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Tax-exempt hospitals: New requirements of IRC Section 501(r)

By Ann T. Hollenbeck

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Under the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, 2010 Health Legislation) tax-exempt hospitals must satisfy new requirements to maintain their tax-exempt status under Internal Revenue Code (IRC) Section 501(c)(3). For tax-exempt organizations operating more than one hospital, each hospital must satisfy these requirements separately. These new requirements are set forth in new Code Section 501(r) and described below.

Community health needs assessment

Effective for tax years beginning after March 23, 2012, tax-exempt hospitals must conduct a community health needs assessment (CHNA) once every three years, and adopt an implementation strategy to meet the community health

needs identified in the CHNA. The CHNA must include input from persons who represent broad interests of the community served by the hospital facility, including those with special knowledge or expertise in public health. Additionally, the CHNA report must be made widely available to the public.

Tax-exempt hospitals are required to complete a CHNA by the last day of their first tax year beginning after March 23, 2012. Failure to complete a CHNA in any applicable three-year period may result in a \$50,000 excise tax.

The 2010 Health Legislation also requires hospitals to provide certain related information on IRS Form 990, including: (a) a report that describes how the hospital is addressing the needs identified in the CHNA, along with a summary of needs that are not being addressed and an explanation of why; and (b) audited financial statements. The IRS will review the hospitals' community benefit activities once every three years.

IRS Notice 2011-52: General

On July 7, 2011, the IRS published Notice 2011-52,¹ which

describes anticipated regulations for the CHNA that are expected to be included in the proposed regulations under IRC Section 501(r). Hospitals that conduct CHNAs and adopt implementation strategies prior to the effective date of the CHNA requirements may rely on guidance provided under Notice 2011-52 until six months after further guidance is issued.

IRS Notice 2011-52: Anticipated regulations

The IRS provides that CHNA documentation shall be in the form of a written report, which must include the following:

- A description of the community served by the hospital and how the description was determined.
- A description of the process and methods used to conduct the assessment, including a description of the sources and dates of the data and other information used in the assessment, and the analytical methods applied to identify community health needs.
- A description of how the hospital took into account input from persons who represent broad interests of the community served by the hospital, including a description of when and how the hospital consulted with these persons. The report should also identify any organizations from which the hospital received input.
- A prioritized description of all the community health needs identified through the CHNA,

as well as a description of the process and criteria used in prioritizing such health needs.

- A description of the existing health care facilities and other resources within the community available to meet the health needs identified in the CHNA.

How and when a CHNA is conducted

The IRS provides that a CHNA is “conducted” in the tax year that the written report is made widely available to the public. The IRS also provides that a hospital satisfies the requirements only if a CHNA identifies and assesses the health needs of, and takes into account, input from persons who represent the broad interests of the community served by the hospital. To satisfy these requirements, the IRS will allow a hospital to base a CHNA on information collected by other organizations, such as a public health agency.

Community served by a hospital

The IRS provides that a hospital may take into account all relevant facts and circumstances in defining the community it serves; however, the IRS expects that such definition will include a geographic location. The IRS also provides that the hospital’s community may not be defined in a manner that circumvents the requirement to assess the health needs of the community actually served by the hospital.

Persons representing the broad interests of the community

A CHNA must, at a minimum, take into account input and information from: (1) persons with special knowledge of or expertise in public health; (2) federal, tribal, regional, state, or local health agencies; and (3) leaders, representatives or members of medically underserved, low-income, and minority populations and populations with chronic disease needs in the community served by the hospital. Additionally, a hospital may also consult with other persons located in or serving the community, such as a health care consumer advocate, nonprofit organization, or academic expert.

Making the CHNA widely available

A CHNA can be made “widely available to the public” when the written report is posted on the hospital’s website or when posted on the website of the organization that owns the hospital. However, in order to comply with this requirement:

1. the website must clearly inform readers that the CHNA is available online and provide instructions for downloading the CHNA document;
2. the CHNA document is posted in a format that will produce the exact image of the hospital’s written report when accessed, downloaded, viewed, and printed in hard copy;

3. any individual with access to the Internet can download, view, and print the CHNA document without the use of special hardware or software and without paying a fee to the hospital; and
4. the hospital provides any individual requesting a copy of the written report with the direct website address where the CHNA document can be accessed.

Demonstrate an implementation strategy

The IRS defines a hospital’s “implementation strategy” as a written plan that addresses each of the community health needs identified through the CHNA. Compliance with this requirement is accomplished by either: (1) describing how the hospital plans to meet the health need; or (2) identifying such need as one that the hospital does not intend to meet, and explaining why the hospital does not intend to or cannot meet the need. The IRS will consider the CHNA implementation strategy as “being adopted” when such strategy is approved by the hospital’s authorized governing body.

Reporting requirements

On Schedule H of the Form 990, a hospital must provide: (1) a description of how it is addressing the needs identified in the CHNA; and (2) a description of any needs not being addressed, along with an

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explanation why such needs are not being addressed. The hospital must also attach the CHNA implementation strategy to its Form 990. If the hospital only conducts one CHNA and adopts one implementation strategy in a given three-year period, the IRS will allow the hospital to attach the same implementation strategy to the Form 990 for each of those three years.

Requirements of IRS to Congress

The IRS is required to conduct a review of each tax-exempt hospital's community benefit activities at least once every three years. These reviews will be based largely on the data reported on the IRS

Form 990 and the community needs assessment prepared by each hospital. These reviews have reportedly begun and are not considered audits by the IRS. The IRS does not intend to contact each hospital undergoing a review, and the IRS will not notify the subject hospital that a review has commenced.² Additionally, an annual aggregate hospital data report is required to be submitted by the IRS to Congress, as well as a trend report every five years.

Financial assistance policy

Effective for tax years beginning after March 23, 2010, each tax-exempt hospital must adopt and

make widely available a written financial assistance policy that contains the following two key components.

First, it must incorporate (a) eligibility criteria for financial assistance and whether such assistance includes free or discounted care; (b) the basis for calculating amounts charged to patients; (c) the method for applying for financial assistance; (d) for hospitals that do not have a separate billing and collections policy, a statement of the collection-related actions the hospital may take in connection with non-payment; and (e) how the hospital will



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widely publicize the policy within the community it serves.

Second, it must commit the hospital to provide non-discriminatory emergency medical care, regardless of whether an individual is eligible for financial assistance under the hospital's financial assistance policy. (It is not clear how this changes a hospital's EMTALA obligations or how this affects a tax-exempt hospital that does not operate an emergency room.)

Limitations on patient charges

Effective for tax years beginning after March 23, 2010, tax-exempt hospitals must limit the charges for emergency or other medically necessary care provided to individuals eligible for assistance under the hospitals' financial assistance policy to not more than the amounts generally billed to individuals who have insurance covering such care. Additionally, hospitals must prohibit the use of "gross charges" when billing individuals who qualify for financial assistance. Although the 2010 Health Legislation does not define "gross charge," the term generally means the full cost that a hospital charges without applying the discount negotiated with insurance providers.

Much debate and controversy has surrounded this question. Senate Finance Committee ranking member Chuck Grassley (R-Iowa) made his opinion clear in remarks

to BNA: "The starting point for what these individuals should pay is what those with insurance pay...I'm concerned that some tax-exempt hospitals and their lawyers are spending too much time figuring out how to charge aid-qualified patients the maximum, not the minimum, contrary to congressional intent."³ The American Hospital Association (AHA) and other groups have argued that exempt hospitals should be able to apply their financial assistance policies to "chargemaster rates" so long as no aid-eligible patient pays more than the lowest commercial insurance rate or what Medicare pays. Patient advocates, however, believe that Congress clearly intended tax-exempt hospitals to calculate charges starting with rates that are already adjusted.

Billing and collection requirements

Effective for tax years beginning after March 23, 2010, the 2010 Health Legislation prohibits hospitals from taking extraordinary collection actions before making reasonable efforts to determine whether individuals are eligible for assistance under the hospitals' financial assistance policies. "Extraordinary collection actions" include lawsuits, liens on residences, arrests, or other similar collection practices. The definition of "reasonable efforts" will be determined by subsequent regulation, although it presumably would include notification to patients of

the written financial policy upon admission, in billing statements, and by follow-up telephone calls.

Conclusion

Immediate attention to the new requirements of Code Section 501(r) is imperative. Tax-exempt hospitals should evaluate their existing policies regarding financial assistance, patient charges and billing and collections to ensure compliance with the new standards. Further, tax-exempt hospitals should begin their efforts to analyze their community's needs and plan for the preparation of a formal community health needs assessment. ■

This outline provides only general information and is not legal or tax advice for any particular circumstance. IRS Circular 230 Disclosure: To ensure compliance with requirements imposed by the Internal Revenue Service, we inform you that any U.S. federal tax advice contained in this communication was not intended or written to be used, and cannot be used, by any person for the purpose of (i) avoiding tax-related penalties or (ii) promoting, marketing or recommending to another person any transaction or matter addressed in this communication.

1. To read Notice 2011-52 in its entirety, go to: <http://www.irs.gov/pub/irs-drop/n-11-52.pdf>
2. Bureau of National Affairs, Inc: BNA Health Care Daily Report, April 8, 2011.
3. Bureau of National Affairs, Inc: BNA Health Care Daily Report, October 8, 2010.