

EOTS NewsFlash

Exempt Organizations Tax Services

August 30, 2012

Section 501(r) public comments deadline approaching; overview of proposed regulations

Overview

On June 22, 2012, the Internal Revenue Service and the Treasury Department issued a notice of proposed rulemaking ("NPRM" or "proposed regulations") under Internal Revenue Code section 501(r) pertaining to requirements that charitable hospitals must satisfy to be exempt under section 501(c)(3). The NPRM contains comprehensive and detailed proposed guidance regarding key aspects of the statute, including financial assistance policies (FAPs), emergency care policies, billing and collection policies, and amounts that may be charged for care provided to individuals eligible for financial assistance under the facility's FAPs.

The Treasury Department and IRS request public comments by September 24, 2012, regarding the NPRM, which is proposed to be effective for taxable years beginning on or after the date that final regulations are adopted. Taxpayers may rely on the proposed regulations until temporary or final regulations are issued.

This newsletter provides some general observations about the NPRM, describes its general approach and framework, summarizes areas not addressed by the proposed rules, and provides a summary of the NPRM's key provisions. PwC is considering providing formal comments to the Treasury Department and IRS based on its assessment of the proposed guidance and is seeking input from its clients and others, particularly with respect to identifying those areas that raise significant compliance burden concerns, require significant changes to a hospital's ongoing operational processes or relationships with its patients in order to implement, or require additional clarification. For a discussion of section 501(r) generally, please refer to the June 22, 2012 [*EOTS NewsFlash*](#).

General observations

Far-reaching "consumer-protection" tax regulations

The NPRM is a tax regulation that affects virtually every aspect of a hospital's operations and administration. Its substantive and procedural requirements will impact the patient intake, patient discharge, financial assistance, billing, collection,



emergency room, and community relations functions of each hospital facility operated by a hospital organization described in section 501(c)(3). The proposed rules interpret the section 501(r) statutory requirements by providing comprehensive consumer-type protections for individuals who are or may be eligible for financial assistance under the facility's financial assistance policy. In addition, some of the proposed rules regarding billing and collections policies and emergency care policies apply to all individuals regardless of eligibility for financial assistance, and in some cases to care not covered by the facility's financial assistance policy.

Meaning of FAP-eligible individual

Many of the proposed rules are dependent upon an individual being a "FAP-eligible individual" under the NPRM. The NPRM defines "FAP-eligible individual" to mean any individual who is eligible for financial assistance under the facility's financial assistance policy, without regard to whether the individual has applied for assistance under the policy. This appears to have the effect of presuming an individual to be FAP-eligible unless and until the individual is determined to be ineligible or certain time periods specified in the NPRM have passed. Further clarification regarding the definition of FAP-eligible individual, the consequences that flow from the definition, and the information a facility may take into account when making FAP-eligibility determinations, will be required before final rules are adopted in order to provide greater certainty regarding application of these rules.

Complexity of FAP notification and reasonable efforts processes

The proposed rules regarding the requirements to notify an individual of the facility's FAP, and the steps that must be taken to satisfy the reasonable efforts requirement before extraordinary collections actions may be commenced, are among the NPRM's most complicated and detailed rules. These rules will impact the content and processes of communications with a facility's patients at virtually every stage from patient intake and the provision of care until ultimate payment or resolution of the bill. The NPRM's proposed guidance regarding a facility's agreements with third party debt collection agencies would also result in many of those agreements having to be revised to comply with section 501(r). Although many hospitals already conduct comprehensive notification and communications programs regarding their financial assistance and billing and collection policies, all hospitals subject to section 501(r) will have to review existing processes and policies to determine whether and which additional steps would be required under the NPRM.

Complying with AGB rules

A hospital organization will want to carefully review the NPRM's required methods to determine the maximum amounts a facility may charge FAP-eligible individuals for emergency and other medically necessary care in order to remain exempt under section 501(c)(3). Under the NPRM, one of two methods must be adopted by the hospital facility, and the choice of methods is permanent and may not be changed, so the selection could have longstanding implications for the facility's charges for this type of care. Further, the requirement that a hospital facility disclose in its FAP its AGB method and, if applicable, either state the AGB percentages of gross charges or explain how such information may be obtained, would make such AGB information widely available to the public.

Interaction with other rules and reporting requirements

The extent to which the NPRM rules will be in addition to, and in some cases inconsistent with, state consumer protection laws or other regulations addressing

billing and collection practices of hospitals is unclear and will require considerable review and attention. In addition, the potential interaction between the NPRM and financial accounting rules pertaining to patient charges, collections, financial assistance amounts and bad debt, as well as the interaction with Form 990 Schedule H reporting, will also have to be considered.

Interim compliance and consequences

Although many hospital organizations already have processes in place that address the key areas covered by section 501(r) - including financial assistance policies, emergency care policies, and billing and collection policies - the NPRM would impose significant new content and process requirements on many hospital organizations in these areas. In the absence of guidance explaining the consequences of a failure to satisfy the various requirements of the statute, and prior to the issuance of final or temporary regulations implementing these requirements, hospital organizations must consider whether to move forward to incorporate the NPRM provisions into their systems and processes, or adopt a wait-and-see approach until final guidance is issued.

Approach and framework of the proposed regulations

The proposed regulations, including the explanatory preamble, are 94 pages long and contain highly detailed guidance regarding various aspects of section 501(r). It is clear that the IRS and Treasury opted for a "rules-based" rather than a "principles-based" approach to this guidance. The result is a set of proposed rules that provide comprehensive and highly specific "bright line" standards applying many of the section 501(r) mandates.

The NPRM does not impose quantitative or qualitative standards on the types or amounts of care, charity care, or community benefit a charitable hospital must provide. Further, the proposed regulations do not impose quantitative or qualitative standards on an individual's eligibility for financial assistance or the types or quantity of financial assistance a hospital facility must provide. The NPRM instead requires that each hospital facility adopt and implement a financial assistance policy setting forth eligibility and assistance criteria, and provides highly detailed proposed guidance focusing on numerous protections mandated by section 501(r) with respect to individuals who are eligible for financial assistance under the facility's financial assistance policy.

These protections include establishing and implementing a written financial assistance policy (FAP), making the individual aware of the FAP eligibility requirements and types of financial assistance, providing free copies of the FAP and FAP-related materials via various means, making the individual aware of available assistance to complete the FAP-application process, limiting the amounts that may be charged a FAP-eligible individual for medical care, and prohibiting extraordinary collection actions for certain periods while FAP-eligibility is being determined (and ultimately reversing and apparently not initiating any new ECAs against any individual determined to be FAP-eligible).

The proposed regulations would adopt a notification period during which the hospital facility must either make a FAP-eligibility determination or provide notifications to the individual about the FAP and related materials, and an application period during which the hospital facility must accept a FAP application submitted by an individual

who was provided care by the facility. Numerous protections for FAP-eligible individuals are provided during these periods.

Items not addressed by the proposed regulations

The proposed guidance does not address the consequences of failing to satisfy the statutory requirements of section 501(r), which is reserved for future guidance. The NPRM also does not address community health needs assessments (CHNAs), which were addressed in IRS Notice 2011-52. (A description of the CHNA notice is available [here](#)) Hospital organizations may rely on the guidance in Notice 2011-52 with respect to any CHNA made widely available to the public, and any implementation strategy adopted, on or before the date that is six months after the date further guidance regarding the CHNA requirements is issued.

Key aspects of the proposed regulations

1. **Definition of hospital facility and hospital organization.** The proposed regulations provide clarification regarding the meaning of these key terms. In particular, pending further guidance, they limit the application of section 501(r) to organizations described in section 501(c)(3) that are operating one or more hospital facilities, which appears to be intended to track the Form 990 Schedule H definition of the same term. The NPRM provides that a government hospital that is described in or seeking exemption under section 501(c)(3), as well as a hospital facility operated by a disregarded entity of which a section 501(r) hospital organization is the sole member, is subject to section 501(r). The NPRM generally excludes foreign hospitals from the requirements of section 501(r), and reserves for future guidance the treatment of a hospital facility operated by a joint venture of which a section 501(r) hospital organization is a partner or member.
2. **Content of the FAP.** Section 501(r) requires each hospital facility to establish a financial assistance policy. The NPRM does not require the facility to provide any financial assistance to any individual, but nonetheless implements the statutory requirement that each facility establish a written FAP setting forth (1) eligibility criteria for financial assistance, and whether such assistance includes free or discounted care; (2) the basis for setting amounts charged to patients; (3) the method for applying for financial assistance; (4) in the case of an organization that does not have a separate billing and collections policy, the actions the hospital organization may take in the event of nonpayment; and (5) measures to widely publicize the FAP within the community to be served by the hospital organization. The proposed regulations require numerous specific content items that must be included in a hospital facility's FAP in order for a hospital facility to be treated as satisfying the statute's FAP content requirements.
3. **Description of the Notification Period and the Application Period.** The NPRM adopts two periods - the notification period and the application period - during which the hospital facility must take certain actions with respect to identifying FAP-eligible individuals, and is prohibited from taking certain billing and collection actions with respect to FAP-eligible individuals. The notification period is the period beginning on the date the medical care was provided to the individual and ending on the date that is 120 days after the date of the first billing statement issued to the individual. The hospital facility must either make a FAP-eligibility determination or provide certain notices to the individual regarding the FAP and FAP application process by

the end of the notification period. The application period is the period beginning on the date the medical care is provided and ending on the date that is 240 days after the date of the first billing statement provided to the individual. The hospital facility must accept and process a FAP application from an individual if it is submitted before the end of the application period. The NPRM provides specific rules regarding actions that must be taken in the event of incomplete and completed applications, and also describes actions that are permitted, prohibited, or required during the notification and application periods.

4. **Making the FAP Widely Available to the Public.** The statute and proposed regulations require the hospital facility to make the FAP widely available to the public. Under the NPRM, this means that each hospital facility must make the FAP available through various means. Each facility is required to make the FAP readily available on a website, upon request and without charge in public locations in the facility, and upon request and without charge by mail. The facility must also conspicuously display certain information regarding the FAP in public places at the facility's site. In addition, a hospital facility may (but is not required to) widely publicize its FAP using summaries that do not contain all of the information in the FAP, and to provide certain information updates separately from the FAP. The NPRM also mandates making a FAP plain language summary and the FAP application and instructions available in various circumstances, including prior to the patient's discharge from the hospital facility. For facilities serving communities with significant concentrations of individuals with limited proficiency in the English language (generally applicable if a non-English language is a primary language of more than 10% of the residents of the community served by the hospital facility), the NPRM requires the facility to make certain FAP related materials available in these other primary non-English languages.
5. **Determinations of FAP-Eligibility.** The NPRM contains certain rules regarding the FAP application process, assisting individuals with the FAP application process, and information that may be relied on by the hospital facility to make FAP-eligibility determinations. Financial assistance may not be denied an individual based on the omission of information or documentation if such information or documentation is not specifically required by the FAP or FAP application form. Under the proposed regulations, a hospital facility is prohibited from relying on signed waivers from an individual stating the individual will not seek financial assistance to determine whether the individual is FAP-eligible.
6. **Emergency Medical Care Policy.** Section 501(r)(4) requires a hospital organization to establish a written policy relating to emergency medical care. The emergency medical care policy must require the hospital organization to provide, without discrimination, care for emergency medical conditions to individuals regardless of their eligibility under the organization's FAP. The NPRM describes what a hospital facility must include in its written emergency medical care policy. The policy will generally satisfy this requirement if it requires the hospital facility to provide care for emergency medical conditions within the meaning of the Emergency Medical Treatment and Labor Act (EMTALA). The proposed regulations further provide that any hospital policy or procedure that discourages individuals from seeking emergency medical care may jeopardize a hospital's compliance with the requirement to establish a nondiscriminatory emergency medical care policy. This includes, for example, demanding that emergency department patients

pay before receiving treatment or permitting debt collection activities in the emergency department. Accordingly, the NPRM provides that the emergency medical care policy fails to satisfy section 501(r) unless the policy prohibits debt collection activities from occurring in the emergency department or in other hospital venues where such activities could interfere with the treatment of emergency medical conditions without discrimination.

7. Billing and Collection Policy. Each hospital facility is required to have a billing and collections policy, either as a stand-alone policy or as part of its FAP. The proposed regulations define the term "billing and collections policy" as a written policy that describes the actions a hospital facility may take in the event of nonpayment. This includes any actions, including extraordinary collections actions, the hospital facility or an authorized party may take related to obtaining payment of a bill for medical care provided by the facility. The policy must address the process and time frames the facility will use in taking actions relating to obtaining payment for medical care, the reasonable efforts the facility will take to determine an individual's eligibility for financial assistance, and the persons responsible for determining when extraordinary collections actions may be taken.
8. Establishing a FAP, Emergency Medical Care Policy, or Separate Billing and Collection Policy. A FAP, separate billing and collection policy, or emergency medical care policy, is established only if the policy has been adopted by an authorized body of the hospital organization for the hospital facility and the facility has implemented the policy. For this purpose, an authorized body means the hospital organization's board of directors or trustees or equivalent controlling body, a committee of such body permitted under state law to act on behalf of the body, or other parties authorized by the governing body of the hospital organization to act on its behalf to the extent permitted under state law. This may include, for example, one or more executives of the hospital facility. Under the NPRM, a hospital facility has implemented a policy if it has consistently carried out such policy. A hospital organization may establish a single policy for multiple hospital facilities, although the written policy must describe different features and terms if they vary across facilities.
9. Prohibition Against Extraordinary Collection Actions. Section 501(r)(6) requires a hospital organization to make reasonable efforts to determine whether an individual is FAP-eligible before engaging in extraordinary collection actions (ECAs) against the individual. The NPRM describes the actions that are considered ECAs and the reasonable efforts a facility must make to determine FAP-eligibility before engaging in such ECAs. In general, an ECA includes any actions taken against an individual relating to payment of a bill for care covered under the facility's FAP that require a legal or judicial process, such as placing a lien or foreclosing on an individual's property, commencing a civil action against the individual, or garnishing the individual's wages. Selling an individual's debt to a third party and reporting adverse information to consumer credit reporting agencies or credit bureaus also constitute an ECA. The proposed regulations do not require a facility to obtain governing body approval before taking ECAs, although the actions must comport with the facility's billing and collections policy. The NPRM provides rules regarding agreements between the hospital facility and third parties who are sold or referred medical care debt, and actions a facility must take with respect to complete and incomplete FAP applications to satisfy the reasonable efforts requirements.

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10. Limitation on Charges to Amounts Generally Billed for Emergency Care and Other Medically Necessary Care. Section 501(r)(5) and the proposed regulations require a hospital organization to limit amounts charged for emergency or other medically necessary care provided to individuals eligible for assistance under the organization's FAP (FAP-eligible individuals) to not more than the amounts generally billed (AGB) to individuals who have insurance covering such care. The NPRM describes how a hospital facility determines the maximum amounts (that is, the AGB) it may charge FAP-eligible individuals for emergency and other medically necessary care. In general, the guidance allows a hospital facility to adopt either a look-back method (under which the AGBs must be revised at least annually) or a prospective method to determine AGB. For those facilities that adopt the look-back method, the NPRM provides flexibility to adopt a single AGB percentage for all care, or separate AGB percentages for certain components of care, but requires inclusion of Medicare claims and limits a facility's ability to take private health insurance claims into account for this purpose. The prospective method requires the facility to use the billing and coding process it would use if the individual were a Medicare fee-for-service beneficiary and setting the AGB amount at the amount the facility would expect to be paid by Medicare and the individual for such care. Under the NPRM, the facility must continue using the same AGB methods once they are adopted. The guidance also addresses what the facility may do if a FAP-eligible individual has not yet applied for financial assistance at the time charges are made, and how to make corrections to charges in the event an individual is later found to be FAP-eligible.
 11. Prohibition Against Gross Charges. Section 501(r) prohibits the use of gross charges. Under the statute, it was unclear whether the prohibition against gross charges applied to all individuals or only to those who are FAP-eligible. The NPRM eliminates the uncertainty and clarifies that the gross charges prohibition applies only to FAP-eligible individuals. The proposed regulations require a hospital facility to limit the amount charged for any medical care it provides to a FAP-eligible individual to less than the gross charges for that care. Thus, under the NPRM, a hospital facility may not charge the full amount of gross charges for any type of medical care provided to a FAP-eligible individual, regardless of whether the care is emergency or other medically necessary care. Under the proposed guidance, a hospital facility may use gross charges for any medical care provided to an individual who is not FAP-eligible, even if the care is emergency or other medically necessary care. The proposed regulations define gross charges (also known as the chargemaster rate) to mean the hospital facility's full, established price for medical care that the hospital facility consistently and uniformly charges all patients before applying any contractual allowances, discounts, or deductions. The NPRM permits the facility to include the gross charge amount on a hospital bill as the starting point to which various contractual allowances, discounts, or deductions are applied, provided that the gross charges are not the actual amount a FAP-eligible individual is expected to pay.
 12. Items for Which IRS has Requested Comments. The IRS and Treasury Department specifically requested public comments on over 20 different items in the NPRM. See attachment, *Areas for Which IRS has Requested Public Comments.*

As stated earlier, the NPRM is far-reaching and proposes rules which will have a significant impact on non-tax operational aspects of every hospital facility that is subject to these requirements.

Please contact any of the individuals listed below if you have any questions or comments regarding section 501(r) and the proposed guidance, or if you wish to provide input regarding the submission of comments to the IRS and Treasury Department regarding the NPRM.

For additional information, please contact a National Tax Services Exempt Organizations Tax Services Practice representative:

<i>Marcia Krause</i>	<i>202-414-1012</i>	<i>marci.k.krause@us.pwc.com</i>
<i>Rob Friz</i>	<i>267-330-6248</i>	<i>robert.w.friz@us.pwc.com</i>
<i>Travis Patton</i>	<i>202-414-1042</i>	<i>travis.patton@us.pwc.com</i>
<i>Gwen Spencer</i>	<i>617-530-4120</i>	<i>gwen.spencer@us.pwc.com</i>
<i>Laura Parello</i>	<i>646-471-2472</i>	<i>laura.j.parello@us.pwc.com</i>
<i>Howard Schoenfeld</i>	<i>202-414-1717</i>	<i>howard.schoenfeld@us.pwc.com</i>
<i>Ron Schultz</i>	<i>202-346-5096</i>	<i>ronald.j.schultz@us.pwc.com</i>
<i>Caroline Burnicki</i>	<i>617-530-5767</i>	<i>caroline.n.burnicki@us.pwc.com</i>
<i>Michelle Michalowski</i>	<i>202-414-1615</i>	<i>michelle.g.michalowski@us.pwc.com</i>
<i>Eric McNeil</i>	<i>267-330-6415</i>	<i>eric.m.mcneil@us.pwc.com</i>
<i>Erin Couture</i>	<i>617-530-6179</i>	<i>erin.couture@us.pwc.com</i>

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