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Op. No. 64-6

STATE OF HAWAII  
DEPARTMENT OF THE ATTORNEY GENERAL  
HONOLULU

January 30, 1964

Honorable Edward J. Burns  
Director of Taxation  
State of Hawaii  
Honolulu, Hawaii

Attention: Mr. John A. Bell

Dear Sir:

This opinion is submitted in response to a request by Mr. Bell for advice as to whether or not Kaiser Foundation Health Plan, Inc., is exempted from the payment of Hawaii gross income taxes on its receipts derived from operation of its health plan.

We reply in the affirmative.

Kaiser Foundation Health Plan, Inc., hereinafter sometimes referred to as the "Health Plan", is a California corporation registered to do business in Hawaii and operates a nonprofit medical and hospital service program under contract with individuals and groups. Membership in the Plan is open to the public and the members pay a regular fee each month.

The Health Plan seeks an exemption on the basis of section 117-20, Revised Laws of Hawaii 1955, as amended, the pertinent portions of which provide as follows:

"§ 117-20. Exemptions, persons exempt, applications for exemption. The provisions of this chapter shall not apply to the following persons:

. . .

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(h) . . . organizations operated exclusively for the benefit of the community and for the promotion of social welfare, and from which no profit inures to the benefit of any private stockholder or individual;

. . .

The exemptions enumerated in this section from (f) to (i), both inclusive, shall apply only:

. . .

(3) to the fraternal, religious, charitable, scientific, educational, communal or social welfare activities of such persons, or to the activities of such hospitals, infirmaries and sanitariums as such, and not to any activity the primary purpose of which is to produce income even though such income is to be used for or in furtherance of the exempt activities of such persons."

Subsection (h), quoted above, is very similar to Internal Revenue Code Section 501(c)(4) which was derived from earlier code sections similarly worded and which provides for an exemption from federal income taxation of "civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare. . . ."

In interpreting the Code provisions, the United States Treasury Department has promulgated certain regulations and the pertinent portions read as follows:

"Reg. 1.501(c)(4)-1. Civic organizations . . .

(a) Civic organizations.--(1) In general. A civic leagues or organization may be exempt as an organization in section 501(c)(4) if--

- (i) It is not organized or operated for profit; and
- (ii) It is operated exclusively for the promotion of social welfare.

(2) Promotion of social welfare--  
(i) In general.--An organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements. . . ."

Under both the Hawaii statute and the Internal Revenue Code, it appears that an organization to be entitled to an exemption must satisfy two conditions: it must be (1) operated exclusively for the promotion of social welfare and (2) not organized or operated for profit. That the Health Plan is operated on a nonprofit basis appears to be sustained from the facts submitted to us. Whether the Health Plan is entitled to an exemption would, then, hinge on whether or not it is an organization operated exclusively for the promotion of social welfare.

Almost all of the cases dealing with the question of whether or not a particular organization is a "social welfare" organization merely reach a conclusion on the basis of the facts presented and do not attempt to define the phrase. In Comm. v. Lake Forest, Inc., 305 F.2d 814 (1962), however, the court construed the phrase "social welfare" to mean the well-being of persons as a community. Generally, the courts, as in the Lake Forest case, appear to give the phrase a broad and very elastic interpretation (see generally 6 Mertens, Federal Income Taxation, § 34.18 (Zimet ed. 1957)), and, further, give it a liberal interpretation in favor of the exemption. See Scotfield v Rio Farms, Inc., 205 F.2d 68 (1953).

The Internal Revenue Service has ruled that the Health Plan is entitled to an exemption from the payment of federal income taxes as a social welfare organization. The ruling to grant the exemption is not binding upon the State of Hawaii, but because our statute is patterned after the Code provisions and is substantially similar to it, the ruling is persuasive and should be considered along with all pertinent cases and rulings.

The Hawaii Medical Service Association, hereinafter sometimes referred to as the "Association", a nonprofit Organization operated for the same purpose as Kaiser Foundation Health Plan, Inc., but administered differently, has been granted an exemption from the payment of all Hawaii taxes, except the

unemployment compensation tax, as a mutual benefit society under section 185-19. It does not appear that an application for exemption under the social welfare provision was made by the Association.

The Internal Revenue Service has also ruled that the Association is entitled to an exemption from the payment of federal income taxes under the fraternal benefit society exemption provision of the Code. It is not known whether the Association ever sought an exemption under the "social welfare" provision of the Code. However, it appears to be clear that, had it not qualified for the exemption under the fraternal benefit society exemption provision, it probably would have qualified under the "social welfare" provision. This conclusion appears to be supported by Rev. Rul. 55-495, 1955-2 Cum. Bull. 259, which concerns an association which was organized for the purpose of assisting its members in time of sickness or distress, and in case of death. Membership in the association is restricted to individuals who subscribe to a designated religious creed, are of good character and health, and have the ability to earn a livelihood. The association sought an exemption as a fraternal benefit society. The Internal Revenue Service ruled that the association was not entitled to an exemption as a fraternal benefit society but that it was entitled to an exemption as a "social welfare" organization. The Internal Revenue Service so ruled despite the fact that membership in the association is restricted and not open to the public. It appears that both Kaiser Foundation Health Plan, Inc., and the Hawaii Medical Service Association present stronger cases for exemption as "social welfare" organizations than this organization.

Subparagraph (3) of section 117-20, above-quoted, does not appear to substantially affect the question of whether or not the Health Plan is entitled to an exemption inasmuch as it appears that its activities, for the purposes of its present claim for exemption, are all social welfare activities.

Applying the decisions of the courts and the rulings of the Internal Revenue Service to the facts as presented and as available to us, we conclude that Kaiser Foundation Health Plan, Inc., is an organization operated exclusively for the benefit of the community and for the promotion of social welfare and from which no profit inures to the benefit of any private stockholder or individual. The activities of the Health Plan in operating its medical service plan would appear to clearly benefit the community and promote social welfare. Medical and hospital services are made more easily available to the public at lower cost to them, having the effect of encouraging them

to seek medical assistance when needed rather than when financially able, with resultant community benefit.

On the basis of the foregoing, we are of the opinion that Kaiser Foundation Health Plan, Inc., is entitled to an exemption from the payment of Hawaii gross income taxes under section 117-20, Revised Laws of Hawaii 1955, as amended.

Very truly yours,

/s/ RALPH W. KONDO

RALPH W. KONDO  
Deputy Attorney General

APPROVED:

/s/ BERT T. KOBAYASHI

BERT T. KOBAYASHI  
Attorney General