

PPACA's Additional Requirements Imposed on Tax-Exempt Hospitals Will Increase Transparency and Accountability on Fulfilling Charitable Missions

By Cynthia S. Marietta, J.D., LL.M. (Health Law)
csmarie@central.uh.edu

Introduction

Over the past decade, there has been growing concern that charitable hospitals afforded tax-exempt status are not fulfilling their charitable missions.¹ Five years ago, the United States Government Accountability Office (GAO) reported there was no discernible difference between the levels of charitable care provided by tax-exempt and for-profit hospitals.² Since then, media reports and congressional and state investigations have uncovered a host of concerns about the billing and collection practices of tax-exempt hospitals, including their use of aggressive tactics for collections and charging uninsured patients more than patients with insurance coverage.³ Just recently, a survey revealed that a significant number of nonprofit hospitals are not adequately publicizing their charity care programs or telling needy patients they may qualify for charity care.⁴

During the past few years, legislators have pushed to hold tax-exempt hospitals accountable for their special tax status and the federal tax benefits they receive.⁵ With the enactment of the Patient Protection and Affordable Care Act (PPACA),⁶ tax-exempt hospitals will now be held accountable for their special tax status and the charitable patient care and community benefits they are required to provide. Provisions in the PPACA outline specific measures for accountability and will enhance transparency to ensure that charitable hospitals are indeed acting charitably.⁷

¹ Julie Appleby, *Hospitals Keeping Quiet on Charity Care*, Kaiser Health News.com, May 5, 2010, <http://www.kaiserhealthnews.org/Stories/2010/May/05/Consumer-Groups-Criticize-Hospitals-On-Publicizing-Charity-Care.aspx>.

² United States Gov't Accountability Off'c, *NonProfit, For-Profit, and Government Hospitals: Uncompensated Care and Other Community Benefits, Statement of David M. Walker*, May 26, 2005, available at <http://www.gao.gov/new.items/d05743t.pdf>.

³ *Id.*; see also Sen. Chuck Grassley, *Memorandum: Grassley's Provisions for Tax-Exempt Hospital Accountability Included in New Health Care Law*, March 24, 2010, http://www.grassley.senate.gov/news/Article.cfm?customel_dataPageID_1502=25912.

⁴ John Commins, *Few Tax-Exempt Hospitals Offer Details on Charity Care for Needy Patients*, Health Leaders Media, May 5, 2010, <http://www.healthleadersmedia.com/content/LED-250620/Few-Taxexempt-Hospitals-Offer-Details-on-Charity-Care-for-Needy-Patients###>. The survey report, "Best Kept Secrets," examines whether nonprofits hospitals are meeting the voluntary guidelines established by the American Hosp. Ass'n. *Id.*

⁵ Sen. Chuck Grassley, *Memorandum, supra* note 3; see also Darren Barbee, *Texas Senator Wants to Guarantee Hospitals Do Their Share of Charity Care*, FORT-WORTH STAR TELEGRAM, Sept. 29, 2009, <http://www.rodneycellis.com/news/?id=0143>.

⁶ Patient Protection and Affordable Care Act, Pub. L. No. 11-148, 124 Stat. 119, Tit. IX, § 9007, Tit. X, Subtit. H, § 10903 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010).

⁷ Grassley, *Memorandum, supra* note 3.

Overview of PPACA's Additional Requirements for Tax-Exempt Hospital Organizations

Before the PPACA was enacted, charitable hospital organizations could qualify for federal tax exemption if they satisfied the criteria described in § 501(c)(3) of Internal Revenue Code of 1986 (IRC).⁸ Now the PPACA imposes additional requirements on charitable hospitals to qualify for § 501(c)(3) tax exempt status. Specifically, § 9007(a) of the PPACA amends § 501 of the IRC by adding new § 501(r) which outlines the additional requirements.⁹ To earn § 501(c)(3) tax-exempt status, hospital organizations must:

1. Conduct a “community health needs assessment” (“CHNA”) every three years and then adopt and implement a strategic plan to meet the community’s health needs identified through the assessment. The CHNA must take into account input from public health experts and individuals in the community who represent the broad interests of the community in the area served by the organization. The CHNA must be made available to the public.¹⁰
2. Submit on their Internal Revenue Service (“IRS”) Form 990 a description of how the organization is addressing the needs identified in the CHNA and a description of any such needs that are not being addressed together with the reasons why such needs are not being addressed.¹¹
3. Establish a written financial assistance policy, to include:
 - (a) The criteria for eligibility for financial assistance,
 - (b) The method for applying for financial assistance,
 - (c) The basis for calculating amounts charged to patients,
 - (d) The action to be taken in the event of nonpayment, and
 - (e) A description of the procedures to publicize the policy.¹²
4. Establish a written policy concerning emergency medical care, requiring the organization to provide care for emergency medical conditions regardless of the patient’s ability to pay.¹³

⁸ GAO, *supra* note 2. Section 501(c) specifies 28 types of entities that are eligible for tax-exempt status. *Id.*

⁹ PPACA, *supra* note 6, at §9007.

¹⁰ *Id.* at § 9007(a)(1)(3).

¹¹ *Id.* at § 9007(d). As added by the PPACA, § 9007(d) amends § 6033(b) of the Internal Revenue Code of 1986 by adding new paragraph 6033(b)(15). Section 6033(b)(15) requires hospital organizations to include on their Form 990, such description. *See also* Garrett Gluth, *IRS Notice 2010-39: Request for Comments Regarding Additional Requirements for Tax-Exempt Hospitals*, <http://www.irs.gov/charities/index.html>.

¹² PPACA, *supra* note 6, at § 9007(a)(1)(4)(A).

¹³ *Id.* at § 9007(a)(1)(4)(B).

5. Limit the amounts charged for emergency or non-emergency medical care to patients eligible for financial assistance to not more than the amount generally billed and prohibit the use of gross charges.¹⁴
6. Refrain from engaging in extraordinary billing and collection actions until after reasonable efforts have been made to determine whether a patient is eligible for financial assistance.¹⁵
7. Provide audited financial statements of the organization.¹⁶

Not only must a hospital organization satisfy the above additional requirements, but the organization's community benefit activities will be subject to review by the Department of Treasury at least once every three years.¹⁷ Any organization that fails to meet the CHNA requirements for any taxable year will be subject to an excise tax of \$50,000,¹⁸ and the amount of such excise tax must be reported on the annual tax return.¹⁹ All of the new requirements, with the exception of the CHNA requirements, will apply to taxable years after March 23, 2010.²⁰ The CHNA requirements become effective for taxable years after March 23, 2012.²¹

According to the PPACA, the Department of Treasury will issue regulations and guidance concerning these new requirements, and specifically, guidance relating to what constitutes "reasonable efforts" when determining eligibility for financial assistance for billing and collections purposes.²² The IRS and the Department of Treasury are currently soliciting comments regarding these new requirements.²³ Comments are due by July 22, 2010.²⁴

In Addition to PPACA Requirements, Hospital Organizations Must Still Satisfy Criteria to Qualify for Federal and State Tax-Exempt Status

Federal 501(c)(3) Tax-Exempt Status:

In addition the PPACA new requirements, a hospital organization seeking federal tax exempt status under § 501(c)(3) of the IRC, must still satisfy the § 501(c)(3) charitable organization criteria by showing:

¹⁴ *Id.* at § 9007(a)(1)(5), §10903(a). The PPACA, however, does not define "gross" charges.

¹⁵ *Id.* at § 9007(a)(1)(6).

¹⁶ *Id.* at § 9007(d).

¹⁷ *Id.* at § 9007(c).

¹⁸ *Id.* at § 9007(b). As added by the PPACA, § 9007(b) amends Subchptr. D of chptr. 42 of the Internal Revenue Code of 1986 by adding new § 4959. *See also* Gluth, *supra* note 11, at 1-2.

¹⁹ *Id.* at § 9007(d). As added by the PPACA, § 9007(d) amends § 6033(b) of the Internal Revenue Code of 1986 by amending § 6033(b)(10), which requires hospital organizations to report the amount of excise tax imposed under § 4959. *See also* Gluth, *supra* note 11, at 1-2.

²⁰ *Id.* at § 9007(f), §10903. Gluth, *supra* note 11, at 3.

²¹ PPACA, *supra* note 6, at § 9007(f)(2).

²² *Id.* at § 9007(a)(7).

²³ Gluth, *supra* note 11, at 4.

²⁴ *Id.*

(1) that it is organized and operated for an exempt “charitable purpose” as described in section 501(c)(3),

(2) that no part of its net earnings inure to the benefit of any private shareholder or individual, and

(3) that it does not participate in political campaigns on behalf of any candidate or conduct substantial lobbying activities.²⁵

The term, “charitable,”²⁶ is used in § 501(c)(3) in its generally accepted legal sense and includes the “promotion of health.”²⁷ In 1969, when the IRS issued Revenue Ruling 69-545, it established the “community benefit” standard for determining whether a hospital organization satisfies the “charitable purpose” requirement.²⁸ The “community benefit” standard identifies whether a health care organization operates to promote health in a way that benefits the community as a whole.²⁹ The standard sets out factors to be considered in measuring whether the organization provides “community benefits,” and includes: (1) whether the governance board that is composed of a broad base of members in the community; (2) whether a full-time emergency room is open to everyone, regardless of his or her ability to pay; (3) whether the medical staff has admission criteria open to all qualified physicians consistent with the size and nature of the facility; (4) whether surplus funds are used to improve facilities, equipment, patient care, medical training, research, and education; and (5) whether services are provided to a broad cross section of the community through charity care, including participation in Medicaid and Medicare.³⁰

State Tax-Exempt Status:

In addition to federal tax-exempt status, charitable hospital organizations may also receive exemptions from state and local income, property, and sales taxes.³¹ Some states, including Texas, have defined the “community benefit” standard for nonprofit hospitals. For instance, in Texas, a nonprofit hospital or hospital system is required to provide “community benefits,” which includes both charity care, as defined by the IRS, and

²⁵ Internal Revenue Code § 501(c)(3); GAO, *supra* note 2; *see also* Internal Rev. Serv., *Exemption Requirements – Section 501(c)(3) Organizations*, Dec. 7, 2009, <http://www.irs.gov/charities/charitable/article/0,,id=96099,00.html>.

²⁶ According to the IRS, the term “charitable” is used in its generally accepted legal sense and includes relief of the poor, the distressed, or the underprivileged, among other things. *See* Internal Rev. Serv., *Exempt Purposes*, Dec. 7, 2009, <http://www.irs.gov/charities/charitable/article/0,,id=175418,00.html>.

²⁷ *See* IRS Rev. Rul. 69-545, 1969-2 C.B. 117. A revenue ruling is a formally published interpretation of tax law by the IRS upon which taxpayers are entitled to rely. *See also* GAO, *supra* note 2, at 7.

²⁸ IRS Rev. Rul. 69-545, *supra* note 27.

²⁹ *Id.*

³⁰ *Id.*; *see also* GAO, *supra* note 2, at 7; Jason Gries, *IRS Report provides Insight into Community Benefit and Executive Compensation Practices of Tax-Exempt Hospitals*, Feb. 15, 2009, <http://greisguide.com/2009/02/15/irs-report-provides-insight-into-community-benefit-and-executive-compensation-practices-of-tax-exempt-hospital/>.

³¹ GAO, *supra* note 2, at 7.

government-sponsored indigent care, by complying with any one of the following three standards:

- (1) Provide charity care and government-sponsored indigent care equal to 100 percent of the hospital's or hospital system's tax-exempt benefits;
- (2) Provide charity care and government-sponsored indigent care at a level which is reasonable in relation to (a) the community needs as determined through a community needs assessment, (b) the available resources of the hospital or hospital system, and (c) the tax-exempt benefits received by the hospital or hospital system; or
- (3) Provide charity care and community benefits in a combined amount equal to at least five percent of the hospital's net revenue, as long as the charity care and government-sponsored indigent care are provided in an amount equal to at least four percent of net patient revenue.³²

The PPACA's Additional Requirements May Resolve the Growing Concern that U.S. (and Texas) Charitable Hospitals are Not Fulfilling Their Charitable Missions

The imposition of the PPACA's additional requirements to qualify for § 501(c)(3) tax-exempt status comes on the heels of the decade-long concern that charitable hospitals afforded tax-exempt status are not fulfilling their charitable missions.³³ For the past few years, legislators have pressed to hold tax-exempt hospitals accountable for the special tax status they receive. On a national level, Senator Chuck Grassley [R-Iowa] co-authored the bill provisions in the PPACA, imposing the additional requirements on tax-exempt hospitals.³⁴ These provisions are the culmination of several years of his leadership in pushing for transparency and accountability of tax-exempt organizations, including hospitals.³⁵

In Texas, Senator Rodney Ellis [D-Houston] has raised concern about whether the state's nonprofit hospitals are fulfilling their share of charity care.³⁶ He has proposed amending the current law governing Texas nonprofit hospitals' charity-care quotas to improve uniformity, transparency, and an effective enforcement mechanism to ensure nonprofit hospitals comply with charity requirements and account for their charity care.³⁷ In August 2009, Sen. Ellis sent a letter to Texas Attorney General, Greg Abbott, expressing his concern about the lack of enforcement of the law and requesting the Attorney General's office ("AG's Office") to issue an opinion regarding the reporting and accountability of charity care provided by nonprofit hospitals in Texas.³⁸ Sen. Ellis

³² TEX. HEALTH & SAFETY CODE ANN. § 311.045 (a), (b) (Vernon 2009).

³³ Appleby, *supra* note 1.

³⁴ Grassley, *Memorandum*, *supra* note 3.

³⁵ *Id.*

³⁶ Barbee, *supra* note 5.

³⁷ *Id.*

³⁸ See Correspondence to Attorney General Greg Abbott, Aug. 27, 2009, available at <http://www.oag.state.tx.us/opinions/opinions/50abbott/rq/2009/pdf/rqo821GA.pdf>.

subsequently withdrew his request for a formal opinion,³⁹ but left pending a more or less informal request for the AG's Office to assess the law and recommend ways to improve the provision and accountability of charity care in Texas.⁴⁰

Now with the PPACA in effect, concerns about the lack of transparency and levels of accountability for providing charity care may be resolved or at least somewhat diminished with the imposition of the additional requirements. Charitable hospitals in the U.S. will now have to conduct a CHNA and implement a plan and then account for any failures to address community needs on the Form 990. If they fail to satisfy the CHNA requirements, they could be subject to a punitive measure in the form of a hefty excise tax beginning in 2012.

Conclusion

Charitable hospital organizations seeking to qualify for federal tax-exempt status must satisfy not only § 501(c)(3) criteria but also the PPACA's additional requirements. Among other things, these requirements impose transparency on hospital organizations and require a level of accountability for providing adequate charity care. In a nutshell, those charitable hospital organizations seeking to reap the benefits of tax-exempt status will have to prove they are fulfilling their charitable missions.

Health Law Perspectives (July 2010)

Health Law & Policy Institute

University of Houston Law Center

<http://www.law.uh.edu/healthlaw/perspectives/homepage.asp>

The opinions, beliefs and viewpoints expressed by the various Health Law Perspectives authors on this web site do not necessarily reflect the opinions, beliefs, viewpoints, or official policies of the Health Law & Policy Institute and do not constitute legal advice. The Health Law & Policy Institute is part of the University of Houston Law Center. It is guided by an advisory board consisting of leading academicians, health law practitioners, representatives of area institutions, and public officials. A primary mission of the Institute is to provide policy analysis for members of the Texas Legislature and health and human service agencies in state government.

³⁹ Attorney General of Texas, Pending Opinion Requests, *available through* <http://www.oag.state.tx.us>.

⁴⁰ Telephone conference with Sen. Rodney Ellis' office staff, June 15, 2010.