


## An Update on Section 501(r): Additional Federal Tax Requirements for Charitable Hospitals

**October 17, 2013**

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## Overview

- Community Health Needs Assessment requirement – section 501(r)(3)
- Financial assistance policy requirements – section 501(r)(4)
- Limitations on charges – section 501(r)(5)
- Billing and collection requirements – section 501(r)(6)

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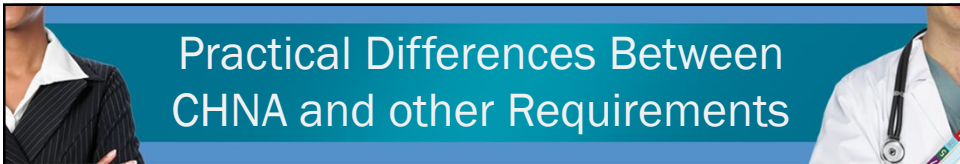


## Primary Focus on Requirements other than CHNA

- This presentation focuses on requirements relating to financial assistance and emergency medical care policies, charges for certain care provided to individuals eligible for financial assistance, and billing and collections, and also consequences of failure to comply
- Highlights of requirements relating to the CHNA requirement will also be discussed, including the recent guidance requirement to adopt an implementation strategy
- The presentation also highlights both similarities and differences between the CHNA requirement and other requirements that have practical significance

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## Practical Differences Between CHNA and other Requirements

- The CHNA requirement generally is met once every three years (and with annual reporting)
- The requirements relating to financial assistance policies, limitations on charges and billing and collections, on the other hand, apply continuously to operations of a hospital organization
- Accordingly, the requirements other than the CHNA may have more impact on day-to-day operations. Provisions for failures to meet the requirements and effective dates accordingly have somewhat different impact with respect to the CHNA and non-CHNA requirements

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### Overview of the Community Health Needs Assessment Requirement – Section 501(r)(3)

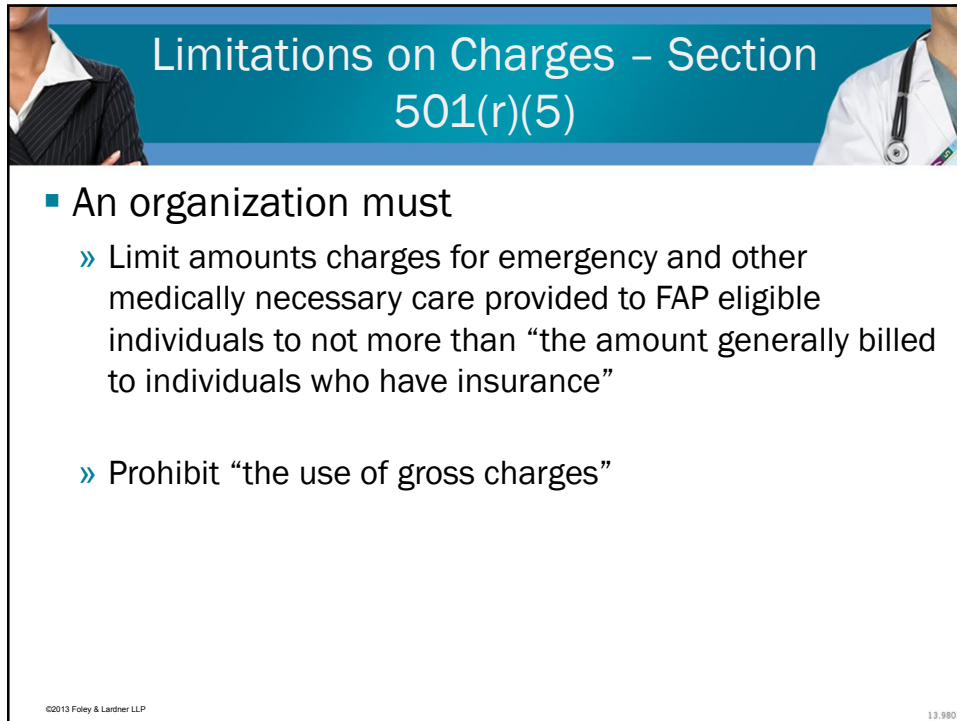
- An organization must adopt a CHNA at least every three years and adopt an implementation strategy to meet community health needs identified through such assessment
- The CHNA must take into account input from persons who represent the broad interests of the community served, including those with special knowledge of public health and be made widely available to the public

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### Overview of Financial Assistance Policy Requirement – Section 501(r)(4)

- An organization must establish for each hospital facility
  - » A written financial assistance policy, including eligibility criteria for financial assistance, the basis for calculating amounts charged to patients, the method for applying for financial assistance, actions the organization may take in the event of nonpayment, including collections actions and reporting to credit agencies, and measures to widely publicize the policy in the community service
  - » A written emergency care policy, requiring care for emergency medical conditions without discrimination

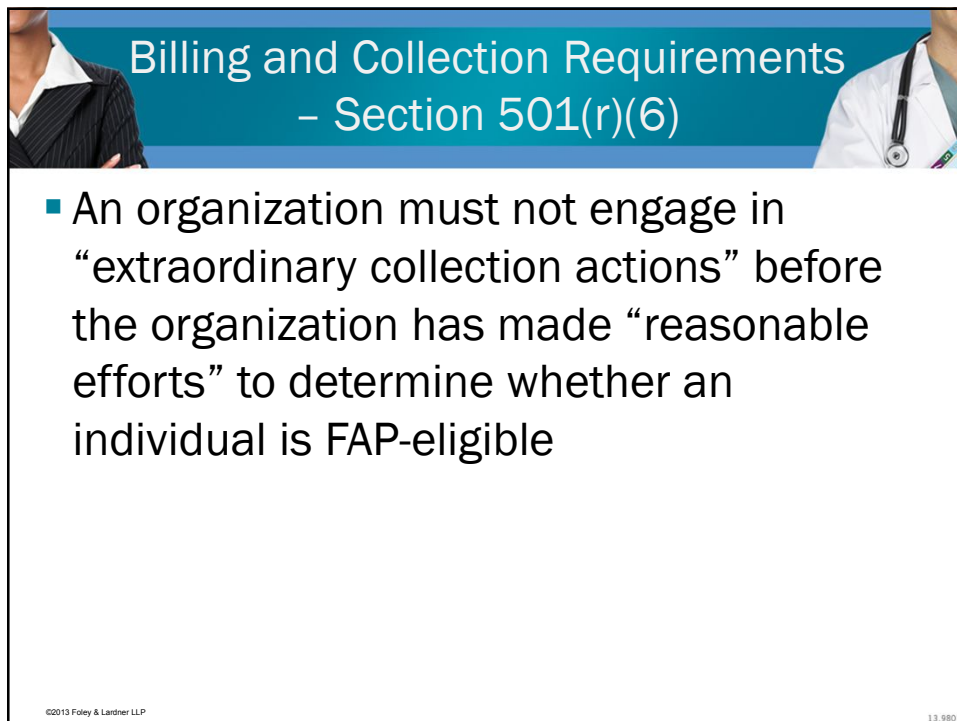
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## Limitations on Charges – Section 501(r)(5)

- An organization must
  - » Limit amounts charges for emergency and other medically necessary care provided to FAP eligible individuals to not more than “the amount generally billed to individuals who have insurance”
  - » Prohibit “the use of gross charges”

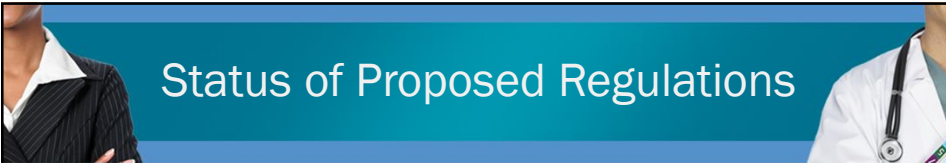
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## Billing and Collection Requirements – Section 501(r)(6)

- An organization must not engage in “extraordinary collection actions” before the organization has made “reasonable efforts” to determine whether an individual is FAP-eligible

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## Status of Proposed Regulations

- Proposed regulations published on June 26, 2012 (the 2012 proposed regulations) concern financial assistance policies, limitations on charges and billing and collection requirements, but not the Community Health Needs Assessment requirement or consequences of noncompliance
- Proposed regulations published on April 5, 2013 (the 2013 proposed regulations) mostly concern the CHNA requirement, but also importantly address consequences of noncompliance and some other points relevant to the non-CHNA requirements
- To be published as final regulations at the same time

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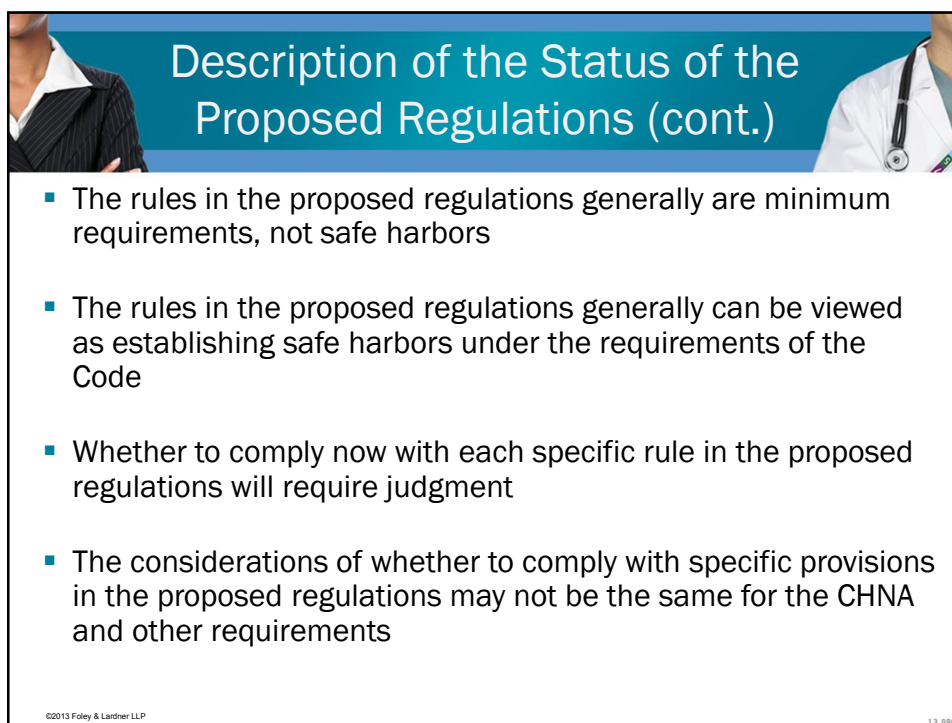
## Description of the Status of the Proposed Regulations

- Not currently effective, but address rules in the Code that are currently effective
- Proposed tax regulations are frequently, but not always, significantly revised when published in final form
- CHNA requirements are possibly less susceptible to significant revision than the non-CHNA requirements because the 2013 proposed regulations considered detailed public comments to Notice 2011-52
- The proposed regulations set forth very detailed and specific requirements

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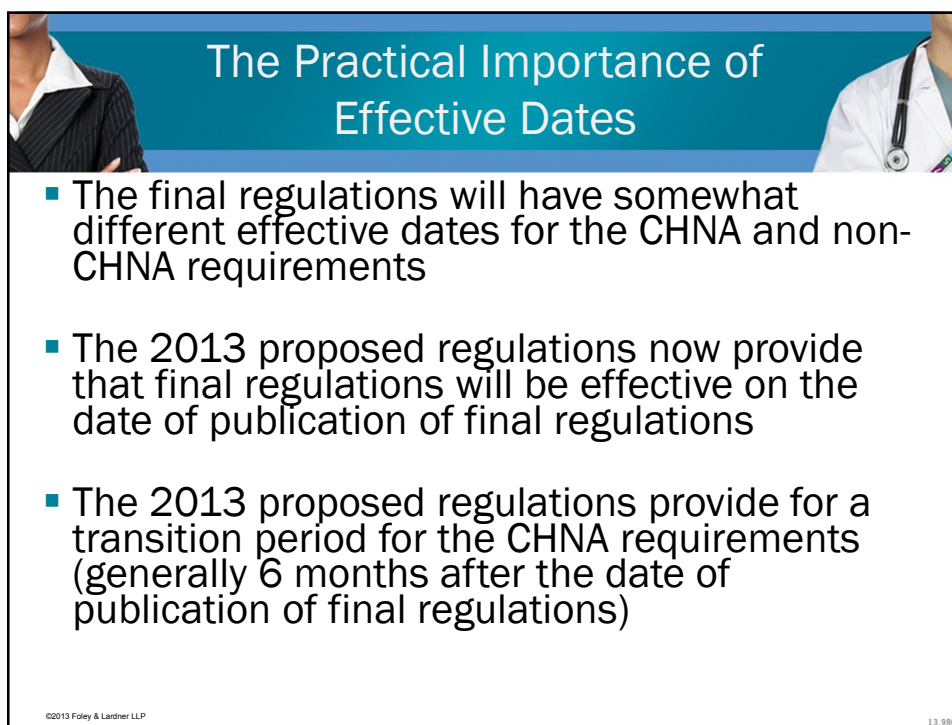




## Description of the Status of the Proposed Regulations (cont.)

- The rules in the proposed regulations generally are minimum requirements, not safe harbors
- The rules in the proposed regulations generally can be viewed as establishing safe harbors under the requirements of the Code
- Whether to comply now with each specific rule in the proposed regulations will require judgment
- The considerations of whether to comply with specific provisions in the proposed regulations may not be the same for the CHNA and other requirements

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## The Practical Importance of Effective Dates

- The final regulations will have somewhat different effective dates for the CHNA and non-CHNA requirements
- The 2013 proposed regulations now provide that final regulations will be effective on the date of publication of final regulations
- The 2013 proposed regulations provide for a transition period for the CHNA requirements (generally 6 months after the date of publication of final regulations)

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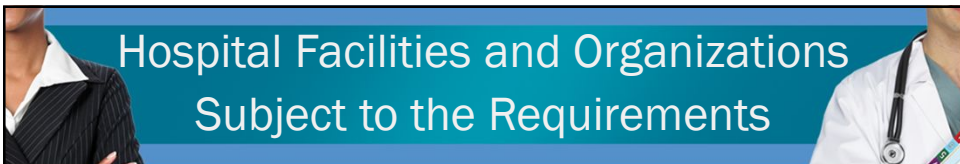


## The Practical Importance of Effective Dates (cont.)

- The 2013 proposed regulations do not currently provide for any transition relief for the non-CHNA requirements. This effective date is stricter than the effective date proposed in the 2012 proposed regulations (the first taxable year after the date of publication of final regulations)
- The preamble to the 2013 regulations states that the Treasury Department will consider transition relief for the non-CHNA requirements “based on the estimated amount of time to come into compliance with those rules rather than a particular organization’s taxable year.” That appears to mean that there will be some transition period or periods, but there is no indication of how long they will be

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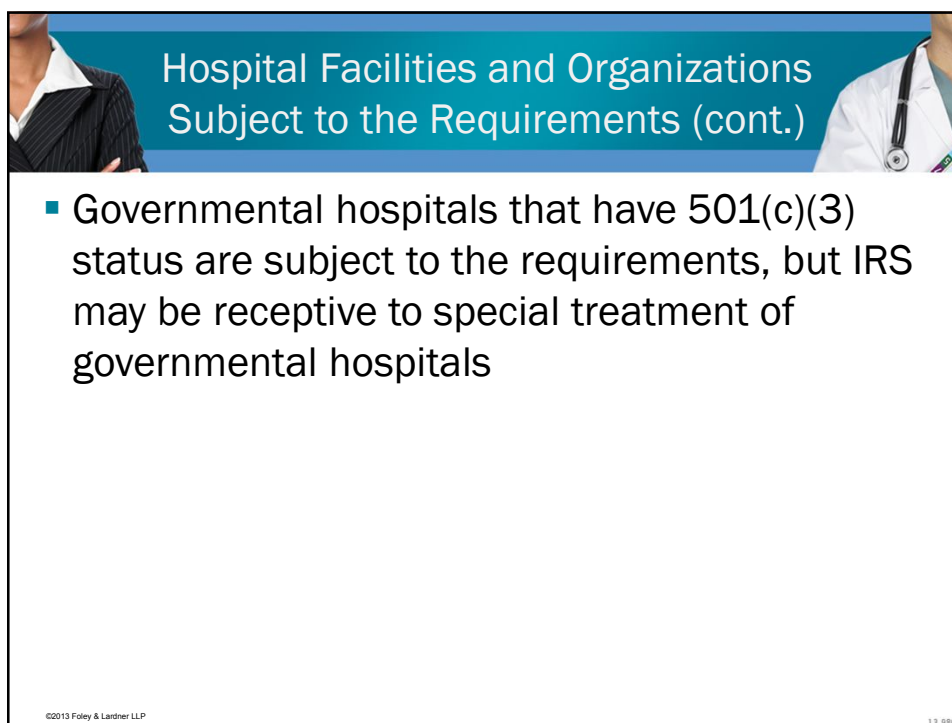


## Hospital Facilities and Organizations Subject to the Requirements

- The requirements apply separately to hospital facilities
- Hospital facilities are defined by reference to state law licensing requirements, as clarified in the 2013 proposed regulations
- Hospital organizations generally include organizations operating hospital facilities through joint ventures and similar arrangements

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### Hospital Facilities and Organizations Subject to the Requirements (cont.)

- Governmental hospitals that have 501(c)(3) status are subject to the requirements, but IRS may be receptive to special treatment of governmental hospitals

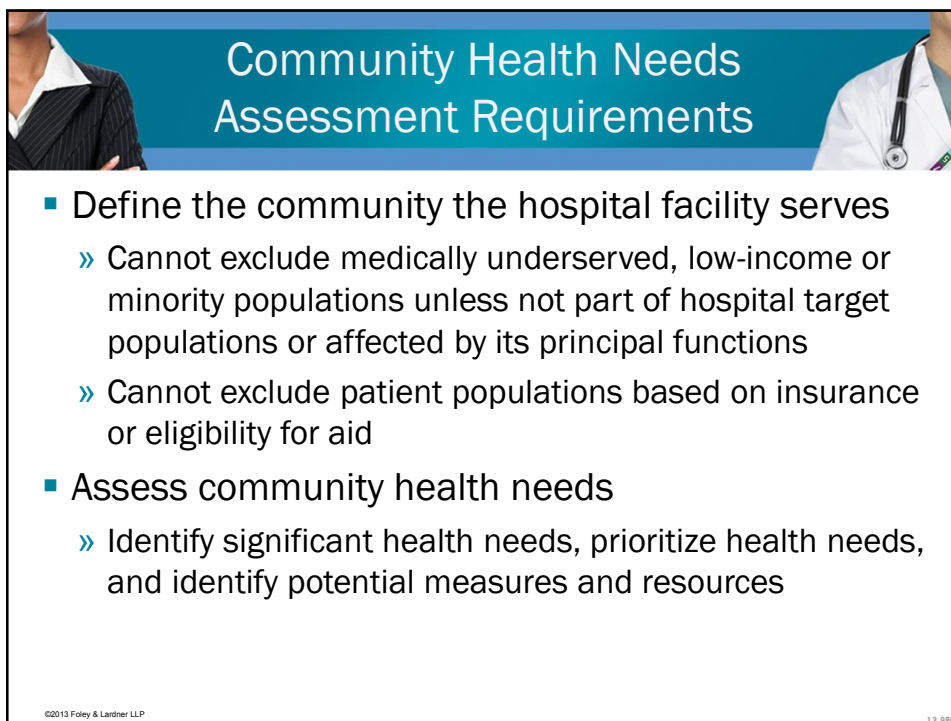
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### Transition Rule for Adoption of First CHNA Implementation Strategy

- Special transition rules for adopting first CHNA implementation strategy
- For CHNA conducted in taxable year beginning before March 23, 2012, adopt implementation strategy in first 4 ½ months of the first taxable year after March 23, 2013
- For CHNA conducted in taxable year beginning after March 23, 2012, adopt implementation strategy 4½ months after CHNA due date

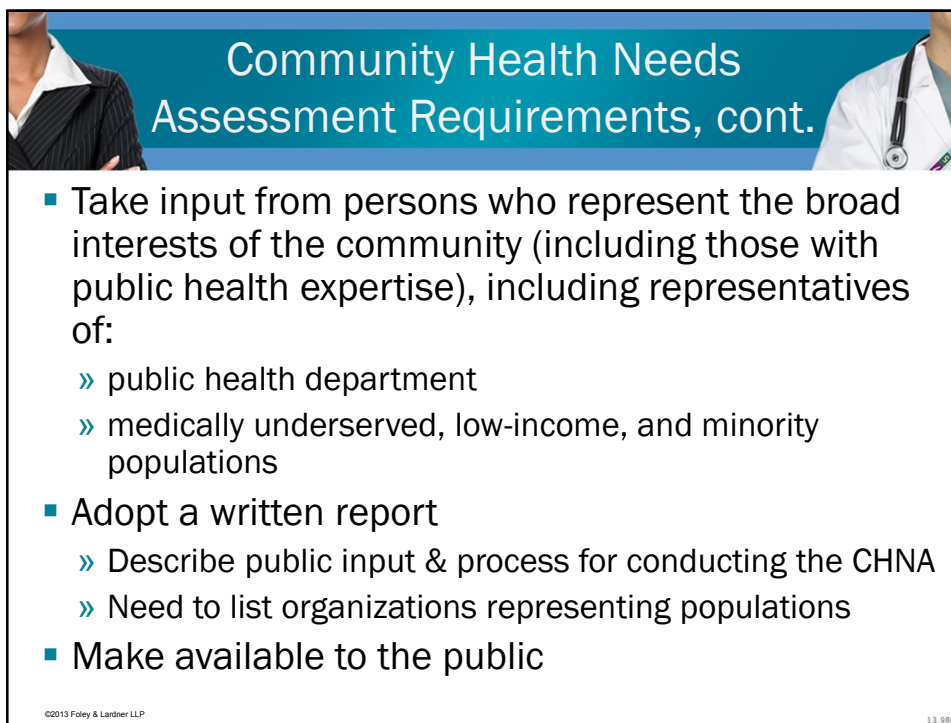
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**Community Health Needs Assessment Requirements**

- Define the community the hospital facility serves
  - » Cannot exclude medically underserved, low-income or minority populations unless not part of hospital target populations or affected by its principal functions
  - » Cannot exclude patient populations based on insurance or eligibility for aid
- Assess community health needs
  - » Identify significant health needs, prioritize health needs, and identify potential measures and resources

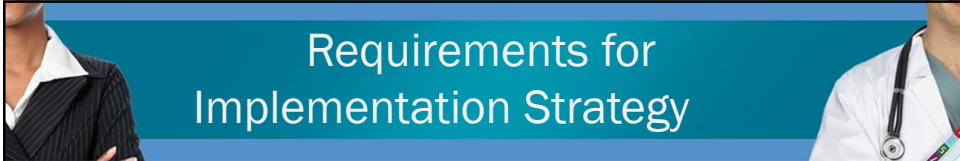
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**Community Health Needs Assessment Requirements, cont.**

- Take input from persons who represent the broad interests of the community (including those with public health expertise), including representatives of:
  - » public health department
  - » medically underserved, low-income, and minority populations
- Adopt a written report
  - » Describe public input & process for conducting the CHNA
  - » Need to list organizations representing populations
- Make available to the public

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## Requirements for Implementation Strategy

- The 2013 proposed regulations require that an implementation strategy must (1) describe how the hospital facility plans to address each significant health need or (2) identify the health need as one the hospital facility does not intend to address and explain why the hospital does not intend to address the health need
- The implementation strategy must also (1) identify the programs and resources the hospital plans to commit to address the health need, (2) describe any planned collaboration with other facilities or organizations

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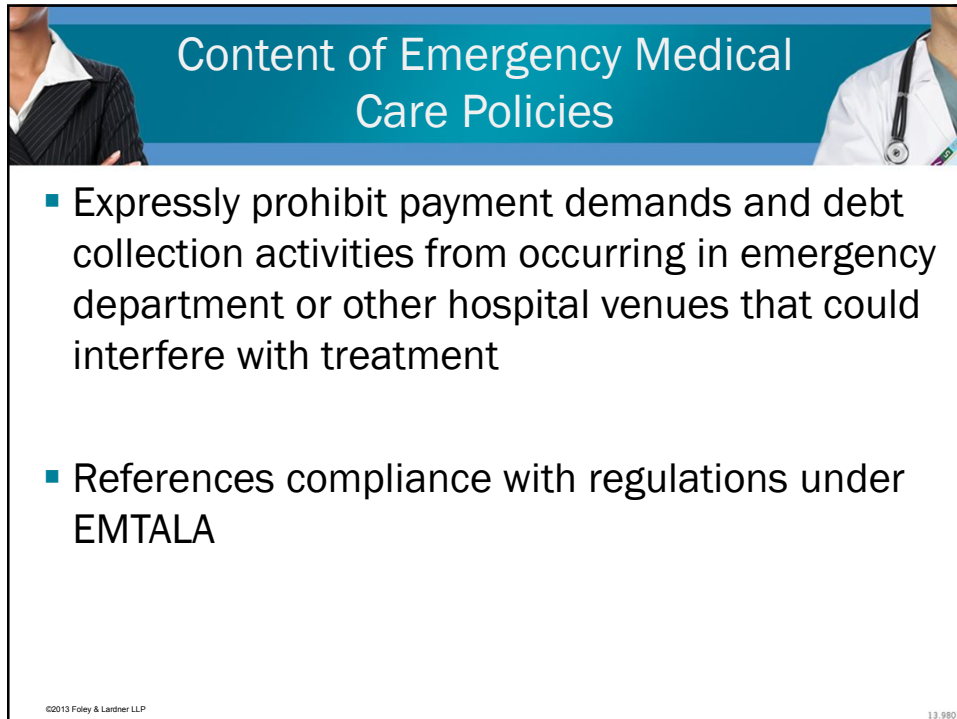


## Content of Financial Assistance Policies

- The 2012 proposed regulations describe the required content of an FAP in great detail, including detailed descriptions of particular procedures and time periods
- Financial assistance may not be denied based on an omission of information and documentation not specifically required by the FAP

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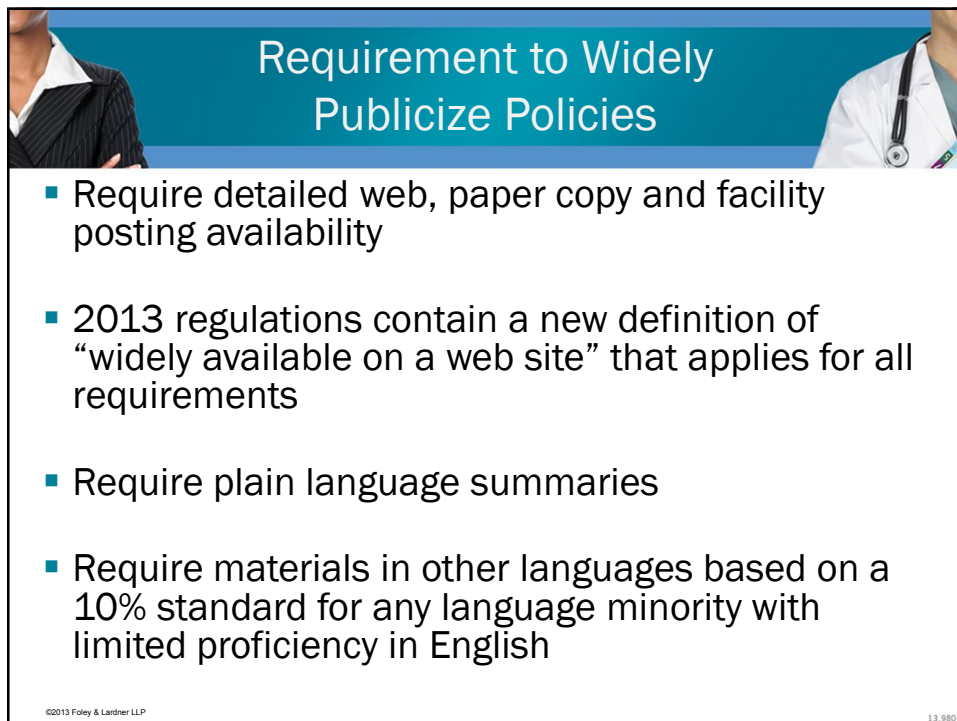
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## Content of Emergency Medical Care Policies

- Expressly prohibit payment demands and debt collection activities from occurring in emergency department or other hospital venues that could interfere with treatment
- References compliance with regulations under EMTALA

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## Requirement to Widely Publicize Policies

- Require detailed web, paper copy and facility posting availability
- 2013 regulations contain a new definition of “widely available on a web site” that applies for all requirements
- Require plain language summaries
- Require materials in other languages based on a 10% standard for any language minority with limited proficiency in English

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## Limitations on Charges

- Permit only two specified methods to determine "amounts generally billed"
- "Look-back Method" based on either Medicare fee-for-service only or Medicare fee-for-service together with all private health insurer paying claims
- "Prospective Medicare Method"
- One method must be chosen and consistently used
- Limitations on "gross charges"

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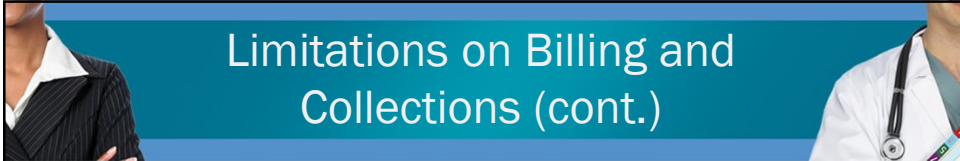


## Limitations on Billing and Collections

- Generally defines "extraordinary collection actions" by reference to legal or judicial process, but also include selling debt and reporting to credit agencies
- Very detailed procedural requirements for "reasonable efforts" to determine eligibility
- "Notification period" beginning on first date care provided, ending 120 days after first billing statement provided

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## Limitations on Billing and Collections (cont.)

- "Application period" beginning on first date care provided, ending 240 days after first billing statement
- Specified procedures for receipt of complete application, incomplete application and no application

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## Relationship to Form 990

- Implementation plan must be attached to Schedule H
- Schedule H, Section B now contains detailed questions that track 501(r) requirements; reporting the "wrong" answers could be a red flag for the IRS
- Many of the subsidiary questions in Schedule H, Section B are not requirements
- Future guidance on disclosure of failures to comply possibly could require disclosures in addition to Form 990

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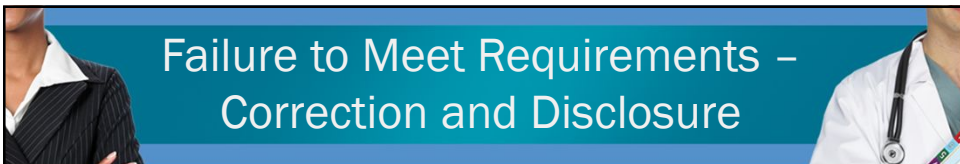


## Consequences of Failure to Meet Requirements – “Minor and Inadvertent”

- “Minor and inadvertent” omissions and errors do not result in noncompliance if they were “due to reasonable cause” and the hospital facility corrects the omission or error as promptly after discovery as is reasonable given the nature of the omission or error
- In light of the detail and scope of the 501(r) requirements, this provision permitting foot faults may be frequently relied upon

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## Failure to Meet Requirements – Correction and Disclosure

- Failures that are not “willful” or “egregious” will be excused if the hospital facility corrects and discloses
- Future IRS guidance will provide rules for correction and disclosure
- “Willful” failure includes failure due to gross negligence, reckless disregard, or willful neglect
- Standard for “egregious” failures may be less well defined

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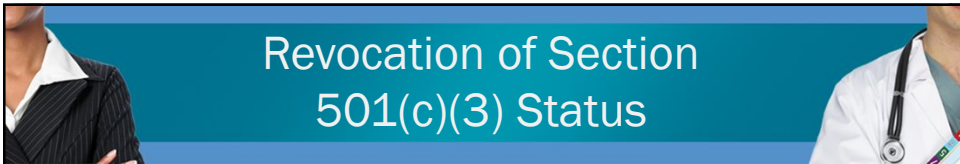


## Separate Application to Hospital Facilities

- The proposed regulations emphasize that the requirements apply separately to “hospital facilities”
- Accordingly, a hospital facility could be noncompliant, but the organization operating the facility still qualify as a 501(c)(3) organization

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## Revocation of Section 501(c)(3) Status

- The 2013 proposed regulations adopt a “facts and circumstances” test
- Factors include the relative size, scope and significance of failures and whether failures have previously occurred
- Similar to standards set forth in final regulations determining whether “excess benefit transactions” can result in revocation. Treas. Reg. §1.501(c)(3)-1(f)

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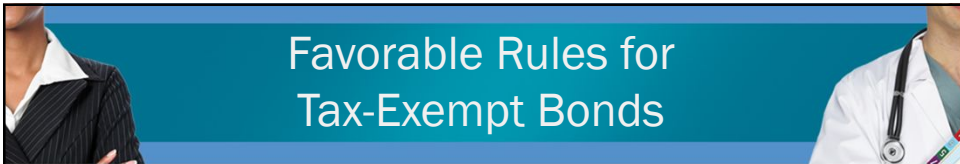


## Taxation of Noncompliant Hospital Facilities

- If a hospital facility is noncompliant, income from the hospital facility is subject to income tax, even if the organization remains a 501(c)(3) organization
- Note that the tax is technically not the unrelated trade or business income tax
- Rules are provided to not double count UBIT income and deductions

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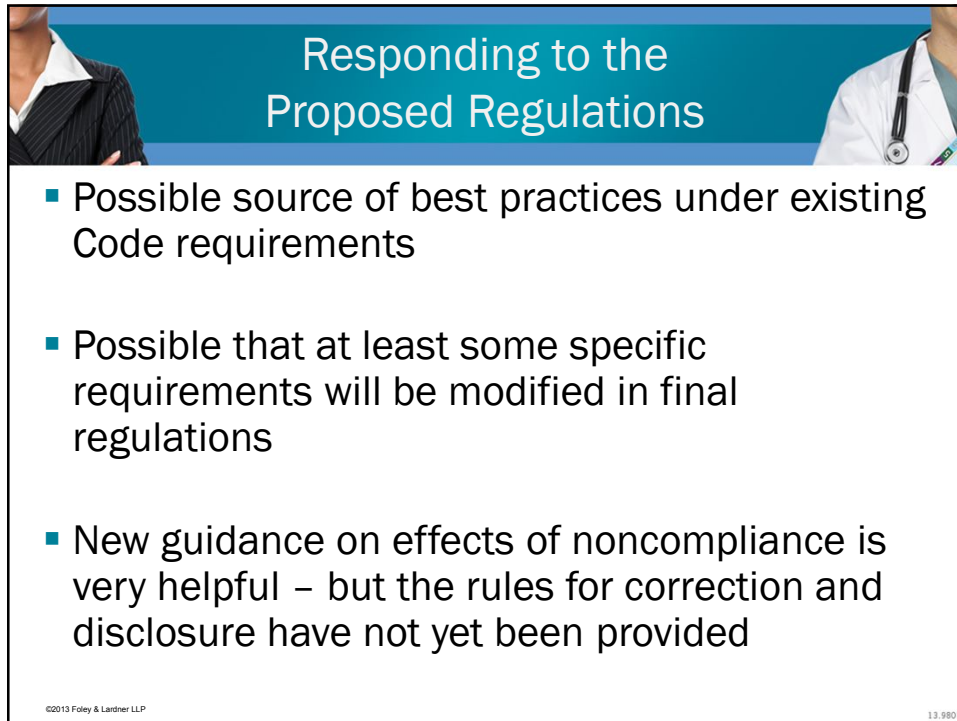


## Favorable Rules for Tax-Exempt Bonds

- Failure of a hospital facility to comply with 501(r) will not, in itself, affect the tax-exempt status of bonds financing the facility, unless 501(c)(3) status is revoked
- The basis for this favorable rule in part is that noncompliance is not technically treated an unrelated trade or business
- Compliance with detailed 501(r) requirements will remain important for tax-exempt bond opinions, but may not be necessary in bond document covenants

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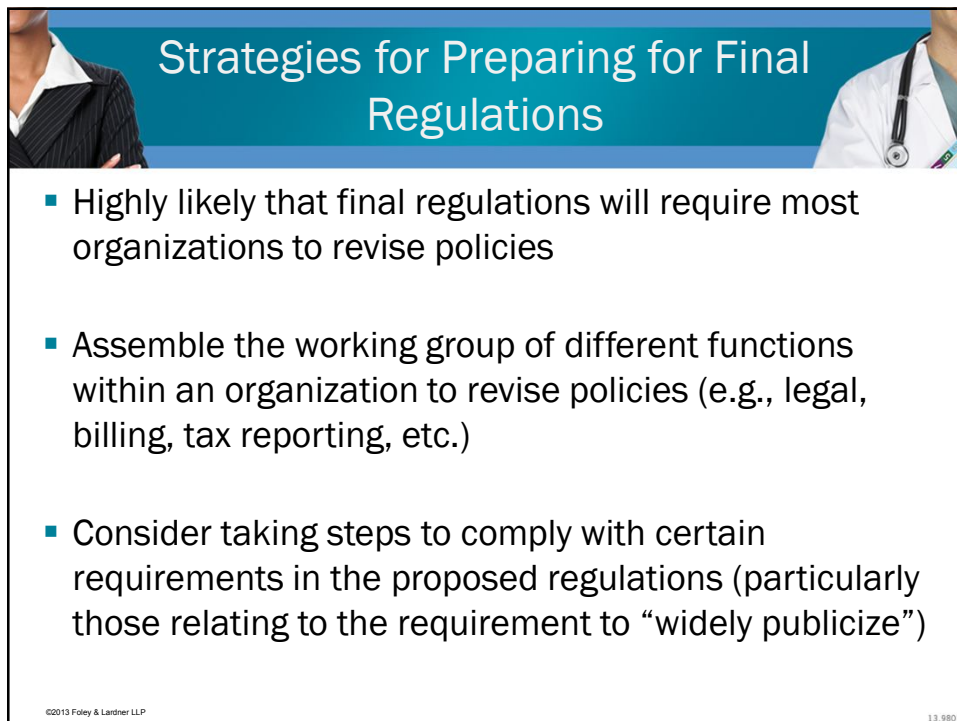
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## Responding to the Proposed Regulations

- Possible source of best practices under existing Code requirements
- Possible that at least some specific requirements will be modified in final regulations
- New guidance on effects of noncompliance is very helpful – but the rules for correction and disclosure have not yet been provided

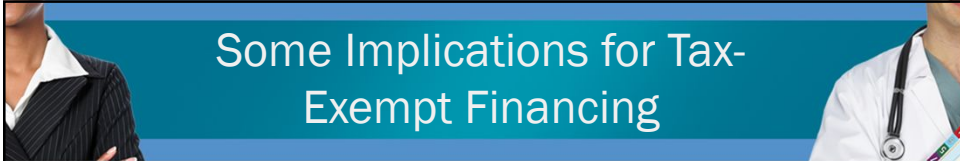
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## Strategies for Preparing for Final Regulations

- Highly likely that final regulations will require most organizations to revise policies
- Assemble the working group of different functions within an organization to revise policies (e.g., legal, billing, tax reporting, etc.)
- Consider taking steps to comply with certain requirements in the proposed regulations (particularly those relating to the requirement to “widely publicize”)

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## Some Implications for Tax-Exempt Financing

- Schedule H will be increasingly important for due diligence purposes
- Special disclosures of 501(r) noncompliance possibly may be disclosure items for securities law purposes
- Opinions regarding 501(r) compliance are not currently conventionally required, but that practice possibly could change

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## Questions & Answers

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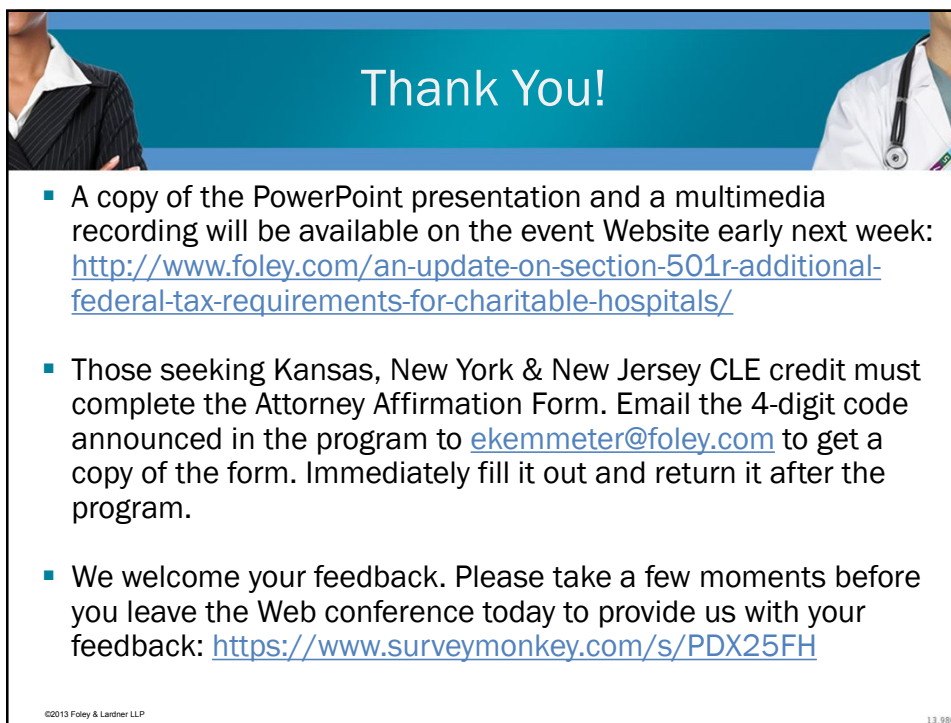
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## Thank You!

- A copy of the PowerPoint presentation and a multimedia recording will be available on the event Website early next week: <http://www.foley.com/an-update-on-section-501r-additional-federal-tax-requirements-for-charitable-hospitals/>
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