IRS Proposes Requirements to Make Charitable Hospitals More “Charitable”

On April 5, 2013, the Internal Revenue Service (IRS) published a proposed rule regarding certain requirements for tax exempt hospitals to conduct Community Health Needs Assessments (CHNA). These provisions were made as a part of the 2010 Patient Protection and Affordable Care Act (ACA) in an effort to increase community-based preventive public health services, e.g., weight loss clinics, smoking cessation programs, in lieu of charity medical care. The approximately 2,900 tax exempt hospitals across the U.S. receive an estimated $13 billion in tax benefits annually. However, a recent study utilizing 2009 IRS data for more than 1800 charitable hospitals indicated that the level of community benefits provided varied significantly, i.e., from 1.1% to 20.1% of the hospital’s operating expenses. Hospitals spent an average of only 7.5% of operating expenses on community benefits. Of this amount, 85.3% was spent on patient care services and only 5.3% on community health improvement. In March 2013, the City of Pittsburgh brought forth a civil action complaint against the University of Pittsburgh Medical Center (UPMC) alleging that UPMC failed to meet the criteria to qualify as an Institution of Purely Public Charity (IPPC). Included in the list of allegations were that UPMC: (1) subsidized for-profit enterprises in lieu of supporting charitable activities; (2) replaced hospitals in underserved, poor communities with those in areas of higher socioeconomic status; and, (3) paid unreasonable compensation and benefits to UPMC officers, not consistent with the charitable status of UPMC. UPMC, comprised of more than 20 hospitals, 400 outpatient sites, and over 50,000 employees, boasted annual compensation exceeding $1 million for over 20 employees in fiscal year 2011, with the highest-paid—UPMC President and CEO Jeffrey Romoff—paid an annual salary of over $5.9 million. Previously, tax-exempt hospitals were only required to submit to the IRS a list of community benefits provided on an annual basis. However, under the recent proposed rule, hospitals will also be required to conduct and widely publicize the results of a CHNA at least every 3 years, and develop an implementation strategy to address identified community health needs found in the CHNA, to be filed with the Form 990 on an annual basis. The new regulations would go into effect for every tax year after March 23, 2012.

Consequences for failing to adhere to the regulations result in revocation of a facility’s tax exempt status, after a thorough review, as well as any other applicable penalties published in prior rules. In addition, an excise tax may be applied to those tax-exempt hospitals that fail to complete a CHNA under the proposed rule. All rulings and investigations of misconduct will be conducted for hospitals on a case-by-case basis, regardless of hospital subsidy or system ownership, i.e., a tax-exempt health system would retain charitable status, if only one hospital has tax-exempt status revoked.

The provisions detailed in the April 5 proposed rule, while more demanding than previous regulations, were designed to allow charitable hospitals to retain the flexibility of identifying and choosing the method(s) by which to address those particular community needs that are prioritized in the CHNA. Despite this relative “freedom,” it is anticipated that the provision of the proposed regulations would result in greater transparency in the conduct of tax-exempt hospitals, and may have the potential to positively impact healthcare costs and consumer access to healthcare as well.

3 Ibid, Bloomberg, April 24, 2013
7 Ibid, Bloomberg, April 24, 2013
10 Ibid, Internal Revenue Service, April 5, 2013, p. 10
Mr. Cimasi holds a Masters in Health Administration from the University of Maryland, as well as several professional designations: Accredited Senior Appraiser (ASA – American Society of Appraisers); Fellow Royal Intuition of Chartered Surveyors (FRICS – Royal Institute of Chartered Surveyors); Master Certified Business Appraiser (MCBA – Institute of Business Appraisers); Accredited Valuation Analyst (AVA – National Association of Certified Valuators and Analysts); and, Certified Merger & Acquisition Advisor (CM&AA – Alliance of Merger & Acquisition Advisors). He has served as an expert witness on cases in numerous courts, and has provided testimony before federal and state legislative committees. He is a nationally known speaker on healthcare industry topics, the author of several books, the latest of which include: “Accountable Care Organizations: Value Metrics and Capital Formation” (2013 - Taylor & Francis, a division of CRC Press), “The Adviser’s Guide to Healthcare” – Vols. I, II & III [2010 – AICPA], and “The U.S. Healthcare Certificate of Need Sourcebook” [2005 - Beard Books]. His most recent book, entitled “Healthcare Valuation: The Financial Appraisal of Enterprises, Assets, and Services” will be published by John Wiley & Sons in the Fall of 2013.

Mr. Cimasi is the author of numerous additional chapters in anthologies; books, and legal treatises; published articles in peer reviewed and industry trade journals; research papers and case studies; and, is often quoted by healthcare industry press. In 2006, Mr. Cimasi was honored with the prestigious “Shannon Pratt Award in Business Valuation” conferred by the Institute of Business Appraisers. Mr. Cimasi serves on the Editorial Board of the Business Appraisals Practice of the Institute of Business Appraisers, of which he is a member of the College of Fellows. In 2011, he was named a Fellow of the Royal Institution of Chartered Surveyors (RICS).