporation.
   The Articles of Incorporation of FSMB provide that the FSMB is "operated exclusively for scientific and education purposes." To help achieve these objectives, the FSMB studies, determines, advocates and/or advances the adoption and maintenance by the District of Columbia, the several states of the United States and its territories and insular possessions of adequate and uniform standards for licensure in medicine. The FSMB also develops and improves the quality of licensing examinations given to members of the medical profession and assists by means of research and study the member medical boards to improve the quality of their examinations.

2. DC Board of Medicine Website.
   The DC Board of Medicine is a member of FSMB. It's mission statement is "To protect and enhance the health, safety, and well-being of District of Columbia residents by promoting evidence-based best practices in health regulation, high standards of quality care and implementing policies that prevent adverse events."

3. Definition of Non-Profit under ZR-16 vs. definition of 501(c)(3) organization.
   Text of each definition is included, showing significant differences in the two definitions.

4. Kentucky Bar Foundation v. Commissioner, 78 T.C. 921(1982).
   The Oppositions' legal expert cited Rev. Rul. 73-567 to argue that the FSMB cannot meet the requirements of "exclusive operation" under 501(c)(3) because professional certification activities are ineligible under this section. Rev. Rul. 73-567 is clearly distinguishable from the activities of FSMB. The organization described in that ruling was an organization providing board certification in a particular specialty. The ruling also indicated that the organization was formed by members of the medical profession.

   Further, *Kentucky Bar Foundation* is one of at least two cases that rejects the view that professional organizations further the private business interests of the members rather than the public. In that case, the Tax Court held that an organization formed to provide facilities for the operation of the Kentucky State Bar Association, a unified bar, was nonetheless eligible for section 501(c)(3) status. The Service argued that several activities, including an ethics inquiry tribunal, furthered the private interests of lawyers, rather than the public. The court held that protection of the public from unethical lawyers primarily furthered the public interest and was consistent with section 501(c)(3) status for the organization.

5. Professional Standards Review Organizations vs. Commissioner, 74 T.C. 240 (1980).
   Originally, the Service originally concluded that Professional Standards Review Organizations did not qualify for exemption, notwithstanding that they were authorized by Congress to carry out functions relating to implementation of Medicare and Medicaid.

After losing several cases, including Professional Standards Review Organization of Queens County in the Tax Court, and a similar case in the District Court for the District of Columbia, the Service finally capitulated and ruled that PSROs qualified for exemption. See also Rev. Rul. 81-276.

6. DocInfo.
   As part of serving the general public, the FSMB hosts the free service called DocInfo where the general public can search disciplinary records of physicians and learn how to file a complaint. The DocInfo service has been highlighted in Consumer Reports as a best resource for patients.

ARTICLES OF INCORPORATION OF
THE FEDERATION OF STATE MEDICAL BOARDS OF THE UNITED STATES, INC.

The undersigned hereby associate themselves together for the purpose of forming a nonprofit corporation pursuant to Article 19, Chapter 21, Reissue Revised Statutes of 1943, more commonly known as the Nebraska Nonprofit Corporation Act, and for that purpose adopt these Articles of Incorporation, to wit:

ARTICLE I

The name of the corporation shall be the Federation of State Medical Boards of the United States, Incorporated.

ARTICLE II

The corporation shall have perpetual existence.

ARTICLE III

The corporation is organized exclusively for scientific and educational purposes, and its activities shall include the furtherance of the following objects and purposes:

SEC. A. To keep itself and its members informed concerning the medical and other healing arts practice acts of the District of Columbia, the several states of the United States and its territories and insular possessions, and of foreign countries, and of rules and regulations promulgated thereunder and concerning other pertinent desirable practices, methods or factors relating to the medical and other healing art licensure.

SEC. B. To study, determine, advocate and /or advance the adoption and maintenance by the District of Columbia, the several states of the United States and its territories and insular possessions of adequate and uniform standards for licensure in medicine and/or in the healing arts, and of proper administrative and enforcement provisions in such practice acts, and to study, determine, advocate and/or advance the interstate and interjurisdictional endorsement of medical licensure on such terms and under such conditions as the organization may determine desirable to protect and promote uniformity in the administration of medical practice acts.

SEC. C. To develop and improve the quality of licensing examinations given to members of the medical profession, and to assist by means of research and study the member medical boards to improve the quality of their examinations.

SEC. D. To obtain and disseminate information regarding proposed legislation and administrative actions affecting the healing arts and licensure.

ARTICLE IV

SEC. A. To conduct its affairs, the corporation shall have and exercise all of the powers enumerated in Section 21-1904, R.R.S. 1943, together with any and all powers granted by the Nebraska Nonprofit Corporation Act and the laws of the State of Nebraska which may be necessary or convenient to carry out the purposes for which the corporation is organized, provided such acts and powers are in furtherance of the educational and scientific purposes of the corporation and provided further that no substantial part of the activities or funds of the corporation shall be devoted to carrying on propaganda or otherwise attempting to influence legislation and the corporation shall not participate or intervene in any political campaign on behalf of any candidate for public office.

SEC. B. The corporation may contract and become bound for debts and may convey, encumber or charge its property after an affirmative vote of at least a majority of the members of the Board of Directors.

SEC. C. Upon dissolution or final liquidation of the corporation, all remaining assets shall be distributed only for scientific or educational purposes.

ARTICLE V

The corporation shall have members which will be classified as follows:

SEC. A. Medical Boards

SEC. B. Fellows

SEC. C. Honorary Fellows

SEC. D. Associate Members

SEC. E. Courtesy Members

SEC. F. Affiliate Member Boards

The qualifications, rights, obligations and manner of election of the members in each of the various categories of membership shall be set forth in the corporation's Bylaws. The corporation shall not issue stock and shall declare no dividends.

ARTICLE VI

The affairs of the corporation shall be conducted by a Board of Directors of not less than five members, the exact number of which shall be fixed by the Bylaws, including a President, a President-elect, Vice President, Secretary, Treasurer and such other officers as may be provided for in the Bylaws. The members of the Board of Directors and the officers shall be elected or appointed at such times and in such manner and for such terms as may be prescribed in the Bylaws.

ARTICLE VII

There shall be nine Directors constituting the initial Board of Directors. The names and addresses of the persons serving as the initial Directors are:

R.C. Derbyshire, MD
227 East Palace Avenue
Santa Fe, New Mexico

George H. Lage, MD
812 S.W. Washington St.
Portland, Oregon

Rhett McMahon, MD
304 Reymond Building
Baton Rouge, Louisiana

M.H. Crabb, MD
1707 Medical Arts Building
Fort Worth, Texas

Harold E. Jervey, Jr., MD
1515 Bull Street
Columbia, South Carolina

Frederick T. Merchant, MD
1051 Harding Memorial Parkway
Marion, Ohio

Leo T. Heywood, MD
828 Medical Arts Building
Omaha, Nebraska

P.T. Lamey, MD
422 Citizens Bank Building
Anderson, Indiana

Bernard A. O'Hora, MD
110 West Sugnet Road
Midland, Michigan

ARTICLE VIII

The corporation's registered address is to be the address of the executive office of the Federation of State Medical Boards, designated as the Secretary's office until a permanent executive office is established.

ARTICLE IX

The names and addresses of the incorporators are:

R.C. Derbyshire, MD
227 East Palace Avenue
Santa Fe, New Mexico

Frederick T. Merchant, MD
1061 Harding Memorial Parkway
Marion, Ohio

George H. Lage, MD
812 S.W. Washington St.
Portland, Oregon

Leo T. Heywood, MD
828 Medical Arts Building
Omaha, Nebraska

Rhett McMahon, MD
304 Reymond Building
Baton Rouge, Louisiana

P.T. Lamey, MD
422 Citizens Bank Building
Anderson, Indiana

M.H. Crabb, MD
1707 Medical Arts Building
Fort Worth, Texas

Bernard A. O'Hora, MD
110 West Sugnet Road
Midland, Michigan

Harold E. Jervey, Jr., MD
1515 Bull Street
Columbia, South Carolina

ARTICLE X

The private property of the incorporators, directors and officers shall not be subject to the payment of corporate debts.

ARTICLE XI

The Articles of Incorporation may be amended at any duly called meeting of the members of the corporation by the affirmative vote of at least three-fourths of the Medical Board members present and voting. The corporation's Bylaws may be adopted, amended or repealed in such a manner as may be provided in the Bylaws.

IN WITNESS WHEREOF, we execute these Articles of Incorporation this 8th day of February 1966.

/s/ R.C. Derbyshire, MD
/s/ Rhett McMahon, MD
/s/ Harold E. Jervey, Jr., MD
/s/ Leo T. Heywood, MD
/s/ Bernard A. O'Hora, MD
/s/ George H. Lage, MD
/s/ M.H. Crabb, MD
/s/ Frederick T. Merchant, MD
/s/ P.T. Lamey, MD

On the 8th day of February 1966, before me, the undersigned Notary Public in and for Douglas County, State of Nebraska, personally appeared R.C. Derbyshire, MD; George H. Lage, MD; Rhett McMahon, MD; M.H. Crabb, MD; Harold E. Jervey, Jr., MD; Frederick T. Merchant, MD; Leo T. Heywood, MD; P.T. Lamey, MD; and Bernard A. O'Hora, MD, to me known to be the identical persons whose names are subscribed to the foregoing instrument, and they acknowledge the execution thereof and the signatures thereon to be their voluntary act and deed for the purposes set out therein.

IN WITNESS WHEREOF, I have hereunto set my hand and notorial seal the date last above written.

(SEAL) /s/ William J. Hotz, Jr.
Notary Public

Amendments to the Articles of Incorporation of the Federation of State Medical Boards of the United States, Inc.:

April 12, 2003: Article VI of the Articles of Incorporation of the Federation of State Medical Boards of the United States, Inc., was amended by the House of Delegates on April 12, 2003, to read:

> The affairs of the corporation shall be conducted by a Board of Directors of not less than five members, the exact number of which shall be fixed by the Bylaws, including a Chair, a Chair-Elect, Vice Chair, Secretary, Treasurer and such other officers as may be provided for in the Bylaws. The members of the Board of Directors and the officers shall be elected or appointed at such times and in such manner and for such terms as may be prescribed in the Bylaws.

May 1, 2004: Article VI of the Articles of Incorporation of the Federation of State Medical Boards of the United States, Inc., was amended by the House of Delegates on May 1, 2004, to read:

> Effective at the time of the House of Delegates Annual Meeting in 2006, the affairs of the corporation shall be conducted by a Board of Directors of not less than five members, the exact number of which shall be fixed by the Bylaws, including a Chair, a Chair-Elect, Secretary, Treasurer and such other officers as may be provided for in the Bylaws. The members of the Board of Directors and the officers shall be elected or appointed at such times and in such manner and for such terms as may be prescribed in the Bylaws."

April 22, 2017: Article V of the Articles of Incorporation of the Federation of State Medical Boards of the United States, Inc., was amended by the House of Delegates on April 22, 2017, as follows:

The corporation shall have members which will be classified as follows:

SEC. A. Medical Boards

SEC. B. Fellows

SEC. C. Honorary ~~Members~~ Fellows

SEC. D. Associate Members

SEC. E. ~~Life Members~~ Courtesy Members

SEC. F. Affiliate Member Boards

Department of Health

Office Hours
Monday to Friday, 8:15 am to 4:45 pm, except District holidays

Connect With Us
899 North Capitol Street, NE, Washington, DC 20002
Phone: (202) 442-5955
Fax: (202) 442-4795
TTY: 711
Email: doh@dc.gov

Ask the Director
Agency Performance

Amharic (አማርኛ)
Chinese (中文)
French (Français)
Korean (한국어)
Spanish (Español)
Vietnamese (Tiếng Việt)

Listen

SHARE

Board of Medicine

ATTENTION: The DC Board of Medicine has changed it's processes regarding Physician Assistant Delegation Agreements. The Board is no longer issuing letters "approving" Delegation Agreements, but instead will only be confirming receipt of said agreements via email. All other requirements for Physician Assistant Delegation Agreements remain in effect.

Mission Statement

"To protect and enhance the health, safety, and well-being of District of Columbia residents by promoting evidence-based best practices in health regulation, high standards of quality care and implementing policies that prevent adverse events."

Established in 1879, the DC Board of Medicine (BoMed), a division within the DC Department of Health, Health Regulation and Licensing Administration (HRLA), has the responsibility to regulate the practice of medicine (MD/DO) in the District of Columbia.

The Board accepts applications for licensure through national examination; waiver of national examination; reactivation of an inactive license; reinstatement of an expired, suspended, or revoked license, or by eminence pursuant to the Health Occupations Revision Act (HORA). All applicants for licensure must establish, to the Board's satisfaction, that they possess the appropriate skills, knowledge, judgment, and character to practice medicine in the District of Columbia. In addition, applicants must demonstrate to the Board that they are proficient in understanding and communicating medical concepts and information in English.

The Board also oversees the regulation of Trauma Technologists, Physician Assistants, Naturopathic Physicians, Anesthesiology Assistants, Acupuncturists, Surgical Assistants, Polysomnographers, and Postgraduate Physicians in Training. Regulation is achieved through the application process; the disciplinary process and through outreach and educational activities.

Members of the Board are appointed by the Mayor and serve a three year term for a maximum of three terms. The Board issues a **quarterly newsletter** that provides up-to-date information on the Board's current activities.

The Board meets on the last Wednesday of each month, unless otherwise noted. Open session is from 8:30 am - 9:30 am and members of the public are invited to join the Board. If you would like to present a topic, you must schedule a time to be placed on the agenda. Contact Lisa Robinson at **lisaa.robinson@dc.gov**. Executive session is closed to the public.

Definition of "Non-Profit" differs from 501(c)(3)

501(c)(3)

- Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.
- Source: 26 U.S. Code § 501(c)(3)

ZR 16 Regulations

- **Organization, Non-Profit**: An organization organized, registered with the appropriate authority of government, and operated exclusively for religious, charitable, literary, scientific, community, or educational purposes, or for the prevention of cruelty to children or animals; provided that no part of its net income inures to the benefit of any private shareholder or individual

Tax Court & Board of Tax Appeals Reported Decisions

KENTUCKYBARFOUNDATION v. COMMISSIONER, 78 TC 921, Code Sec(s) 501.

KentuckyBarFoundation, Inc., a Non-Stock, Non-Profit Corporation, Petitioner v. Commissioner of Internal Revenue, Respondent

Case Information:

[pg. 921]

Code Sec(s):	501
Docket:	Docket No. 14892-80X.
Date Issued:	06/09/1982
Judge:	Opinion by Fay, *J.*
Disposition:	Decision for taxpayer.

HEADNOTE

1.EXEMPT ORGANIZATIONS-Organization descriptions-religious, charitable, etc. organizations-public purposes

distinguished from private interest. Non-profit foundation formed by Kentucky State Bar Association to raise funds for construction of Bar Center was exempt organization. IRS Claim that Bar Center activities dealing with lawyer referral service, client security fund, inquiry tribunal and fee arbitration plan served substantial nonexempt purpose of promoting, protecting and enhancing legal profession was rejected. Bar Center activities all served charitable purposes and any private or non-exempt purpose was insignificant.

Reference(s): 1982 P-H Fed ¶21,025(5) Code Sec. 501 .

Syllabus

Official Tax Court Syllabus

Petitioner, a nonprofit organization, was operated to accumulate funds for the purpose of acquiring land for and contributing to the cost of constructing the proposed Kentucky Bar Center Headquarters, which will house the offices of petitioner, the Kentucky Bar Association, a public law library, and other public areas. *Held*: Any benefit accruing to the legal profession through the activities to be conducted at the Kentucky Bar Center Headquarters is incidental to the broad charitable purposes served by those activities. Thus, petitioner is an exempt organization within the meaning of sec. 501(c)(3), I.R.C. 1954. *St. Louis Union Trust Co. v. United States,* 374 F.2d 427 (8th Cir. 1967), and *Dulles v. Johnson,* 273 F.2d 362 (2d Cir. 1959), followed.

Counsel

Bart A. Brown, Jr. and *Ronald D. Aucutt,* for the petitioner. *Carolyn A. Boyer,* for the respondent.

OPINION

Fay,*Judge*:

Respondent determined petitioner does not qualify for exemption from Federal income tax as an organization described in section 501(c)(3). [1] Having exhausted its administrative remedies within the Internal Revenue Service

as required by section 7428(b)(2), petitioner has timely invoked the jurisdiction of this Court for declaratory judgment pursuant to section 7428(a). The issue is whether petitioner is operated exclusively for exempt purposes within the meaning of section 501(c)(3).

This case was submitted for decision on the stipulated [pg. 922] administrative record under Rule 122, Tax Court Rules of Practice and Procedure. The evidentiary facts and representations contained in the administrative record are assumed to be true for purposes of this proceeding.

Petitioner, the KentuckyBarFoundation, had its principal office in Frankfort, Ky., when its petition was filed.

Since 1934, all persons licensed to practice law in Kentucky have been required to be members of the Kentucky Bar Association, otherwise known as an integrated bar association. Under the constitution of Kentucky, the Kentucky Supreme Court is empowered to control and administer the law in the Commonwealth of Kentucky, including the right to practice law, and the rules, regulations, and membership of the Kentucky Bar Association (the bar association). [2] The board of governors of the bar association is the delegate of the Kentucky Supreme Court for the purpose of administering and enforcing the rules. [3]

Petitioner, the KentuckyBarFoundation, is a nonstock, nonprofit organization incorporated on May 28, 1958, under the laws of the Commonwealth of Kentucky. Under petitioner's articles of incorporation, its stated purpose is to foster, promote, and carry on certain educational, literary, scientific, and charitable purposes, both directly and by the application of assets or income for such purposes, or to the use of any other organization whose purposes and operations are exclusively charitable, scientific, literary, or educational. Since its creation in 1958, petitioner has accumulated funds until such time as an appropriate use for such funds could be found. When the increasing and expanded duties of the bar association forced it out of the limited space it occupied in the State Capitol Building, petitioner accumulated funds for the purpose of acquiring land for, and contributing to the costs of, construction of the proposed Kentucky Bar Center Headquarters (hereinafter the bar center), which would provide permanent housing for both the bar association and petitioner, a public law library, and other public areas. It is not anticipated that petitioner's funds will be used for operating expenses of [pg. 923]the bar center. From July 1, 1974, through August 31, 1979, petitioner received contributions totaling $180,012.62 and earned passive investment income of $8,479.43. In 1978 and 1979, petitioner distributed $177,988.67 to the board of trustees of the bar center to acquire land to be used in constructing the bar center. [4]

On October 10, 1979, petitioner filed an application for recognition of exemption under section 501(c)(3). On May 22, 1980, respondent issued a final adverse determination and denied petitioner's exempt status on the ground

petitioner was not operated exclusively for exempt purposes within the meaning of section 501(c)(3).

The issue is whether petitioner is operated "exclusively" for exempt purposes, or whether, as respondent contends, petitioner serves a "substantial nonexempt purpose" by promoting the interest and reputation of the legal profession.

An organization may qualify for exemption from Federal income tax under sections 501(a) and 501(c)(3) if it is operated exclusively for one or more of the exempt purposes enumerated in section 501(c)(3). For this purpose, "exclusively" is given a connotation different from its ordinary meaning. It does not mean "solely" or "absolutely without exception." *Church in Boston v. Commissioner,* 71 T.C. 102, 107 (1978). Thus an organization will not be denied exemption if it partakes in activities not in furtherance of an exempt purpose so long as such non-conforming activities are insubstantial in comparison to activities which further exempt purpose(s). *Better Business Bureau v. United States,* 326 U.S. 279 (1945); Duffy v. Birmingham, 190 F.2d 738 (8th Cir. 1951). Similarly, where activities further both exempt and nonexempt purposes, the exemption will not be denied if the nonexempt purposes are insubstantial. *Ohio Teamsters Trust Fund v. Commissioner,* 77 T.C. 189, 196 (1981); *Professional Standards Review v. Commissioner,* 74 T.C. 240 (1980).

The proper focus is the purpose or purposes toward which the activities are directed, (*B.S.W. Group, Inc. v. Commissioner,* 70 T.C. 352 (1978)), and a mere statement of that purpose is **[pg. 924]**not determinative. Nor is a State court's determination of that purpose determinative. *Watson v. United States,* 355 F.2d 269 (3d Cir. 1965). The parties herein agree that since petitioner's principal activity is the raising of funds for the construction of the bar center, petitioner's exempt status depends on the nature of the activities to be conducted at the center. Such proposed activities include the following:

(1) a continuing legal education program,

(2) a public law library,

(3) publication of the "Kentucky Bench and Bar,"

(4) a Client Security Fund,

(5) an Inquiry Tribunal,

(6) a Fee Arbitration Plan, and

(7) a Lawyer Referral Service.

Respondent agrees that certain activities-the continuing legal education program, the public law library, and the publication of the "Kentucky Bench and Bar"-serve an exempt purpose (educational) within the meaning of section 501(c)(3). Respondent further agrees that petitioner's exempt status should be determined exclusively by an analysis of the remaining activities-the lawyer referral service, the client security fund, the inquiry tribunal, and the fee arbitration plan. Thus, in its narrowest sense, the issue before us is whether any of the four disputed activities serves such a nonexempt purpose so as to deny petitioner its requested exemption. With respect to each activity, the thrust of respondent's argument is that a substantial nonexempt purpose, namely that of promoting, protecting, and enhancing the legal profession, is served. [5] We disagree.

Lawyer Referral Service

The bar association's lawyer referral service (referral service) was established on July 1, 1977. The referral service is conducted on a statewide basis with the exception of Jefferson County (Louisville) wherein the local bar association maintains [pg. 925]its own referral service. A person seeking a lawyer may use a toll-free telephone line. He is initially interviewed by a bar association staff member and is then referred to a participating member of the referral service who is selected on a rotating basis within a convenient geographic area. An initial fee of $10 is charged for a one-half hour consultation. Any charge for further consultation or work must be agreed upon by the attorney and the client and must be in keeping with the stated objectives of the referral service. The participating attorney must also agree:

> (1) to carry certain amounts of professional liability insurance,
> (2) to permit any fee dispute arising from a referral to be submitted to binding arbitration under the Fee Arbitration Plan,
> (3) to grant all clients referred an appointment as soon as practicable after request is made, and
> (4) to abide by all rules of the Referral Service regarding registration, qualification to practice law, and investigation into the responsibility, capability, character and integrity of the attorney.

Each participating member of the referral service must pay a fee to the association to be used to defray the costs of operating the service. At the time its petition was filed herein, the fee was $25 per year. The referral service is operated from the office of the director of the bar association.

The preamble to the rules governing the referral service states:

> The Kentucky Bar Association recognizes that there exists a large group of persons of moderate means who have felt that legal services were not readily available. In order to respond to the needs of those persons, it is the position of the Kentucky Bar Association that a lawyer referral service be established.

The stated long-term objectives of the referral service are:

> 1. to assist the general public by providing a way in which any person who can afford to pay a reasonable fee for legal services may be informed of and referred to a member of the Kentucky Bar.
> 2. encourage lawyers to recognize the obligation to provide legal services to the general public, and
> 3. to acquaint people in need of legal services with the value of consultation with a lawyer to identify legal problems and seek to solve them.

We find the operation of the referral service is consistent with the preamble and its stated objectives. It serves a genuinely charitable purpose. [pg. 926]

We find substantial support in the Circuit Court of Appeals decisions of *St. Louis Union Trust Co. v. United States,* 374 F.2d 427 (8th Cir. 1967) and *Dulles v. Johnson,* 273 F.2d 362 (2d Cir. 1959), cert. denied 364 U.S. 834

(1960), wherein bar associations which operated legal referral services were held to be organizations operated exclusively for charitable purposes within the meaning of sections 2055(a) and 812(d), IRC 1939 (predecessor to sec. 2055(a)), respectively. Respondent contends the decisions in *St. Louis Union Trust* and *Dulles* incorrectly understate the benefits inuring to the legal profession and to the individual members of the profession. [6] However, we agree with the statement of the Eighth Circuit Court of Appeals:

> the government overemphasizes the incidental economic benefits and unjustifiably would taint with an accusation of commercialism legal activity which is dedicated to the public good. [*St. Louis Union Trust Co. v. United States, supra,* at 435.]

We reject respondent's assertion that the referral service exists to help young law school graduates establish a practice. The referral service is open to all responsible attorneys, and there is no evidence a selected group of attorneys are the primary beneficiaries of the service. The referral service is intended to benefit the public and not to serve as a source of referrals. We find any nonexempt purpose served by the referral service and any occasional economic benefit flowing to individual attorneys through a referral incidental to the broad charitable purpose served.

Client Security Fund

On October 20, 1971, the client security fund was established by the bar association and approved by order of the Court of Appeals (now the Supreme Court of Kentucky) for the purpose of providing indemnification to clients who suffer pecuniary losses by reason of fraudulent or other dishonest acts by any [pg. 927]member of the association acting in his or her capacity as an attorney. [7] The fund is maintained in a separate account by three trustees appointed by the board of governors of the bar association. It is funded from a portion of the dues paid by bar association members, contributions, and investment income. Claims may be made against the fund for wrongful acts, except negligent acts of malpractice, committed by practicing attorneys against their clients. Claims are recognized only to the extent they are not otherwise recoverable under any insurance, indemnity, or bond arrangement. All payments from the fund are a matter of grace, subject to the discretionary approval of the board of governors of the bar association.

The public must often deal on faith in its relationship with lawyers. As the Second Circuit Court of Appeals stated,

"It is the function of bar associations to see that this faith is not misplaced

*** the true benefit from a disciplined and socially responsive bar accrues directly to the public." *Dulles v. Johnson, supra,* at 366. The client security fund provides protection to the public in the form of indemnification to clients who suffer at the hands of fraudulent and dishonest members of the bar association. It is a means by which the Bar Association fulfills its responsibility to the public. Moreover, no individual attorney stands to derive any direct economic benefit from the administration of this plan. We find any favorable effect the plan has on the image of the legal profession is merely an incidental consequence of its basic charitable nature.

Inquiry Tribunal

Section 116 of the Kentucky Constitution specifically delegates the responsibility of policing unauthorized and unethical actions of bar association members to the Kentucky Supreme Court. [8] The Kentucky Supreme Court has further delegated many of its responsibilities to the board of governors of the bar [pg. 928]association (the board), to the director of the bar association, and to the inquiry tribunal. [9] The board is responsible for determining the merits of a charge of breach of ethics by any member of the bar association, while the principal role of the inquiry tribunal is to determine whether a formal charge should be filed against the attorney. [10] Thus, the inquiry tribunal is an integral part of the bar association's disciplinary functions.

Again, respondent urges us to find a substantial nonexempt purpose is served via promotion of the legal profession through the association's disciplinary functions. Respondent maintains both the Eighth and Second Circuit Courts of Appeals in *St. Louis Union Trust Co. v. United States, supra,* and *Dulles v. Johnson, supra,* understated the public esteem the legal profession derives from its disciplinary functions. We disagree and adopt the reasoning of the Circuit Courts. As the Eighth Circuit Court of Appeals stated:

> this activity as to *** internal discipline is one primarily and substantially imbued and indeed infected with a public purpose. Of course, a profession's image and its relations with the public will be enhanced when it demonstrates ethics, effective discipline, and the protection of the public from invasion externally by incompetent and illtrained persons and from imposition internally by the rascals of the profession. But this is an incident and a result rather than a basic characteristic of the endeavor. [*St. Louis Union Trust Co. v. United States,* 374 F.2d at 436.]

We see no meaningful differences in the activities and purposes behind the disciplinary operations of the bar associations involved in *St. Louis Union Trust* and *Dulles* and the disciplinary functions conducted by the Kentucky Bar Association herein. Clearly, the functions of an integrated State bar association which pertain to the maintenance of high standards of conduct and ethics have a direct public benefit. Enforcement of those high standards is necessary to assure public confidence in the legal system. We find the activities of the inquiry tribunal do not defeat petitioner's exempt status. [pg. 929]

Fee Arbitration Plan

On September 20, 1975, the bar association adopted a fee arbitration plan in order to establish a procedure whereby fee disputes between an attorney and a client may be resolved by submission to binding arbitration. A three-member panel listens to the dispute. Members of the panel are not compensated for their services. Other than stenographic charges, no charge or fee is required of any party making use of the arbitration services. The panel renders a written decision with a statement of the dispute and the panel's findings. Since the inception of the fee arbitration plan in 1975, only 27 cases have arisen under the plan. The major use made of the center with respect to the fee arbitration plan is to provide a limited amount of staff support to the assistant director of the bar association who is responsible for transmitting certain documents and maintaining records of disputes.

The fee arbitration plan was adopted to provide a means of resolving disputes arising out of the lawyer-client relationship. Any client can avail himself of this procedure at no cost, excepting stenographic expenses. The plan relieves the judicial branch of Government of the burden of resolving those disputes. Thus, the plan clearly serves a charitable purpose. See  sec. 1.501(c)(3)-1(d)(2), Income Tax Regs.

We reject respondent's contention that the fee arbitration plan serves a substantial noncharitable purpose by providing a low-cost, low-profile method for collecting disputed fees. The infrequent use of the procedure does not bear out respondent's contention. Only 27 cases have arisen under the plan since its inception in 1975. Respondent infers a much too narrow purpose is served by the plan. We find any intangible benefit accruing to the legal profession is only incidental to the charitable purpose served by the fee arbitration plan.

Moreover, the administration of the fee arbitration plan constitutes a minor activity at the bar center. With respect to the available procedure, the bar center is involved to a very limited extent-it lends staff support in the nature of transmitting documents and maintaining records and is only minimally involved in the proceedings. Less than one percent of the assistant director's time is devoted to the plan. Even if the fee arbitration plan were held

to be a nonexempt purpose, the activities conducted at the center with respect to the plan [pg. 930]constitute an insignificant part of the plan itself and a very small portion of all the activities conducted at the center. Thus, in any event, the activities conducted at the center with respect to the fee arbitration plan do not preclude petitioner's exempt status. See *Better Business Bureau v. United States,* 326 U.S. 279 (1945).

In summary, respondent presumes each activity is motivated by the self-interest of the legal profession and its individual members. In each instance, the thrust of respondent's argument is that, through the promotion and enhancement of the legal profession, the activities conducted at the center serve a substantial noncharitable purpose. In each instance, we have found to the contrary.

Petitioner is a nonprofit organization-it has no earnings which benefit individual members of the bar association. None of the activities are connected with political or legislative causes. Instead, each of the activities involved herein is a result of the responsibility of the bar association, as a delegate of the Kentucky Supreme Court, to maintain public confidence in the legal system-a goal of unquestionable importance in a civil and complex society. The activities at issue are devoted to that goal through various means of improving the administration of justice. Respondent discounts the truly beneficial and charitable nature of these activities. As set forth above, any private or nonexempt purpose resulting from these efforts clearly is insignificant and tenuous. Accordingly, we find petitioner is operated exclusively for exempt purposes and is entitled to section 501(c)(3) exemption.

To reflect the foregoing,

An appropriate decision will be entered.

[1] Unless otherwise provided, all section references are to the Internal Revenue Code of 1954 as amended.

[2] Ky. Const. sec. 116.

[3] Ky. Sup. Ct. rule 3.070.

[4] The board of trustees of the center was created and authorized by the Kentucky Supreme Court to act with respect to all matters relating to the ownership, management, and control of the bar center. Ky. Sup. Ct. Rules

3.115(1), 3.115(2) and 3.115(2)(g).

[5] Since the lawyer referral service, client security fund, and fee arbitration plan do not fit neatly within any of the enumerated categories of charitable activity set forth in sec. 1.501(c)(3)-1(d)(2), Income Tax Regs., respondent argues those activities are not charitable activities within the meaning of sec. 501(c)(3). Respondent's argument must be rejected. The concept of "charity" clearly is not limited to those enumerated activities but is to be used in its generally accepted legal sense. Sec. 1.501(c)(3)-1(d)(2), Income Tax Regs.

[6] Respondent's position is illustrated in Rev. Rul. 80-287, 1980-2 C.B. 186, and Rev. Rul. 71-505, 1971-2 C.B. 232.

[7] We emphasize that, being an integrated bar association, every attorney licensed to practice in Kentucky is a member of the bar association.

[8] The Kentucky Supreme Court has adopted the standards embodied in the American Bar Association's Code of Professional Responsibility.

[9] Ky. Sup. Ct. rules 3.140 et seq.

[10] The director's role is primarily administrative.

Revenue Rulings

Rev. Rul. 81-276, 1981-2 CB 128, IRC Sec(s). 501

Headnote:

Rev. Rul. 81-276, 1981-2 CB 128 -- IRC Sec. 501 (Also Sections 170, 509; 1.170A-9, 1.509(a)-2.)

Reference(s): Code Sec. 501; Reg § 1.501(c)(3)-1

Professional standards review organization (PSRO).

An organization was established to perform the services of a professional standards review organization (PSRO) pursuant to section 249F of the Social Security Amendments of 1972, and was designated as a PSRO for a particular area by the Department of Health and Human Services (HHS). It derives all of its support from contracts with HHS that provide for payment for all reasonable and necessary expenses incurred by it in the performance of its functions. The organization qualifies for exemption under section 501(c)(3) of the Code and is not a private foundation under section 509(a) because it is described in section 170(b)(1)(A)(vi). Rev. Rul. 74-553 distinguished.

Full Text:

ISSUES

(1) Does the professional standards review organization described below qualify for exemption from federal income tax under section 501(c)(3) of the Internal Revenue Code?

(2) If the organization is described in section 501(c)(3) of the Code, is it also described in section 170(b)(1)(A)(vi) and thus not a private foundation within the meaning of section 509(a)?

FACTS

The nonprofit organization, *M,* which otherwise qualfies for exemption under section 501(c)(3) of the Code, was formed to establish and perform the services of a professional standards review organization (PSRO) pursuant to section 249F of the Social Security Amendments of 1972, 42 U.S.C. section 1320c *et seq.* (1974). *M* has been designated as a PSRO for a particular area by the Department of Health and Human Services (HHS), and satisfies the requirements for such designation set out in 42 U.S.C. section 1320c *et seq.* (1974) and the regulations thereunder. *M* has engaged solely in activities designed to further the purposes of this statute.

M's principal activity is the review of the professional activities of physicians and other health care practitioners, and institutional and non-institutional providers of health care services, in the provision of health care services and items for which payment is made under medicare and medicaid. In conducting this review, *M* develops and applies professional norms of care, diagnosis, and treatment and determines whether:

(A) the health care services and items are or were medically necessary;

(B) the quality of such services meets professionally recognized standards of health care; and

(C) in case such services are proposed to be provided in a hospital or other health care facility on an inpatient basis, whether such services and items could, consistent with the provision of appropriate medical care, be effectively provided on an outpatient basis or more economically in an inpatient health

care facility of a different type.

Generally, no payments for health care services or items can be made under medicaid or medicare unless such services or items are reviewed and approved by *M.*

M's membership is open without charge to all licensed physicians engaged in the active practice of medicine, surgery, or osteopathy in *M*'s designated area. The composition of *M*'s board of directors is not tied to any membership or association in any medical society.

M derives all of its income from contracts with HHS, which provides for the payment of all reasonable and necessary expenses incurred by *M* in carrying out its functions.

LAW AND ANALYSIS-Issue (1)

 Section 501(c)(3) of the Code provides for the exemption from federal income tax or organizations organized and operated exclusively for charitable 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. Such term includes lessening the burdens of government.

In the general law of charity, the promotion of health is considered to be a charitable purpose. *Restatement (Second) of Trusts,* 368, 372; *Bogert, Trusts and Trustees,* 374 (rev. 2d ed. 1977); *IV Scott on Trusts* 368, 372 (3rd ed. 1967). See  Rev. Rul. 69-545, 1969-2 C.B. 117.

The legislative history of the Social Security Amendments of 1972 and the statute itself indicate that Congress' objectives in establishing PSROs were twofold. First, PSROs were intended to reduce overutilization of the health services provided under medicare and medicaid (and the impact of such overutilization on the health of the aged and poor) by assuring that payments for health care services under governmental health care programs would be made only when, and to the extent, medically necessary. *See* S. Rep. No. 92-1230, 92d Cong., 2d Sess. 254 (1972) and 42 U.S.C. section 1320c. Second, PSROs were intended to enable the medical profession to assume the government's responsibility for reviewing the appropriateness and quality of services provided

under medicare and medicaid. *See* S. Rep. No. 92- 1230 at 255-8.

By operating as a designated PSRO and restricting federal health care payments to services that are medically necessary, *M* is promoting the health of the beneficiaries of governmental health care programs by preventing unnecessary hospitalization and surgery. In addition, by assuming the government's burden of reviewing the appropriateness and quality of services provided under medicare and medicaid, *M* is lessening the burdens of government within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations.

M's activities may indirectly further the interests of the medical profession by promoting public esteem for the medical profession, and by allowing physicians to set their own standards for the review of medicare and medicaid claims and thus prevent outside regulation. However, such benefits to members of the medical profession are incidental to the benefits *M* provides in promoting health and lessening the burdens of government. *SeeVirginia Professional Standards Review Foundation v. Blumenthal,*466 F. Supp. 1164 (D.D.C. 1979) and *Professional Standards Review Organization of Queens County, Inc. v. Commissioner,*74 T.C. 240 (1980), acq. 1980-2 C.B. 2. The Service will follow these cases in like situations.

Accordingly, *M* is operated exclusively for charitable purposes and thus qualifies for exemption from federal income tax under section 501(c)(3) of the Code.

The organization in this case is distinguishable from the one described in Rev. Rul. 74-553, 1974-2 C.B. 168. Rev. Rul. 74-553 holds that a nonprofit organization formed by members of a State medical association to operate peer review boards for the primary purposes of establishing and maintaining standards for quality, <Page 130> quantity, and reasonableness of costs of medical services qualifies for exemption from tax under section 501(c)(6) of the Code but not under section 501(c)(3). Unlike the organization described in Rev Rul. 74-553, membership in *M* is open by law to all physicians without charge. Further, *M* is an organization mandated by federal statute as the exclusive method of assuring appropriate quality and utilization of care provided to medicare and medicaid patients. Also, the composition of the board of directors of *M* is not tied to any membership or association with any medical society. Finally, *M* has authority to make final decisions regarding quality and utilization of medical care for purposes of payment under the medicare and medicaid programs. *See Virginia Professional Standards Review Foundation v. Blumenthal,* at 1171.

LAW AND ANALYSIS-Issue (2)

Section 509(a) of the Code provides that the term "private foundation" does not include a section 501(c)(3) organization described in section 170(b)(1)(A)(vi).

Section 170(b)(1)(A)(vi) of the Code describes an organization that normally receives a substantial part of its support (exclusive of income received in the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501(c)(3)) from a governmental unit or from direct or indirect contributions from the general public.

Section 1.170A-9(e)(2) of the regulations provides that an organization will be treated as publicly supported for purposes of section 170(b)(1)(A)(vi) of the Code if the total amount of support it normally receives from government units equals at least 33 ⅓?percent of the total support it normally receives from all sources.

Section 1.170A-9(e)(7)(i)(a) of the regulations provides that the term "support" does not include any amounts received from the exercise or performance by an organization of its exempt purpose or function.

Section 1.170A-9(e)(8)(i) of the regulations provides that the term "support from a governmental unit" includes any amounts received from a governmental unit, including amounts received in connection with a contract entered into with a governmental unit for the performance of services, unless such amounts constitute amounts received from the exercise or performance of the organization's exempt functions as provided in section 1.170A-9(e)(7)(i)(a).

Section 1.170A-9(e)(8)(ii) of the regulations provides that any amount paid by a governmental unit to an organization is not to be treated as received from the exercise or performance of its exempt functions if the purpose of the payment is primarily to enable the organization to provide a service to the direct benefit of the public rather than to serve the direct and immediate needs of the payor.

In this case, HHS pays all reasonable and necessary expenses incurred by *M* in carrying out its functions. *See* 42 U.S.C. 1320c-17. It must be determined whether the amounts, paid to *M* by HHS, constitute payments made to serve the direct and immediate needs of the government (gross receipts) or payments made primarily to confer a direct benefit upon the general public (support from a governmental unit).

PSROs perform a function that promotes the health of the beneficiaries of governmental health care programs in the areas in which the PSROs operate. Congress has noted that the primary beneficiaries of the PSRO program

are the millions of persons dependent on medicare and medicaid for health care. *See* S. Rep. No. 92-1230 at 256. It follows that the payments made by HHS to *M* are made primarily to confer a direct benefit upon the general public. Thus, the payments constitute support from a governmental unit under section 1.170A-9(e)(8)(ii) of the regulations.

Since *M* receives all of its support in the form of support from a governmental unit, it satisfies the 33 1/3 percent public support test of section 1.170A-9(e)(2) of the regulations. Accordingly, *M* is described in section 170(b)(1)(A)(vi) of the Code and is not a private foundation within the meaning of section 509(a).

HOLDINGS

(1) The professional standards review organization described above is operated exclusively for charitable purposes and thus qualifies for exemption from federal income tax under section 501(c)(3) of the Code.

(2) The organization is not a private foundation within the meaning of section 509(a) of the Code because it is described in section 170(b)(1)(A)(vi).

APPLICATION INSTRUCTIONS

Even though an organization considers itself within the scope of this revenue ruling, it must file an application on Form 1023, Application for Recognition of Exemption, in order to be recognized by the Service as exempt under section 501(c)(3) of the Code. See sections 1.501(a)-1 and 1.508-1(a) of the regulations. In accordance with the instructions to Form 1023, the application should be filed with the District Director of Internal Revenue for the key district indicated therein.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 74-553 is distinguished.

Tax Court & Board of Tax Appeals Reported Decisions

PROFESSIONAL STANTARDS REVIEW v. COMMR., 74 TC 240, Code Sec(s) 501.

Professional Standards Review Organization Of Queens County, Inc, Petitioner v. Commissioner of Internal Revenue, Respondent

Case Information:

[pg. 240]

Code Sec(s):	501
Docket:	Docket No. 9952-77X.
Date Issued:	05/08/1980
Judge:	Opinion by WILBUR, *J.*
Disposition:	Decision for taxpayer.

HEADNOTE

1.EXEMPT ORGANIZATIONS-Organization descriptions-religious, charitable, etc., orgainzations-public purposes

distinguished from private interest. Professional Standards Review Organization was tax exempt organization. Benefit to business interests of medical profession was insubstantial and incidental to purpose of improving medical care and reducing medical costs. Congress specifically desired such organizations to provide self regulation of medical care industry.

Reference(s): 1980 P-H Fed ¶21,025(20). Code Sec. 501

Syllabus

Official Tax Court Syllabus

Petitioner was organized as a professional standards review organization authorized by the Department of Health, Education, and Welfare to establish a physician-sponsored organization responsible for certifying the medical necessity of hospital admissions, the appropriateness of the level of care, and the quality of care rendered for federally subsidized health care programs such as Medicare and Medicaid. *Held,* petitioner's principal purposes are to ensure effective and economical delivery of health care services to patients, and reduce unnecessary Federal spending on health care programs. Any benefits to the medical profession from these activities are incidental, and therefore petitioner is an exempt organization under  sec. 501(c)(3), I.R.C. 1954.

Counsel

Robert P. Borsody, for the petitioner. *James J. McGovern,* for the respondent.

Wilbur,*Judge:*

Respondent determined that petitioner does [pg. 241]not qualify for exemption from Federal income tax under section 501(c)(3). [1] Petitioner challenges respondent's determination and has invoked the jurisdiction of this Court for a declaratory judgment pursuant to section 7428. [2] The issue presented to us is whether petitioner is operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code.

FINDINGS OF FACT

The case was submitted for decision on the stipulated administrative record under Rule 122, Tax Court Rules of Practice and Procedure. The stipulated administrative record is incorporated herein by this reference. The evidentiary facts and representations [pg. 242]contained in the administrative record are assumed to be true for purposes of this proceeding.

Petitioner Professional Standards Review Organization of Queens County, Inc., is a nonprofit corporation formed under New York's Not-for-Profit Corporation Law. Petitioner's offices are located at 112-25 Queens Boulevard, Forest Hills, N.Y. Petitioner has been certified as a professional standards review organization (generally referred to as PSRO) as described in section 249F of the Social Security Amendments of 1972, 42 U.S.C. sec. 1320c (Supp. III 1973). Petitioner's application for exempt status under section 501(c)(3) dated, October 28, 1975, was filed with the Brooklyn, NY., District Office of the Internal Revenue Service. On June 30, 1977, the Internal Revenue Service issued a final adverse ruling that petitioner is not an organization described in section 501(c)(3).

Petitioner, as a PSRO, is authorized by the Department of Health, Education, and Welfare (HEW) to establish a physician-sponsored organization in its geographic area that will be responsible for certifying the medical necessity of hospital admissions, the appropriateness of the level of care, and the quality of care rendered for all federally subsidized patient care-Medicare, Medicaid and maternal and child health programs.

As stated in the certificate of incorporation:

> The purposes for which [petitioner] is to be formed are to promote effective, efficient and economical delivery of health care services of appropriate high quality in recognition of the interests of patients, the public, practitioners and providers in improved health care services with due consideration to cost control, treatment and quality of medical care and educational programs, and to assure through the application of suitable procedures of professional standards review that services be rendered only as and when medically necessary as determined in the exercise of reasonable limits of professional discretion and in the case of services provided by a hospital or other health care facility on an inpatient basis only when and for such period as such services cannot, consistent with professionally recognized health care standards, effectively be provided on an outpatient basis or more economically in an inpatient health care facility of a different type as determined in the exercise of reasonable limits of professional discretion all in

furtherance of the objectives sought under Public Law 92-603, Section 249F (b) (Title 42 Section 1320 C U.S.C.A. et seq.), and to function within the County of Queens, State of New York, designated as Professional Standards Review Organization Area 11 pursuant to 42 CFR, Part 101, Subpart A.

Congress authorized PSROs by statute in 1972. Generally, [pg. 243]PSROs are qualified groups of doctors that (1) establish mandatory cost and quality controls in connection with medical treatment rendered in hospitals and financed under Medicare and Medicaid and (2) monitor such care. PSROs were conceived of as part of a larger effort to curb the rising costs of health care and improve health care services. [3]

Petitioner's officers and directors are all doctors of medicine. Members of petitioner, and of all PRSOs, must be licensed practitioners of medicine or osteopathy. If doctor-sponsored program efforts do not succeed, or in the event the physicians in petitioner's PSRO area had not established a PSRO as of January 1, 1978, the Secretary of HEW would be authorized to name some other public or nonprofit agency to set standards and evaluate medical care for Queens County. On May 3, 1976, petitioner, via its interim board of directors, sent membership solicitation letters to prospective members-doctors who perform professional activities in Queens County and who are licensed to practice medicine by the State of New York. The letter generally explained the origin and function of the PSRO program, and pointed out to the prospective members that their membership in the PSRO of Queen's County (petitioner) would mean that: [pg. 244]

You will exert a direct influence on setting the standards and criteria for health care review.

Your active participation will help raise the standards of medical care in Queens County.

You will have a direct vote in selecting the leaders of your PSRO.

Enclosed in the letter was a membership questionnaire containing additional information regarding PSROs. This information dealt with subjects including how to organize a PSRO, what recourse doctors have if they oppose the PSRO proposed for their "designated area," what effect PSROs will have on doctors' fees, and how the American Medical Association supports PSROs. In answer to one question regarding benefits doctors would derive from

membership in PSROs, the questionnaire noted:

> In general, the benefits which may result from membership consist in maintaining professional input to the extent possible in the development and operation of the PSRO and the review it performs in the area, rather than leaving management of the program, after 1977, to some possibly non-professional organization or agency. As in any peer review program, the individual participating physician tends to learn as much from the review process as those reviewed.

The letter also states that the basic principles behind the PSRO program are that:

> The quality of patient care should be assured through peer review mechanisms of practicing physicians not by governmental agencies acting without the voice of representative physicians.
>
> Cost containment programs may seriously decrease quality of care if inappropriately administered, and the PSRO amendments of 1972 provide the only opportunity for the medical profession to ensure that such programs do not reduce the quality of care.
>
> Review of the need for hospital admissions, length of stay, medical procedures and patient-care quality should be performed by local physicians on the basis of explicit criteria established by local physicians.
>
> To the extent feasible, the primary functions of PSRO (admissions review, concurrent review of the need for continued care, and medical care evaluation) should be delegated to individual hospitals which are willing and able to perform them.
>
> Improvement in patient care and containment of cost should occur primarily through concurrent admission and review procedures and tailored continuing education programs, rather than through punitive actions such as those which now occur with retrospective denial of reimbursement.

Respondent denied petitioner's application for tax-exempt status under section 501(c)(3) on the ground that more than an [pg. 245]insubstantial part of petitioner's activities is not in furtherance of an exempt purpose. He stated:

> By cooperating to achieve the purposes of the statute [which established PSROs] and taking self-regulation upon themselves, the doctors who make up your organization are preventing regulation from the outside. Although your activities may be of significant benefit to the public, it is apparent that you have a purpose of protecting members of the medical profession. Thus, one significant purpose of your organization is to serve the common business interest of members of the medical profession.

In his final adverse ruling, respondent added:

> your activities also promote, to a substantial extent, the common interests of the medical profession because they minimize public criticism by assuring that physicians and other health care practitioners do not improperly utilize health care resources and facilities. ***

OPINION

Petitioner's asserted charitable purpose is to establish and perform the services of a professional standards review organization (PSRO) pursuant to the Social Security Amendments of 1972, ch. 7, tit. 2, sec. 249F(b), 86 Stat. 1430, 42 U.S.C. sec. 1320c et seq. (Supp. V 1972). The PSRO program was established by Congress in 1972 and structured to advance the important congressional policy of ensuring the effective, efficient, and economical delivery of health care services to Medicare and Medicaid beneficiaries. The program was enacted in response to mounting criticism of the method of reviewing the utilization of medical services under Medicare. The Senate Finance Committee summarized the problem as follows:

> The committee has found that present utilization review requirements and activities are not adequate.

Under present law, utilization review by physician staff committees in hospitals and extended care facilities and claims review by medicare carriers and intermediaries are required. These processes have a number of inherent defects. Review activities are not coordinated between medicare and medicaid. Present processes do not provide for an integrated review of all covered institutional and noninstitutional services which a beneficiary may receive. The reviews are not based upon adequately and professionally developed norms of care. *Additionally, there is insufficient professional participation in, and support of, claims review by carriers and intermediaries and consequently there is only limited acceptance of their review activities.* With respect to the quality of care provided, only institutional services are subject to quality control under medicare, and then only indirectly through the application of conditions of participation.

[pg. 246]

*** The detailed information which the committee has collected and developed as well as internal reports of the Social Security Administration indicate clearly that utilization review activities have, generally speaking, been of a token nature and ineffective as a curb to unnecessary use of institutional care and services. Utilization review in medicare can be characterized as more form than substance. ***

*** Apart from the problems experienced in connection with their determinations of "reasonable" charges, the performance of the carriers responsible for payment for physicians' services under medicare has also varied widely in terms of evaluating the medical necessity and appropriateness of such services. Moreover, ever since medicare began, physicians have expressed resentment that their medical determinations are challenged by insurance company personnel. The committee has concluded that the present system of assuring proper utilization of institutional and physicians' services is basically inadequate. The blame must be shared between failings in the statutory requirements and the willingness and capacity of those responsible for implementing what is required by present law.

[S. Rept. 92-1230, to accompany H.R. 1, (Pub. L. 92-603), 92 Cong., 2d Sess. 255 (1972). Emphasis added.]

Accordingly, Congress authorized the establishment of independent review organizations (PSROs) by means of which practicing physicians would assume responsibility for reviewing the appropriateness and quality of the service provided under Medicare and Medicaid.

The sole issue for our consideration is whether petitioner is operated "exclusively" for charitable purposes, or whether, as respondent contends, petitioner serves a "more than insubstantial" noncharitable purpose, namely, promoting the interest and reputation of physicians. [4]

Section 501(a) provides exemption from Federal income tax for an organization organized and operated exclusively for charitable or educational purposes. The burden of proof is on petitioner to overcome the grounds for denial of the exemption set forth in respondent's notice of determination. Rule 217(c)(2)(i) Tax Court Rules of Practice and Procedure.

Petitioner contends that its activities serve the charitable purposes of promoting community health and lessening the [pg. 247]burdens of Government and asserts that any benefits to the medical profession by virtue of its activities are incidental and a natural corollary of performing its exempt functions.

Respondent, citing *Better Business Bureau v. United States,* 326 U.S. 279 (1945), *Baltimore Regional Joint Board Health and Welfare Fund, Amalgamated Clothing & Textile Workers Union v. Commissioner,* 69 T.C. 554 (1978), and similar cases, argues that petitioner serves not only the interests of patients and the public in general but also the interests of medical practitioners and providers.

Better Business Bureau v. United States, supra, held that an organization cannot meet the section 501(c)(3) exclusivity test if it has any "important" nonexempt purpose. Similarly, section 1.501(c)(3)-1(c)(1), Income Tax Regs., provides that an organization will not be regarded as operated for one or more exempt purposes "*if more than an insubstantial part* of its activities is not in furtherance of an exempt purpose." (Emphasis added.)

Respondent suggests that petitioner serves several substantial non-exempt purposes including promoting public esteem for the medical profession by lessening public criticism and allowing physicians to set their own standards for the profession, thus preventing outside regulation. Respondent points specifically to petitioner's statements in the membership-solicitation letter sent to doctors in Queens County.

Petitioner cites the recent District Court case of *Virginia Professional Standards Review Foundation v. Blumenthal,*

466 F. Supp. 1164 (D. D.C. 1979), appeal dismissed No. 79-1501 (D.C. Cir., Aug. 13, 1979), which accorded tax-exempt status to a PSRO. On facts essentially the same as those before us therein, the Court, in a thorough and carefully written opinion, squarely rejected the arguments respondent makes herein.

Petitioner also relies on the legislative history relating to the establishment of PSROs to show, generally, that Congress believed the Federal Government to be "ill-equipped to assume adequate utilization review," and that Congress deemed it "preferable and appropriate that organizations of professionals undertake review of members of their profession rather than for Government to assume that role," and that there are no private interests served in petitioner's performance of this service. (S. Rept. 92-1230, to accompany H.R. 1 (Pub. L. 92-603), 92d Cong., 2d Sess. 258 (1972)). [pg. 248]

A PSRO's function under Federal law is to foster the reduction of unnecessary medical care and thereby unnecessary expense in the Medicare and Medicaid programs. As the Senate Finance Committee noted:

> a significant proportion of the health services provided under medicare and medicaid are probably not medically necessary. In view of the per diem costs of hospital and nursing facility care, and the costs of medical and surgical procedures, the economic impact of this overutilization becomes extremely significant. Aside from the economic impact the committee is most concerned about the effect of overutilization on the health of the aged and the poor. Unnecessary hospitalization and unnecessary surgery are not consistent with proper health care. [S. Rept. 92-1230, *supra* at 254.]

Respondent's argument that petitioner promotes the interests of the medical profession by preventing outside regulation is without merit. We note at the outset that this "self-regulation" was specifically provided for by Congress as the most efficient and effective means of assisting the Government in controlling its costs as the largest purchaser of health care in the United States. [5]

Respondent points, in particular, to the letter which petitioner sent to prospective members, which described the "benefits" which a physician would receive as a member of the Queens County PSRO. It stated, in essence, that a physician's membership in the PSRO would minimize the possibility of outside regulation of the profession.

However, the Senate Finance Committee, in its report on the establishment of PSROs, stressed its hope that physicians would participate in the regulation of their profession via PSROs:

The Committee would stress that physicians-preferably through organizations sponsored by their local associations-should assume responsibility for the professional review activities. Medicine, as a profession, should accept the task of advising the individual physician where his pattern of practice indicates that he is overutilizing hospital or nursing home services, overtreating his patients, or performing unnecessary surgery.

It is preferable and appropriate that organizations of professionals undertake review of members of their profession rather than for Government to [pg. 249] assume that role. The inquiry of the committee into medicare and medicaid indicates that Government is ill equipped to assure adequate utilization review. Indeed, in the committee's opinion, Government should not have to review medical determinations unless the medical profession evidences an unwillingness to properly assume the task.

But, the committee does not intend any abdication of public responsibility or accountability in recommending the professional standards review organizations approach. While persuaded that comprehensive review through a unified mechanism is necessary and that it should be done through usage, wherever possible and wherever feasible, of medical organizations, the committee would not preclude other arrangements being made by the Secretary where medical organizations are unwilling or unable to assume the required work or where such organizations function not as an effective professional effort to assure proper utilization and quality of care but rather as a token buffer designed to create an illusion of professional concern.

[S. Rept. 92-1230, *supra* at 258. Emphasis added.]

Read in light of the committee's statement, petitioner's membership solicitation letters appear to us primarily to be encouragement to physicians to participate and not appeals based on any private purposes of the organization. Petitioner's activities of lessening the burdens of the Federal Government and promoting public health far outweigh any incidental benefit that individual physicians, or even the profession as a whole, would derive from petitioner's purposes and activities. *Virginia Professional Standards Review Foundation v. Blumenthal,* 466 F. Supp. 1164 (D. D.C. 1979), appeal dismissed No. 79-1501 (D.C. Cir., Aug. 13, 1979). See also

H. Rept. 1860, 75th Cong., 3d Sess. 19 (1939), 1939-1 C.B. (Part 2) 728.

Thus, petitioner has followed the mandate of the Federal Government by voluntarily forming the review organization necessary for the Government to make its Medicare and Medicaid programs cost-effective. In addition, petitioner directly benefits members of the local community who are eligible for benefits under the Medicare and Medicaid programs by improving the quality of health care they receive, and this was also an important goal of Congress in establishing PSROs.

In sum, respondent's claim that petitioner and other PSROs were formed to promote the "interests" of the medical profession is spurious and without foundation. In fact, the PSRO concept was opposed by many in the medical profession, both during the hearings on the 1972 Social Security Amendments and after their enactment. Hearings on H.R. 1 Before the Senate Comm. on Finance, 92d Cong., 2d Sess. 3242, 3252 (1972). [pg. 250]Statement of the Association of American Physicians and Surgeons, *supra* at 2651. See also *Association of American Physicians & Surgeons v. Mathews,* 423 U.S. 975 (1975).

Respondent also contends that petitioner's activities will minimize public criticism and thereby further the "common interests" of the medical profession. On this basis, respondent has characterized petitioner as a professional association under section 501(c)(6) dealing with business leagues. [6]

But, as we have stated and again emphasize for respondent's benefit, petitioner, as a PSRO, is authorized pursuant to Federal law to perform a quasi-governmental function:

> the Government has a responsibility to establish mechanisms capable of assuring effective utilization review. Its responsibility is to the millions of persons dependent upon medicare and medicaid, to the taxpayers who bear the burden of billions of dollars in annual program costs, and to the health care system.
>
> In light of the shortcomings outlined above, the committee believes that the critically important utilization review process must be restructured and made more effective through substantially increased professional participation.
>
> The committee believes that the review process should be based upon the premise that only physicians are, in general, qualified to judge whether services ordered by other physicians are

necessary. *** [S. Rept. 92-1230, to accompany H.R. 1 (Pub. L. 92-603), 92d Cong., 2d Sess. 256, (1972).]

Petitioner, mandated by law, is reviewing the utilization of Government-subsidized programs. This activity does not cast it in the realm of a section 501(c)(6) "business league."[7] For these reasons, the precedents relied upon by respondent dealing with professional organizations properly classified as business leagues are inapposite.

Finally, respondent seems to argue that Congress' failure to explicitly classify PSROs as charitable organizations implies some congressional policy in opposition to granting tax-exempt status to PSROs. The most we can say about the absence of any mention by Congress of PSRO's tax-exempt status in the [pg. 251]implementing legislation is that Congress apparently did not consider the issue.[8] However, Congress' failure to specifically address this issue at that time does not suggest to us that Congress did not regard PSROs as entitled to exemption under section 501(c)(3) and should not leave petitioner without a judicial remedy in the instant case.

In sum, we find that petitioner promotes and regulates health care services to Medicare and Medicaid beneficiaries under the Government-created PSRO program. We find that although petitioner's activities may incidentally prevent outside regulation of the medical profession, this is part and parcel of the congressional policy underlying the statute.

Decision will be entered for the petitioner.

[1] All section references are to the Internal Revenue Code of 1954, as amended, unless otherwise noted.

SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.

(a) Exemption From Taxation.-An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503. ***

(c) List of Exempt Organizations.-The following organizations are referred to in subsection (a):

*** (3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic

facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

[2] SEC. 7428. DECLARATORY JUDGMENTS RELATING TO STATUS AND CLASSIFICATION OF ORGANIZATIONS UNDER SECTION 501(c)(3), ETC.

(a) Creation of Remedy.-In a case of actual controversy involving-

(1) a determination by the Secretary-

(A) with respect to the initial qualification or continuing qualification of an organization as an organization described in section 501(c)(3) which is exempt from tax under section 501(a) or as an organization described in section 170(c)(2),

*** upon the filing of an appropriate pleading, the United States Tax Court, the United States Court of Claims, or the district court of the United States for the District of Columbia may make a declaration with respect to such initial qualification or continuing qualification

*** . Any such declaration shall have the force and effect of a decision of the Tax Court of a final judgment or decree of the district court or the Court of Claims, as the case may be, and shall be reviewable as such.

***

[3] The Senate Finance Committee summarized the necessity of the PSRO program as follows:

"According to recent estimates the costs of the medicare hospital insurance program will overrun the estimates made in 1967, by some $240 billion over a 25-year period. The monthly premium costs for part B of medicare-doctors' bills-rose from a total of $6 monthly per person on July 1, 1966, to $11.60 per person on July 1, 1972. Medicaid costs are also rising at precipitous rates.

"The rapidly increasing costs of these programs are attributable to two factors. One of these is an increase in the unit cost of services such as physicians' visits, surgical procedures, and hospital days. H.R. 1, as reported,

contains a number of desirable provisions which the committee believes should help to moderate these unit costs.

"The second factor which is responsible for the increase in the costs of the medicare and medicaid programs is an increase in the number of services provided to beneficiaries. The Committee on Finance has, for several years, focused its attention on methods of assuring proper utilization of these services. That utilization controls are particularly important was extensively revealed in hearings conducted by the subcommittee on medicare and medicaid. Witnesses testified that a significant proportion of the health services provided under medicare and medicaid are probably not medically necessary. In view of the per diem costs of hospital and nursing facility care, and the costs of medical and surgical procedures, the economic impact of this overutilization becomes extremely significant. Aside from the economic impact the committee is most concerned about the effect of over-utilization on the health of the aged and the poor. Unnecessary hospitalization and unnecessary surgery are not consistent with proper health care. [S. Rept. 92-1230, to accompany H.R. 1 (Pub. L. 92-603), 92d Cong., 2d Sess. 254 (1972).]"

[4] It is undisputed that "exclusively" does not mean "solely." "Exclusively" has been interpreted as requiring that the principal or primary activities must be charitable, and any activities not furthering a charitable purpose must be insubstantial in comparison to the charitable activities. 6 J. Mertens, Law of Federal Income Taxation, sec. 34.07, p. 31 (1975 rev.)

[5] The regulations accompanying sec. 501(c)(3) define the term "charitable" as including "lessening of the burdens of government." Sec. 1.501(c)(3)-1(d)(2), Income Tax Regs. This concept relates to the provision of governmental or municipal services, either directly, or in tandem with existing Government agencies. Clearly, Congress views PSROs as organizations acting in the public interest by improving the quality of medical care in the United States and by obtaining maximum value for every Federal health dollar expended.

[6] Sec. 1.501(c)(6)-1, Income Tax Regs., provides:

"A business league is an association of persons having some common business interest, the purpose of which is

to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade.

*** "

[7] The District Court in *Virginia Professional Standards Review Foundation v. Blumenthal,*  466 F. Supp. 1164 (D. D.C. 1979), appeal dismissed No. 79-1501 (D.C. Cir., Aug. 13, 1979), also distinguished PSROs from business leagues based on PSRO's quasi-governmental functions.

[8] Petitioner acknowledges that the House conferees rejected a section contained in the Senate version of the Medicare-Medicaid Anti-Fraud and Abuse Amendments, Pub. L. 95-142, 91 Stat. 1175 which would have granted sec. 501(c)(3) tax-exempt status to PSROs. There was no explanation for this action in the Conference Committee report. By way of explanation, Congressman Rostenkowski, Chairman of the Subcommittee on Health of the House Committee on Ways and Means, made this statement about the conferees' action:

"One issue in particular, the interrelationship of tax policy and health policy, which emerged in the Senate amendment pertaining to the tax treatment of PSROs is a broad subject area that we feel must be examined in significant detail. I have assured Senator Dole [the primary Senate sponsor of the amendment] and the other Senate conferees that the entire impact of the tax code on the financing and delivery of health care is an issue that the Ways and Means Subcommittee on Health hopes to explore during the next session. And I would even take this opportunity to solicit the views of members and others concerned about specific areas appropriate for the committee's review. [19 Cong. Rec. E 6362 (daily ed. Oct. 17, 1977).]"

Secure | https://www.consumerreports.org/cro/health/doctors-and-hospitals/what-you-dont-know-about-your-doctor-could-hurt-you/index.htm

Smart Ways to

CHOOSE A DOCTOR

Many people looking for a new doctor start by asking friends, relatives, or co-workers for recommendations. Though those suggestions may be perfectly good, you still need to do your own research. Here, the steps you should take:

1 | KNOW YOUR INSURANCE

A doctor who isn't affordable for you probably isn't Dr. Right. So contact your insurance company and get a list of approved doctors or give your insurer the name of the doctor you are considering. If you're on Medicare, use the Physician Compare tool medicare.gov/physiciancompare to see which doctors accept Medicare.

TIP Don't rely solely on your insurer's website: Doctors frequently add or drop plans, and lists may be out of date. Call the doctor's office and ask.

2 | SPOT RED FLAGS

It's not easy to get clear information about your doctor's disciplinary history. But the best place to at least start is docinfo.org, run by the Federation of State Medical Boards, an organization representing state agencies that license and discipline doctors.

TIP If your search results list anything under "Actions," click on the link, which will take you to a state's website. Once there, you will have to dig deeper to find out exactly what the doctor is on probation for. Some sites are easier to use than others, as we found in our analysis of websites in all 50 states. If you're unclear of what to do or how to interpret what you find, call your state medical board.

3 | LOOK A LITTLE DEEPER

4 | CHECK ON HOSPITAL AFFILIATION

The doctor you choose can determine which hospital you go to. Your insurance company's website and, for Medicare patients, the Physician Compare tool medicare.gov/physiciancompare should list the doctor's hospital affiliations.

TIP For national results, use Consumer Reports' hospital Ratings to compare medical centers in your area.

5 | FOLLOW THE CONNECTIONS

The government now collects information on how much money doctors get from drug and medical device companies. Such payments can be legit, but a physician who receives large payments may be unduly influenced by industry. ProPublica posts that type of payment information.

TIP Also ask the doctor's staff whether the office gets many visits from drug reps. More and more are restricting such sales calls. That's good: They not only can take up a lot of the doctors' time but also may