THE STATE OF SOUTH CAROLINA
In The Supreme Court

RECEIVED
MAR 20 2020
S.C. SUPREME COURT

APPEAL FROM SUMTER COUNTY
Court of Common Pleas

R. Ferrell Cothran, Jr., Circuit Court Judge

Opinion No. 5636 (S.C. Ct. App. filed April 3, 2019)

Win Myat..... Petitioner,

v.

Tuomey Healthcare System..... Respondent.

PETITIONER'S RESPONSE BRIEF TO THE SOUTH CAROLINA HOSPITAL ASSOCIATION'S BRIEF IN OPPOSITION TO THE PETITION FOR CERTIORARI

William R. Padget (S.C. Bar No. 72579)
Francis "Brink" Hinson (S.C. Bar No. 74917)
FINKEL LAW FIRM LLC
1201 Main Street, Suite 1800
Post Office Box 1799
Columbia, SC 29202
(803) 765-2935
Attorneys for Petitioner Win Myat

Other Counsel of Record:

David C. Holler
126 N. Main Street
Sumter, South Carolina 29151
Attorney for Respondent Tuomey Regional Medical Center

Edward H. Bender
S.C. Hospital Association
1000 Center Point Road
Columbia, South Carolina 29210
Attorney for Amicus Curiae S.C. Hospital Association

Wm. Grayson Lambert
M. Craig Garner, Jr.
Burr & Forman LLP
Post Office Box 11390
Columbia, South Carolina 29211
Attorneys for Amicus Curiae S.C. Hospital Association

Table of Contents

TABLE OF AUTHORITIES

Cases

Statutes

Other Authorities

Regulations

Petitioner Win Myat submits this brief in response to the South Carolina Hospital Association's filing ("the Hospital Association"). The Hospital Association advocates that the Solicitation of Charitable Funds Act ("the SCFA") provides an absolute bright-line rule limiting an organization's liability based *solely* on its IRS tax-exempt status and that the organization's actual conduct (and true fitness to receive tax-exempt status) may never be considered by our courts. However, a plain reading of the SCFA, along with its corresponding public policy, fail to support a rigid interpretation because it would ignore expressed parameters of 26 U.S.C. § 501(c)(3) and invite massive taxpayer fraud.[1] Moreover, the Hospital Association's position deprives courts of necessary discretion and would produce irreconcilable results. Lastly, this Court is perfectly equipped to address unique matters, like this one, and fashion appropriate and just relief through doctrines of unclean hands and/or illegality. The Hospital Association's implicit suggestion that such equitable relief is impractical or unwarranted is wholly devoid of support.

ARGUMENT

I. The Hospital Association's Position Ignores the Distinctions in Statutory Language of the SCFA Recodified after *Lazerson*.

The SCFA contains two markedly different definitions of a "charitable organization." The general definitions section provides:

> As used in this chapter, unless a different meaning is required by the context:
>
> (1)(a) "Charitable organization" means a person, as defined in item (7):
>
> (i) **determined by the Internal Revenue Service to**

[1] The Fourth Circuit in *U.S. ex rel. Drakeford v. Tuomey*, 792 F.3d 364 (4th Cir. 2015), expressly addressed the enormity of the frauds committed by Respondent stating that "while the penalty is certainly severe, it is meant to reflect the sheer breadth of the fraud Tuomey perpetrated upon the federal government." *Id.* at 389.

> **be a tax exempt organization** pursuant to Section 501(c)(3) of the Internal Revenue Code;
>
> (ii) that is or holds itself out to be established for any benevolent, social welfare, scientific, educational, environmental, philanthropic, humane, patriotic, public health, civic, or other eleemosynary purpose, or for the benefit of law enforcement personnel, firefighters, or other persons who protect the public safety; **or**
>
> (iii) that employs a charitable appeal as the basis of solicitation or an appeal that suggests that there is a charitable purpose to a solicitation, or that solicits or obtains contributions solicited from the public for a charitable purpose.

S.C. Code Ann. § 33-56-20(1) (emphasis added). Notably, an entity does not have to be tax exempt under Section 501(c)(3) to be subject to the SCFA. An entity can simply hold themselves out to be charitable *or* employ a charitable appeal as the basis for the solicitation of funds to be subject to the Act. *See* S.C. Code Ann. § 33-56-20(1)(a)(ii) & (iii). Importantly, in the operative section of the statute governing the limitation of liability, a different definition of "charitable organization" is provided:

> [A]ny organization, institution, association, society, or corporation **which is exempt from taxation pursuant to Section 501(c)(3)** or 501(d) of Title 26 of the United States Code, as amended.

S.C. Code Ann. § 33-56-170 (emphasis added). When limiting liability, the language that the Legislature chose when recodifying the SCFA is markedly different than the general definitions section. Thereby, giving no weight or deference as to whether an organization has previously been designated by the IRS to be a 501(c)(3) or 501(d) entity. Simply put, Section 170's determining factor is not whether an organization has been determined by the IRS to be tax exempt, but whether an organization would properly qualify to be exempt from taxation pursuant to Section 501(c)(3)'s qualifications of the federal tax code.

The Hospital Association relies on *Lazerson v. Hilton Head Hospital, Inc.*, 312 S.C.

211, 439 S.E.2d 836 (1994) to suggest the IRS's determination is the sole criterion. While *Lazerson* held the SCFA cap constitutional and found it bore a close nexus to the underlying policy objectives of preserving charitable resources, the Court did *not* decide whether the varying definitions of the SCFA permit a court to determine if an organization is eligible to receive the cap on liability established by the SCFA. Such an issue was not before the Court as the statutory expansion came later that year.

Specifically, *Lazerson* was decided on January 6, 1994. Six months later the Legislature expanded and recodified the SCFA simultaneously providing these two varying definitions for "charitable organization." *See* 1994 S.C. Acts No. 461 [2] (June 29, 1994); *Whitner v. State*, 328 S.C. 1, 6, 492 S.E.2d 777, 779 (1997) ("there is a basic presumption that the legislature has knowledge of previous legislation as well as of judicial decisions construing that legislation when later statutes are enacted concerning related subjects"). Critically, one definition defers to the IRS's determination while the operative definition does not. Accordingly, interpretation of the recodified statute with two definitions is one of first impression and warrant's this Court's review.

It is well settled that the cardinal rule of statutory construction is to ascertain and effectuate the intent of the Legislature. Under the plain meaning rule, it is not the court's place to change the meaning of a clear and unambiguous statute. *Hodges v. Rainey*, 341 S.C. 79, 85, 533 S.E.2d 578, 581 (2000). When interpreting a statutory term, a court must read the statute as a whole, and sections that are part of the same statutory scheme must be construed together. *Hughes v. West Carolina Reg. Sewer Auth.*, 386 S.C. 641, 647, 689 S.E.2d 638, 641 (Ct. App. 2009). Our courts apply the canon of construction *expressio*

[2] Codified at S.C. Code § 33-56-10 *et seq.*

unius est exclusion alerius, which provides that "to express or include one thing implies the exclusion of another, or of the alternative." *Riverwoods, LLC v. County of Charleston*, 349 S.C. 378, 384, 563 S.E.2d 651, 655 (2002). It is well settled that distinct statutory language should be given different meanings. *Laird v. Nationwide Ins. Co.*, 243 S.C. 388, 393, 134 S.E.2d 206, 208 (1964) ("Clearly, the legislature, by using this differing language, recognized the distinction...."); *Hughes*, 386 S.C. at 647, 689 S.E.2d at 642 (construing different meanings to statutes with using the words "truck" and "motor truck").

By utilizing different operative language in the recodified Section 33-56-170 the Legislature has signaled that "charitable organization" is not synonymous with the definition found in Section 33-56-20. Accordingly, in construing the provisions of Section 33-56-170, a plain reading demonstrates that qualifying as a "charitable organization" eligible for protections of a cap on its liability is not dependent on whether the organization has received an IRS determination of tax-exempt status. Rather, the proper inquiry is whether the entity meets the requirements of an organization to be exempt from taxation under Section 501(c)(3). It follows that whether a party has or has not been previously determined by the IRS to be a Section 501(c)(3) or 501(d) entity is not dispositive as to whether or not it is entitled to the protections of the SCFA.

When the two definitions are read together, it is apparent that the Legislature intended not just for those organizations that have garnered tax-exempt status to be subject to the SCFA, but also those that truly advance "charitable" purposes and those that solicit funds for "charitable" purposes. *Hodges*, 341 S.C. at 88, 533 S.E.2d at 583 ("statutes dealing with the same subject matter must be reconciled, if possible, so as to render both operative"); *Jones v. State Farm Mut. Auto. Ins. Co.*, 364 S.C. 222, 230, 612 S.E.2d 719, 723 (Ct. App.

2005) ("the language must also be read in a sense which harmonizes with its subject matter and accords with its general purpose").

In construing Section 33-56-170, the precise meaning of "pursuant to Section 501(c)(3)" is critical. "[P]ursuant to" means "in compliance with." BLACK'S LAW DICTIONARY (10th Ed. 2009). Applying the ordinary meaning, the plain language requires the organization to be in compliance with Section 501(c)(3), not simply to have been approved for tax exempt status decades ago.[3] The trial court properly recognized this distinction, rejecting the notion that the IRS's tax-exempt status is all the corporation was required to show.[4]

The requirements for 501(c)(3) compliance are well established. To qualify and maintain tax exempt status, an organization must *not* permit any part of its net earnings to "inure[] to the benefit of any private shareholder or individual [....]" 26 USCA § 501(c)(3). IRS publications further explain this principle:

> **No part of an organization's net earnings may inure to the benefit of an insider.** An insider is a person who has a personal or private interest in the activities of the organization such as an officer, director, **or a key employee**. This means that an organization is prohibited from allowing its income or assets to accrue to insiders. An example of prohibited inurement would include payment of unreasonable compensation to an insider. Any amount of inurement may be grounds for loss of tax-exempt status.

IRS Pub. 4421, *Compliance Guide for 501(c)(3) Public Charities*, p. 4 (Rev. July 2014) (emphasis added); *see also*, IRS Pub. 557, *Tax-Exempt Status for Your Organization* (Rev.

---

[3] At trial, Respondent offered letters dated July 9, 1991, and July 13, 1998, to show its tax-exempt status. App. ROA II pp. 686-687.

[4] App. R p. 20 ("This Court agrees with the Plaintiff's contention that if an organization is acting in a manner inconsistent with its stated charitable purposes that would invalidate is 501(c)(3) status, this Court has the authority to not permit the organization to avail itself to the protections of the SCFA.")

Feb. 2015).

In addition to approval by the IRS, to qualify as a 501(c)(3) nonprofit, an organization: (1) must have a charitable purpose; (2) cannot permit any of its earnings or assets to inure to the benefit of a private individual; (3) cannot engage in substantial lobbying activities; and (4) cannot participate in political campaigns. Martin McWilliams, Jr., et al., *Sculpting a Nonprofit: Part II*, SOUTH CAROLINA LAWYER, March/April 1996. Failure to comply with any of these elements, which comprise the "operational test," results in the organization losing its eligibility for tax exempt status. *Church of Scientology of California v. Comm'r*, 823 F.2d 1310, 1315 (9th Cir. 1987). If an organization fails to demonstrate that it is operated exclusively for exempt purposes, then it is not eligible for 501(c)(3) status. 26 C.F.R. § 1.501(c)(3)-1(a).

Courts have held that an organization's 501(c)(3) status must be revoked or denied, "if even a small part of its income inures" to the benefit of a private shareholder or individual. *See Orange County Agr. Soc., Inc. v. C.I.R.*, 893 F.2d 529, 534 (2nd Cir. 1990); *Church of Scientology of California*, 823 F.2d at 1316. A "private shareholder or individual" is defined broadly as "having a personal and private interest in the activities of the organization." *Presbyterian and Reformed Publishing Co. v. Comm'r*, 743 F.2d 148, 153 (3rd Cir. 1984). For example, the payment of excessive salaries or the "unaccounted for diversions of an organization's resources 'by one who has complete and unfettered control can constitute inurement.'" *Arlie Foundation v. United States of America*, 826 F.Supp. 537, 550 (D.D.C. 1993). Likewise, earnings are found to inure to an individual in instances where a limited number of individuals "reap commercial benefits from the operation of the instrumentality, though they do not do so by direct acquisition or payment

over to them of its earnings." *Harding Hospital v. United States*, 505 F.2d 1068, 1072 (6th Cir. 1974).

In the present case, Petitioner's primary contention is that the federal district court's findings in *United States ex rel. Drakeford v. Tuomey Healthcare Sys., Inc.*, 976 F. Supp. 2d 776, 784 (D.S.C. 2013) aff'd., 792 F.3d 364 (4th Cir. 2015) (hereinafter "*Drakeford*") disqualify Tuomey from 501(c)(3) compliance, and thus disqualify it from the SCFA protections. Importantly, in this case the trial court nor the Court of Appeals provide any discussion as to the effect of *Drakeford* on Respondent's SCFA defense, and the Hospital Association brief does not even make mention of *Drakeford.* All fail to discuss the proverbial elephant in the room.

Drakeford conclusively established that Respondent is guilty of paying certain physicians "in excess of the fair market value for their services" in violation of the provisions of the Stark Laws and False Claims Act, and such excess payments are earnings that inured to the benefit of private individuals.[5] In sum, the organization's net earnings were used to inure to the benefit of insiders. Because of this wrongdoing, Respondent fails to meet and/or no longer meets the qualifications set forth in section 501(c)(3) to remain tax exempt, and thus is not entitled to the protections of the SCFA.

The Hospital Association ignores the distinction in the two SCFA definitions in the hopes that the Court will not examine the effect of these egregious findings by the federal court against one of the Hospital Association's members.

---

[5] The Government alleged and proved that "the compensation packages paid physicians 31% above and beyond their total net collections as independent contractors, and thus in excess of the fair market value for their services." *Drakeford* at 781. These findings are established by the doctrine of collateral estoppel, particularly issue preclusion.

Compounding this established wrongdoing, Petitioner has submitted significant evidence indicating that Respondent provided misleading and false information to the IRS in its annual Form 990 filings, even falsely claiming to the IRS that it had been victorious in the initial trial of the *Drakeford* case.[6] Even while the *Drakeford* litigation with the federal government was ongoing, Respondent was paying its CEO the following compensation in violation of section 501(c)(3)'s inurement prohibitions:

2010 $840,622
2011 $1,011,073 (including $161,003 performance bonus)
2012 $991,462 (including $173,050 performance bonus)
2013 $1,485,190 [7]

The CEO's country club dues were also part of his compensation package.[8] Again, the trial court and Court of Appeals provided no discussion as to the effect of this evidence of inurement as to Respondent's 501(c)(3) status. Such blatant evidence of 501(c)(3) noncompliance disqualifies an organization from the SCFA protections. The Hospital Association turns to a bright-line rule as a means to gloss over the egregious facts of this case.

II. Bright Line Rules Deprive Courts of Discretion and Produce Irreconcilable Results.

Bright line rules eviscerate this Court's aims and ignores the Fourth Circuit's

---

[6] *E.g.* App. R. II pp. 0613-0614 (Tuomey 30(b)(6) Transcript, Ex. 4, Form 990 for 2012, pp. 83-84). Respondent's statement flagrantly omitted the material fact that the 2010 jury had found Tuomey guilty of Stark Law violations and even stated, "[s]ubsequent to the jury verdict in favor of the System [...]," falsely claiming that Tuomey had been victorious in the 2010 trial.

[7] App. R. IV pp. 1687-1693 (March 8, 2016 Hearing Transcript pp. 62-68).

[8] *E.g.* App. R. pp. 0664-0665 (Tuomey 30(b)(6) Transcript Ex. 5, Form 990 for 2013 pp. 40-41).

decision to directly addressing Respondent's known frauds. Specifically, the Fourth Circuit stated that "while the penalty is certainly severe, it is meant to reflect the sheer breadth of the fraud Tuomey perpetrated upon the federal government."[9] With such blatant evidence of inurement in violation of section 501(c)(3) qualification, the best hope for SCFA protection is to urge the Court to rely solely on the decades-old tax status determinations made by the IRS. Our courts should not permit such a myopic standard of review.

Bright-line rules have often been rejected by our courts and for good reason. This Court has "decline[d] to set bright-line rules, as we believe the better approach is to defer to the broad discretion of our able trial courts in addressing such claims on a case-by-case basis." *In Ex Parte Brown*, 393 S.C. 214, 224, 711 S.E.2d 899, 904 (2011) (addressing attorney's fees petitions in appointed cases); *Winrose Homeowners' Ass'n, Inc. v. Hale*, 428 S.C. 563, 566, 837 S.E.2d 47, 48 (2019)("we do not draw a bright-line rule requiring the use of one method over the other" to determine if a foreclosure sale shocks the conscience*);* *Crossland v. Crossland*, 408 S.C. 443, 453, 759 S.E.2d 419, 424 (2014) ("Formulaic principles and bright-line rules will only hinder the ability of family court judges to reach an equitable result."); *Soil Remediation Co. v. Nu-Way Envtl., Inc.*, 317 S.C. 274, 275, 453 S.E.2d 253, 254 (Ct. App. 1994), aff'd, 323 S.C. 454, 476 S.E.2d 149 (1996) (rejecting a bright line application of the Uniform Arbitration Act); *Wiedemann v. Town of Hilton Head Island*, 326 S.C. 573, 580, 486 S.E.2d 263, 266 (Ct. App. 1997), aff'd in part, rev'd in part, 330 S.C. 532, 500 S.E.2d 783 (1998) (interpreting the FOIA laws "we decline to adopt a bright line test which would resolve every dispute on this issue"). As recognized by these

[9] *U.S. ex rel. Drakeford v. Tuomey*, 792 F.3d at 389.

courts, bright-line rules deprive courts of discretion to ensure that just results are reached in individual cases. The Hospital Association's position seeks to strip such discretion from our courts in the application of the SCFA.

Our courts must be afforded discretion to apply the SCFA because the reality is that the IRS rarely examines an organization's qualifications to continue to receive tax exempt treatment. *See* U.S. Government Accountability Office Report on Tax-Exempt Organizations, at p. 2 (December 2014) available at: http://www.gao.gov/assets/670/667595.pdf (detailing that the IRS examination rate for charitable entities was 0.81 percent in 2011, and declined to 0.71 percent in 2013). That amounts to only seven of every one thousand entities being examined for a determination as to whether they actually qualify to receive tax-exempt status. Even in a highly publicized situation where an allegedly charitable organization has been assessed $237,000,000 in penalties and fines for having committed a massive taxpayer fraud, the IRS never undertook any action to evaluate Respondent's 501(c)(3) status.[10]

The Hospital Association argues that the South Carolina Secretary of State has the authority under section 33-56-140 of the South Carolina Code to investigate charitable entities so courts should never examine their conduct. That statute provides that the Secretary of State may file an action to enjoin "a person is using in the solicitation or collection of contributions any device, scheme, or artifice to defraud or to obtain money or property by means of false pretense, representation, or promise. S.C. Code § 33-56-140. Yet, even after the Fourth Circuit's decision affirming the massive judgment and

[10] The trial court noted "the Court is not aware of any action taken by the IRS to revoke Tuomey's 501(c)(3) status"). App. R. p. 20.

confirming "breadth of fraud" perpetrated by Respondent there is nothing in the record indicating that the Secretary of State commenced any action or investigation into these activities. The record in this case establishes that often there is simply no one else watching.

The SCFA's language invites judicial examination to determine eligibility for SCFA protections. As stated by the trial court:

> Protections under the Charitable Funds Act are premised on an organization's eligibility as a 501(c)(3) under federal law. Unless operating exclusively for 501(c)(3) purposes, there is no longer a charitable purpose entitling that organization to the protections of the Charitable Funds Act.
>
> . . . [I]f an organization is acting in a matter inconsistent with its stated charitable purpose that would invalidate is 501(c)(3) status, this Court has the authority to not permit the organization to avail itself of the protections of the SCFA.[11]

It is paramount that our courts be empowered to determine the protections of the SCFA, because it is litigants whose rights are most seriously and individually affected by that determination.

As in this case, bright-line rules often produce irreconcilable results. For example, the federal courts have conclusively determined that Respondent violated federal antifraud laws (i.e. the False Claims Act), assessed hundreds of millions of dollars in penalties and fines, and practically insisted that the offending entity be shut down. To the contrary, the state courts have clothed the same entity with statutory protections specifically designed to protect the resources of charitable institutions that are acting for charitable purposes. These starkly different results cannot be logically reconciled, and highlights why our courts

[11] App. R p. 20 (Trial Court's Order of April 7, 2016).

should not be forced to turn a blind eye toward fraudulent and unlawful conduct in evaluating SCFA qualifications.

III. Unclean Hands And Illegality Disqualify Respondent From The Protections Of The SCFA In This Unique Case Without Implicating Any Of The Policy Considerations Advanced By The Hospital Association.

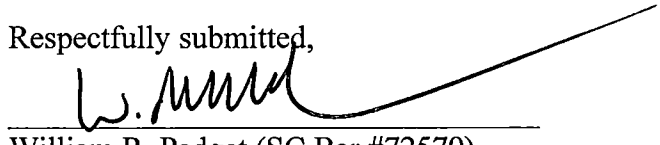
With regard to other, analogous statutory protections, our courts have denied parties the right to avail themselves of these protections where they have "unclean hands." *See In re Lafferty*, 469 B.R. 235, 245 (Bankr. D.S.C. 2012) ("This maxim illustrates the principle that the court will not grant relief to a party who has engaged in wrongful, illegal, or unethical acts."). In *Lafferty*, the bankruptcy court denied the debtors their statutory homestead exemption protections because the debtors sought to avoid a judicial lien through fraudulent and unethical conduct. 469 B.R. at 246. "The purpose of the unclean hands doctrine is to prevent a court from aiding or abetting a party in the commission of a fraud or other misconduct." *Id.* at 245-46.

As to Respondent's 501(c)(3) qualification, it is a "well-established principle that the Congressional intent in providing tax deductions and exemptions is not construed to be applicable to activities that are either illegal or contrary to public policy." *Green v. Connally*, 330 F. Supp. 1150, 1161 (D.D.C.) *aff'd sub nom.*; *Coit v. Green*, 404 U.S. 997, 92 S. Ct. 564 (1971); *see also Bob Jones Univ. v. United States*, 461 U.S. 574, 598 (1983) (refusing to permit a racially discriminatory school from claiming benefit of tax exempt status). Similarly, as a matter of sound public policy, just as articulated in *Green* and *Bob Jones*, Respondent should not be afforded the protections of tax-exempt status conferred by the SCFA.

IV. Conclusion

The guiding principle of statutory construction is to effectuate the intent of the Legislature. The Legislature never intended the SCFA to afford liability protections to an entity that has committed taxpayer fraud in violation of Section 501(c)(3)'s inurement prohibition. The SCFA's differing definitions meanings must be honored. Moreover, the Hospital Association's bright line rule would only invite massive fraud, deprive the courts of necessary discretion to ensure just results, and produce irreconcilable results. Additionally, such a rule is unwarranted when the doctrines of unclean hands and illegality provide courts with an avenue to fashion a unique remedy for this unique circumstance that does not implicate those policy considerations underlying the SCFA.

Respectfully submitted,



March 20, 2020

William R. Padget (SC Bar #72579)
Francis M. Hinson, IV (SC Bar #74917)
FINKEL LAW FIRM LLC
1201 Main Street, Suite 1800
P.O. Box 1799 (29202)
Columbia, South Carolina 29201
T: 803-765-2935
Attorneys for Petitioner Win Myat

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM SUMTER COUNTY
Court of Common Pleas

R. Ferrell Cothran, Jr., Circuit Court Judge

Opinion No. 5636 (S.C. Ct. App. filed April 3, 2019)

Win Myat.....Petitioner,

v.

Tuomey Healthcare System.....Respondent.

PROOF OF SERVICE

I certify that I have served the ***Petitioner's Response Brief to the South Carolina Hospital Association's Brief in Opposition to the Petition for Certiorari*** on the following counsel of record by depositing a copy of it in the United States Mail, postage prepaid, on March 20, 2020:

David C. Holler
126 N. Main Street
Sumter, South Carolina 29151
Attorney for Respondent Tuomey Regional Medical Center

Wm. Grayson Lambert
M. Craig Garner, Jr.
Burr & Forman LLP
Post Office Box 11390
Columbia, South Carolina 29211
Attorneys for Amicus Curiae Prisma Heath Tuomey

Edward H. Bender
S.C. Hospital Association
1000 Center Point Road
Columbia, South Carolina 29210
Attorney for Amicus Curiae S.C. Hospital Association

(Signature on next page)

William R. Padget (SC Bar #72579)
Francis M. Hinson, IV (SC Bar #74917)
FINKEL LAW FIRM LLC
1201 Main Street, Suite 1800
P.O. Box 1799 (29202)
Columbia, South Carolina 29201
T: 803-765-2935
Attorneys for Petitioner Win Myat

RECEIVED

MAR 20 2020

S.C. SUPREME COURT