

Unrelated trade or business; blood bank. Sale of plasma to commercial laboratories by an exempt blood bank, engaged in collecting and maintaining blood products for use by hospitals, is not unrelated trade or business where the blood bank sells either by-product plasma from which red blood cells have been removed for use by hospitals or plasma salvaged from whole blood nearing the end of its shelf life. However, sale of plasma derived from donors through plasma-pheresis or purchased from other blood banks is unrelated trade or business. Rev. Rul. 66-323 modified.

Advice has been requested whether, under the circumstances described below, a blood bank exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954 that sells blood components to commercial laboratories is engaged in unrelated trade or business within the meaning of section 513.

The blood bank collects and maintains inventories of human blood and blood products, which are furnished to hospitals for immediate patient use. As a part of its functions, the blood bank maintains records covering all donors within the geographic area it serves, and it attempts, through contacts with hospitals within or near that area, to keep records on all persons whose blood is known to contain rare antigens and antibodies.

Recent technological developments in the field of medicine have reduced the need for whole blood transfusions by perfecting techniques whereby red blood cells and other components are transfused into the patient in lieu of whole blood. Thus, an increasing amount of the whole blood collected by the blood bank is separated into components to meet the modern medical demands for red blood cell transfusion. As a result, the blood bank is left with a large supply of plasma after the removal of the red blood cells. Since only a small part of this supply of plasma is needed by the hospitals serviced by the blood bank, most of it is sold to commercial laboratories.

The blood bank also obtains plasma from donors through a procedure called plasmapheresis, in which whole blood is drawn from a donor, the red cells are separated and replaced in the donor, and plasma is collected. This plasmapheresis technique is used, primarily, to collect plasma from donors known to have rare antigens, reagents and antibodies in their plasma. The plasma obtained in this way is sold to commercial laboratories for processing into its various components, referred to in profession as plasma fractions.

A third source of plasma is the supply of whole blood that the blood bank maintains for use in the hospitals that it serves. Although the inventory of whole blood maintained by the blood bank is designed to meet the needs of the hospitals, it is impossible to predict accurately the exact amount of each type of

blood that will be needed. Whole blood has a limited shelf life. After the expiration of this period, either the blood must be discarded or the red cells must be extracted and the plasma salvaged. Thus, as unused whole blood maintained in the blood bank's inventory nears the end of its shelf life, the blood bank salvages the plasma and sells it to commercial laboratories.

Finally, the blood bank purchases some plasma from other blood banks. This plasma is not used by the blood bank itself, but is sold to commercial laboratories.

Thus, the plasma that the blood bank sells to commercial laboratories is derived from four different sources:

- (1) by-product plasma, which is what remains of whole blood after the red cells have been extracted for use;
- (2) plasmapheresed plasma drawn from donors by the blood bank;
- (3) salvage plasma, which is plasma extracted from units of whole blood which are no longer fresh enough for transfusions because their shelf life has expired; and
- (4) plasma obtained from other blood banks.

Section 511 of the Code imposes a tax on the unrelated business taxable income of organizations otherwise exempt from tax under section 501(c)(3), with certain exceptions not here pertinent.

In section 512(a)(1) of the Code, the term 'unrelated business taxable income' is defined as the gross income derived by any organization from any unrelated trade or business regularly carried on by it, less certain deductions not here applicable.

Section 513 of the Code defines the term 'unrelated trade or business' as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its exempt function.

Section 1.513-1(d)(2) of the Income Tax Regulations provides that trade or business is related to exempt purposes only where the conduct of the business activities has causal relationship to the achievement of exempt purposes (other than through the production of income); and it is 'substantially related' only if the causal relationship is a substantial one. Thus, for the conduct of trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes. Whether activities productive of gross income contribute importantly to the accomplishment of

any purpose for which an organization is granted exemption depends in each case upon the facts and circumstances involved.

Section 1.513-1(d)(4)(ii) of the regulations provides that, ordinarily, gross income from the sale of products which results from the performance of exempt functions does not constitute gross income from the conduct of unrelated trade or business if the product is sold in substantially the same state it is in on completion of the exempt functions.

None of the sales of plasma described above can be said to bear a causal relationship to the blood bank's exempt purposes. However, where the blood bank is merely disposing of products which result from the performance of its exempt functions, it will not be considered to be engaging in unrelated trade or business.

Since providing blood and blood products to hospitals for immediate patient use is one of the organization's exempt functions, its sale of by-product plasma remaining after the red blood cells are removed for use by the hospitals is not unrelated trade or business. Similarly, since the maintenance of an inventory of whole blood is one of the organization's exempt functions, its sale of plasma salvaged from blood nearing the end of its shelf life is not unrelated trade or business. This assumes, of course, that the amount of whole blood maintained in inventory is not excessive in view of the expected needs of the hospitals that the organization serves.

The sale of plasma derived by the blood bank from donors through the process of plasmapheresis, however, is unrelated trade or business. This plasma is not a product resulting from the performance of the organization's exempt functions, but is obtained for resale. Similarly, the plasma purchased from other blood banks and resold to commercial laboratories is not a result of the performance of an exempt function. The sale of this plasma also constitutes unrelated trade or business.

Rev. Rul. 66-323, 1966-2 C.B. 216, which describes a blood bank exempt under section 501(c)(3) of the Code, is modified. Rev. Rul. 66-323 suggests that all sales of blood and blood products to commercial laboratories will be unrelated trade or business. This conclusion is in error to the extent that it fails to recognize that certain sales may be of products resulting from the organization's performance of its exempt functions. As indicated above, such sales are not unrelated trade or business under section 1.513-1(d)(4)(ii) of the regulations.