
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



***Affordable Care Act: While Much Has
Been Accomplished, the Extent of Additional
Controls Needed to Implement Tax-Exempt
Hospital Provisions Is Uncertain***

June 21, 2012

Reference Number: 2012-13-070

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

Redaction Legend:

2(f) = Risk of Circumvention of Agency Regulation or Statute

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HIGHLIGHTS

AFFORDABLE CARE ACT: WHILE MUCH HAS BEEN ACCOMPLISHED, THE EXTENT OF ADDITIONAL CONTROLS NEEDED TO IMPLEMENT TAX-EXEMPT HOSPITAL PROVISIONS IS UNCERTAIN

Highlights

Final Report issued on June 21, 2012

Highlights of Reference Number: 2012-13-070 to the Internal Revenue Service Acting Commissioner, Tax Exempt and Government Entities Division.

IMPACT ON TAXPAYERS

The Patient Protection and Affordable Care Act (ACA) contains provisions that impact the IRS and tax-exempt hospital organizations. The IRS has made progress establishing controls to assess tax-exempt hospital organization compliance. However, additional work will be required once legal guidance is published. Until guidance is published, the public cannot be assured that the IRS has implemented all controls to ensure compliance with ACA provisions designed to protect those served by tax-exempt hospitals.

WHY TIGTA DID THE AUDIT

This audit was initiated as part of TIGTA's efforts to evaluate the IRS's plans for implementing the various ACA tax provisions. This review addresses the major management challenge of Implementing Health Care and Other Tax Law Changes. The overall objective was to evaluate the IRS's progress in establishing controls to determine whether tax-exempt hospitals comply with select provisions of the ACA.

WHAT TIGTA FOUND

The IRS has made progress establishing controls to determine whether tax-exempt hospitals comply with provisions of the ACA and has already opened reviews of the community benefit activities of approximately 1,700 health care organizations. However, it is difficult to determine at this point how much additional work will be required of the Exempt

Organizations function to fully implement controls because legal guidance has not been published. This guidance, which is currently under review, would provide the Exempt Organizations function with a basis for identifying additional controls needed to determine whether tax-exempt hospitals comply with the ACA.

In addition, the Department of the Treasury will be required in the near future to send its first annual report to Congress regarding tax-exempt hospitals. The IRS is responsible for working with the Department of Health and Human Services to gather the data for this report. While communication has been established, the format and timing of receipt of data have not been formalized.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Director, Exempt Organizations, work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services. The Memorandum of Understanding should take into consideration when information for the annual report to Congress should be received by the IRS and the proper format of the data to ensure it will be timely and usable for the report to Congress.

In response to our report, IRS management agreed with our recommendation. The IRS plans to work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services that takes into consideration when information for the annual report to Congress should be received and the proper format of the data to ensure it will be timely and usable for the report to Congress.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

June 21, 2012

MEMORANDUM FOR ACTING COMMISSIONER, TAX EXEMPT AND GOVERNMENT
ENTITIES DIVISION

FROM: Michael E. McKenney
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Affordable Care Act: While Much Has Been
Accomplished, the Extent of Additional Controls Needed to Implement
Tax-Exempt Hospital Provisions Is Uncertain (Audit # 201110317)

This report presents the results of our review of the Internal Revenue Service's (IRS) progress in establishing controls to determine whether tax-exempt hospitals comply with Section 9007 of the Patient Protection and Affordable Care Act.¹ This review is included in our Fiscal Year 2012 Annual Audit Plan and addresses the major management challenge of Implementing Health Care and Other Tax Law Changes.

Management's complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the IRS managers affected by the report recommendation. Please contact me at (202) 622-6510 if you have questions or Russell P. Martin, Acting Assistant Inspector General for Audit (Management Services and Exempt Organizations), at (202) 622-8500.

¹ Pub. L. No. 111-148, 124 Stat. 119 (2010) (codified as amended in scattered sections of the U.S. Code), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029.



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Abbreviations

ACA	Patient Protection and Affordable Care Act
EO	Exempt Organizations
IRS	Internal Revenue Service



Affordable Care Act: While Much Has Been Accomplished, the Extent of Additional Controls Needed to Implement Tax-Exempt Hospital Provisions Is Uncertain

Background

The Patient Protection and Affordable Care Act¹ (ACA) contains provisions that impact the Internal Revenue Service (IRS) and tax-exempt hospital organizations covered under Internal Revenue Code Section (§) 501(c)(3).² Charities, educational institutions, and religious organizations are among those entities exempt from Federal income tax under § 501(c)(3). Although tax-exempt hospitals are not specifically listed in this Code section, they have long been recognized as charitable organizations when certain conditions are met. Specifically, a hospital must be organized and operated exclusively for charitable purposes, and may not be operated, directly or indirectly, for the benefit of private interests.

In addition to complying with the requirements of § 501(c)(3), tax-exempt hospitals must also satisfy four new exemption requirements in § 9007(a) of the ACA.³ Specifically, hospital organizations must:

1. Conduct a Community Health Needs Assessment every three years and adopt an implementation strategy to meet the community health needs.
2. Establish a written financial assistance policy and a written policy requiring the organization to provide care for emergency medical conditions to individuals regardless of their eligibility under the financial assistance policy.
3. Limit amounts charged for emergency or other medically necessary care that is provided to individuals eligible for assistance under the organization's financial assistance policy.
4. Forego extraordinary collection actions against an individual before the organization has made reasonable efforts to determine whether the individual is eligible for assistance under the hospital organization's financial assistance policy.

The ACA requires tax-exempt hospitals to satisfy four new requirements to keep their tax-exempt status.

111TH CONGRESS } LEGISLATIVE COUNSEL { PRINT 111-1
2d Session

COMPILATION OF PATIENT PROTECTION
AND AFFORDABLE CARE ACT

[As Amended Through May 1, 2010]

INCLUDING
PATIENT PROTECTION AND AFFORDABLE CARE ACT
HEALTH-RELATED PORTIONS OF THE HEALTH CARE AND
EDUCATION RECONCILIATION ACT OF 2010

¹ Pub. L. No. 111-148, 124 Stat. 119 (2010), (codified as amended in scattered sections of the U.S. Code), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029.

² I.R.C. § 501(c)(3) (2006).

³ § 9007(a) of the ACA added § 501(r) to the Internal Revenue Code, which imposes four new requirements a hospital organization must meet to qualify for tax exemption in tax years beginning after March 23, 2010. See Appendix IV for additional information on requirements of the ACA.



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In addition, the IRS is required to review community benefit activities of each hospital organization at least once every three years for each hospital organization described in § 501(r). These reviews include items such as whether the hospital facility meets the community health needs assessment, the financial assistance policy, the limitation of charges, and the billing and collection requirements. Also, § 9007 of the ACA requires the Secretary of the Treasury, in consultation with the Secretary of Health and Human Services, to submit an annual report to Congress on the level of charity care, bad debt expenses, and the unreimbursed costs of means-tested⁴ and non-means-tested government programs.

The Department of Health and Human Services is responsible for the administration of health care policy issue changes, and the IRS is responsible for implementation of tax law changes included in the legislation. Implementing new tax law legislation requires changes to communications, guidance, employee training, education and outreach, and forms and publications. It also requires designing a program to ensure hospitals comply with the changes. The IRS's Exempt Organizations (EO) function within the Tax Exempt and Government Entities Division is responsible for ensuring that tax-exempt hospitals comply with § 9007 of the ACA.

This review focused on ACA provisions impacting tax-exempt hospitals and the IRS and did not encompass a review of all ACA provisions. As we were concluding our fieldwork in January 2012, new regulations affecting tax-exempt hospitals were not finalized. This review was performed at the EO function, Tax Exempt and Government Entities Division Headquarters, in Washington, D.C., during the period August 2011 through January 2012. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

The Department of Health and Human Services is responsible for health care policy issue changes, and the IRS is responsible for tax law changes involving the ACA.



⁴ A "means-tested government program" is a government program for which eligibility depends on the recipient's income or asset level.



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Results of Review

The IRS has made progress establishing controls to determine whether tax-exempt hospitals comply with provisions of the ACA and has already opened reviews of the community benefit activities of approximately 1,700 health care organizations. However, it is difficult to determine at this point how much additional work will be required of the EO function to fully implement controls because legal guidance has not been published. This guidance, which is currently under review, would provide the EO function with a basis for identifying additional controls needed to determine whether tax-exempt hospitals comply with the ACA. Until guidance is published, the public cannot be assured that the IRS has implemented all controls to ensure tax-exempt hospital compliance with ACA provisions designed to protect those served by these hospitals.

In addition, the Department of the Treasury will be required in the near future to send its first annual report to Congress regarding tax-exempt hospitals. The IRS is responsible for working with the Department of Health and Human Services to gather the data for this report. While communication has been established, the format and timing of receipt of data have not been formalized. Because the IRS does not have experience working with this data and may need to quickly assemble the information, we believe the IRS should work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services regarding data needs.

Initial Controls Have Been Established, but Additional Work Is Planned After Legal Guidance Is Published

After the ACA was enacted, EO function employees participated on teams that identified issues affecting tax-exempt hospitals and developed action plans to address the new requirements. This included 1) establishing a process to identify the population of tax-exempt hospitals affected by the legislation, 2) conducting community benefit reviews of tax-exempt hospitals, 3) making changes to forms, 4) developing and conducting training of IRS employees, 5) educating the tax-exempt hospital community about new ACA requirements, and 6) soliciting comments from the tax-exempt sector and collaborating with IRS Counsel on new regulations. Specifically, the following actions were taken:

Identification of tax-exempt hospitals

Prior to passage of the ACA, the IRS did not maintain a database that identified all tax-exempt hospitals. Therefore, the EO function organized an effort to identify the universe of tax-exempt hospitals. This was significant because the IRS needs to know the universe of tax-exempt hospitals to be able to conduct community benefit reviews of every tax-exempt hospital at least



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once every three years, as required by the ACA. The EO function accomplished this by reviewing information from its own Return Inventory and Classification System;⁵ a Medicare/Medicaid Internet website that contains hospital names, addresses, and ownership information; and State and District of Columbia Internet websites containing licensed and registered hospitals. This manual, labor-intensive process involved seven employees and took approximately 1.5 years to identify the universe of 3,377 tax-exempt hospitals. This effort will need to continue due to hospital mergers and the creation of new hospitals. IRS management plans to add an indicator to the Master File⁶ in Fiscal Year⁷ 2013 to make identification of tax-exempt hospitals easier in the future.

The EO function identified from various sources more than 3,300 tax-exempt hospitals that are subject to new tax-exemption requirements.



Reviews of community benefit activities

The EO function developed a method to review the community benefit activities of tax-exempt hospitals. A review of each tax-exempt hospital is required to be conducted once every three years. The IRS will conduct these reviews in phases over three years. Phase one is complete and covered approximately 1,700 health care organizations.⁸ A lead sheet was created to document the results of the examiner's review of the community benefit activities and a Microsoft Office Access database was created to track the data from the lead sheets. As part of the review, the examiner may recommend an ACA-related or non-ACA-related compliance check⁹ or examination. At the conclusion of our audit, examiners had not recommended any compliance checks or examinations related to ACA provisions.¹⁰

⁵ This computer system provides access to return and filer information related to the filing and processing of tax-exempt organization returns.

⁶ The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

⁷ A 12-consecutive-month period ending on the last day of any month, except December. The Federal Government's fiscal year begins on October 1 and ends on September 30.

⁸ We did not review any of the approximately 1,700 ACA community benefit reviews completed by the EO function.

⁹ A compliance check is a contact with a tax-exempt organization that involves a review of filed information and tax returns of the entity. A compliance check does not directly relate to determining a tax liability for any particular tax period, and a tax-exempt organization may legally choose not to participate in a compliance check.

¹⁰ Eight non-ACA examinations and two non-ACA compliance checks were recommended. These 10 referrals involve other areas of tax law including filing requirements and taxable income.



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Changes to forms

Form 990, *Return of Organization Exempt From Income Tax*, Schedule H, *Hospitals*, was revised for Tax Year¹¹ 2010 because § 9007 of the ACA requires a hospital organization to meet four additional exemption requirements for each of its hospital facilities.¹² Specifically,

1. Part V, Section A (Hospital Facilities) was added to require hospital organizations to list each of their hospital facilities that, at any time during the tax year, were required to be licensed, registered, or similarly recognized as a hospital under State law.
2. Part V, Section B (Facility Policies and Practices) was added to gather information on hospital organizations' compliance with the four additional exemption requirements of § 9007. The hospital organization must complete a separate Section B (Facility Policies and Practices) for each of its hospital facilities listed in Part V Section A. Section B was optional for Tax Year 2010.
3. Part V, Section C (Other Health Care Facilities That Are Not Licensed, Registered, or Similarly Recognized as a Hospital Facility) was added to require the hospital organization to list all of its non-hospital health care facilities that it operated during the tax year, whether or not such facilities were required to be licensed or registered under State law.

In addition, an automated process was developed to identify Forms 990 that are received at an IRS campus¹³ with incomplete information on Schedule H. When incomplete forms are identified, Wage and Investment Division¹⁴ employees at the campus will correspond with the tax-exempt hospitals to obtain the missing data. EO function employees that conduct community benefit reviews of tax-exempt hospital organizations also manually review the data entered by tax-exempt hospitals on Schedule H and check publicly available sources, ***2(f)*****
*****2(f)*****.

IRS employee training

The EO function developed training materials and offered training sessions related to § 9007 of the ACA and how it affects the EO function. Topics included an introduction to tax-exempt hospitals, the four new exemption requirements, and new information required for the revised Form 990, Schedule H. General training sessions were held for all EO function employees and

¹¹ A 12-month accounting period for keeping records on income and expenses used as the basis for calculating the annual taxes due. For most individual taxpayers, the tax year is synonymous with the calendar year.

¹² See Appendix V for a copy of the revised Form 990, Schedule H, Part V.

¹³ The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

¹⁴ The IRS is organized into divisions serving groups of taxpayers. The IRS's four divisions include the Tax Exempt and Government Entities, the Large Business and International, the Wage and Investment, and the Small Business/Self-Employed Divisions.



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more detailed training sessions were offered to those employees who review applications for tax-exempt status and examine returns filed by tax-exempt organizations.

Tax-exempt hospital community education

To help educate the hospital community on the Form 990, Schedule H changes, the Tax Exempt and Government Entities Division presented webinars to health associations in Fiscal Years 2010, 2011, and 2012. These webinars included discussions on changes to the Form 990, Schedule H, Part V and presented the attendees with various resources, including a website address, for additional information. The IRS also established a link on its Internet website (IRS.gov) directing tax-exempt customers to an ACA Tax Provision Internet web page. This web page contains links to the various provisions within the ACA, including a section on the additional requirements for tax-exempt hospitals.

Public comments and new regulations

Part of the process of assuring compliance with legal guidelines is translating the specifics of new legislation into detailed regulations, rules, and procedures that provide guidance to IRS customers. Regulations interpret and give directions on complying with the law, but are first published in proposed form in a Notice of Proposed Rulemaking.¹⁵ After public input is fully considered, final or temporary regulations are published in the Federal Register.¹⁶ To obtain comments from the tax-exempt sector and begin providing guidance on ACA provisions concerning tax-exempt hospitals, the IRS issued three notices.

The IRS provided guidance and solicited comments from the tax-exempt hospital sector by issuing notices.



1. Notice 2010-39, *Request for Comments Regarding Additional Requirements for Tax-Exempt Hospitals*, was issued on May 27, 2010. The purpose of the Notice was to solicit comments on requirements for the Community Health Needs Assessment, Financial Assistance Policy, Limitation on Charges, and Billing and Collection. Comments were due to the IRS by July 22, 2010.

¹⁵ A form of IRS guidance which is a public pronouncement that may contain guidance that involves substantive interpretations of the Internal Revenue Code or other provisions of the law. According to IRS Counsel, taxpayers generally may not rely on proposed regulations for planning purposes, except if there are no applicable final or temporary regulations in force and there is an express statement in the proposed regulations that taxpayers may rely on them currently.

¹⁶ The Federal Register is the official daily publication for rules, proposed rules, and notices of Federal agencies and organizations, as well as executive orders and other presidential documents.



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2. Notice 2011-52, *Notice and Request for Comments Regarding the Community Health Needs Assessment Requirements for Tax-exempt Hospitals*, was issued on July 7, 2011. Customer comments from Notice 2010-39 were considered when developing Notice 2011-52. The purpose of Notice 2011-52 was to describe Community Health Needs Assessment requirements that the Department of the Treasury and the IRS anticipate will be included in draft regulations, solicit additional Community Health Needs Assessment comments, and allow hospitals to start the process of conducting a Community Health Needs Assessment and developing implementation strategies in advance of the effective date.

As shown in Figure 1, the IRS provided guidance on the following topics.

Figure 1: Analysis of Guidance Provided in Notice 2011-52

Guidance Topics Where the IRS Requested General Public Comments
Documentation of a Community Health Needs Assessment.
Excise tax on failures to meet the Community Health Needs Assessment requirements.
Reporting requirements (changes to Form 990) related to Community Health Needs Assessments.
Effective date for hospital organizations to conduct a Community Health Needs Assessment and adopt an implementation strategy is the last day of its first taxable year beginning after March 23, 2012.
Guidance Topics Where the IRS Requested Specific Public Comments
Hospital organizations required to meet the Community Health Needs Assessment requirements.
How Community Health Needs Assessments and implementation strategies should be implemented for hospital organizations with multiple hospital facilities.
How and when a Community Health Needs Assessment is “conducted.” ¹⁷
Defining community served by a hospital facility.
Defining persons who represent the broad interests of the community.
Making a Community Health Needs Assessment widely available to the public.

¹⁷ A Community Health Needs Assessment is considered conducted in the taxable year that the written report of its findings is made widely available to the public.



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Guidance Topics Where the IRS Requested Specific Public Comment

Implementation strategy for Community Health Needs Assessments.

How and when an implementation strategy should be adopted.

Source: Treasury Inspector General for Tax Administration analysis of Notice 2011-52.

Although the IRS did not request specific comments on four topics for Notice 2011-52, if received, the comments would be considered. Public comments for Notice 2011-52 were due to the IRS by September 23, 2011, and were still under review at the conclusion of our audit work.

3. Notice 2012-4, *Certain Filing Changes for Tax-Exempt Organizations*, was issued on January 17, 2012, to notify tax-exempt hospital organizations that beginning with Tax Year 2011, Form 990, Schedule H, Part V, Section B (Part V.B.)¹⁸ is no longer optional, with the exception of lines 1 through 7.¹⁹ The IRS has considered public input received regarding Part V.B., and has made revisions for Tax Year 2011, and will consider additional revisions in the future.

Regulations are in draft form to address three of the four new exemption requirements including: 1) Financial Assistance and Emergency Medical Care; 2) Limitation on Charges; and 3) Billing and Collection Practices Requirements. Additionally, the regulations will address the definition of a hospital facility and a hospital organization. These draft regulations are currently being reviewed. Until the regulations are published, IRS management cannot complete training for examination employees and cannot revise examination programs to determine if tax-exempt hospitals comply with the ACA. Because the IRS has not fully developed controls, we cannot determine if the controls will be adequate to identify tax-exempt hospitals noncompliant with the ACA or if there may be gaps in coverage between the IRS and the Department of Health and Human Services that would result in not satisfying the intent of Congress.

¹⁸ Schedule H must be completed by an organization that operated at least one hospital facility during the tax year. A hospital facility includes any facility that is, or is required to be, licensed, registered, or similarly recognized as a hospital under State law, and any other organization that the Secretary of the Treasury determines has the provision of hospital care as its principal function or purpose constituting the basis for its tax-exempt status under § 501(c)(3), without regard to § 501(r).

¹⁹ Form 990, Schedule H, Part V, Section B, lines 1 through 7 pertain to the Community Health Needs Assessment, which are effective only for tax years beginning after March 23, 2012. However, some hospital organizations may have tax years that start before March 23, 2012. Therefore, lines 1 through 7 are not mandatory for all hospital organizations for Tax Year 2012.



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Formal Agreements Have Not Been Negotiated Regarding Data Needs for the Annual Report to Congress

EO function management stated that the IRS will be responsible for submitting to the Department of the Treasury information for the annual report to Congress on the level of charity care, bad debt expense, and unreimbursed costs of means-tested and non-means-tested government programs. The Department of Health and Human Services will provide this information to the IRS for the annual report. Although EO function management has coordinated with the Department of Health and Human Services to obtain this information, the EO function has no control over the timing of receipt or format of the information.

EO function management has set a goal of August 2012 for submitting information to the Department of the Treasury for the first report. In order to meet this timeline, the IRS needs to receive input from the Department of Health and Human Services in July 2012. In addition, because the EO function is not familiar with the Department of Health and Human Services data, this information needs to be received in a format where it can be inserted into the report with minimal analysis or manipulation by the EO function. If this data are not received timely or in a proper format, the report to Congress could either be late or contain inaccurate information on the level of charity care, bad debt expenses, and the unreimbursed costs of means-tested and non-means-tested government programs.

A formalized agreement between the Department of the Treasury and the Department of Health and Human Services on data needs would assist the IRS in gathering and assembling data for the annual report to Congress.



Recommendation

Recommendation 1: The Director, EO, should work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services. The Memorandum of Understanding should take into consideration when information for the annual report to Congress should be received and the proper format of the data to ensure it will be timely and usable for the report to Congress.

Management's Response: IRS management agreed with this recommendation. IRS management plans to work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services that takes into consideration when information for the annual report to Congress should be received and the proper format of the data to ensure it will be timely and usable for the report to Congress.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to evaluate the IRS's progress in establishing controls to determine whether tax-exempt hospitals comply with § 9007 of the ACA.

- I. Identified provisions within § 9007 of the ACA that impact tax-exempt hospitals.
- II. Identified controls established by IRS management to determine whether tax-exempt hospitals comply with § 9007 of the ACA.
 - A. Through discussions with Tax Exempt and Government Entities Division management, identified actions planned or taken to implement § 9007 of the ACA.
 - B. Reviewed the Legislative Analysis, Tracking, and Implementation Services¹ action plan to identify steps planned or taken to implement § 9007 of the ACA.
 - C. Determined whether a Memorandum of Understanding was developed with the Department of Health and Human Services outlining responsibility for § 9007 of the ACA.
 - D. Assessed the IRS's plans to identify the universe of tax-exempt hospitals covered by § 9007 of the ACA.
 - E. Determined the status of implementing the Community Health Needs Assessment provision of the ACA (effective date after March 23, 2012) that impacts tax-exempt hospitals.
 - F. Determined the status of implementing the financial assistance and emergency medical care requirements of the ACA (effective date after March 23, 2010) that impacts tax-exempt hospitals.
 - G. Determined the status of implementing the limitation on charges requirements of the ACA (effective date after March 23, 2010) that impacts tax-exempt hospitals.
 - H. Determined the status of implementing the billing and collection requirements of the ACA (effective date after March 23, 2010) that impacts tax-exempt hospitals.
 - I. Identified the status of the IRS's efforts to review community benefits activities (effective date after March 23, 2010) that impacts tax-exempt hospitals.

¹ Legislative Analysis, Tracking, and Implementation Services is responsible for managing the agency-wide implementation planning and monitoring of legislation having a significant impact on the IRS.



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Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: IRS Notices, action plans, changes to Form 990, *Return of Organization Exempt From Income Tax*, and training materials. We evaluated these controls by reviewing and analyzing documentation and interviewing IRS management.



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Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Acting Deputy Commissioner, Tax Exempt and Government Entities Division SE:T
Director, Exempt Organizations, Tax Exempt and Government Entities Division SE:T:EO
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Director, Communications and Liaison, Tax Exempt and Government Entities
Division SE:T:CL



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Appendix IV

Patient Protection and Affordable Care Act Provisions Affecting Tax-Exempt Hospitals and the Internal Revenue Service

The Patient Protection and Affordable Care Act¹ (ACA) contains provisions that impact the IRS and tax-exempt hospital organizations. Figures 1 and 2 provide four new requirements impacting tax-exempt hospitals and two new requirements impacting the IRS concerning ACA tax-exempt hospital provisions.

Figure 1: ACA Provisions Impacting Tax-Exempt Hospitals

Requirement #1	
Community Health Needs Assessment	<p>A hospital organization is required to conduct a Community Health Needs Assessment every three years and adopt an implementation strategy to meet the community health needs identified through such assessment. The Community Health Needs Assessment must take into account input from persons who represent the broad interests of the community served by the hospital facility, including those with special knowledge of or expertise in public health, and must be made widely available to the public. The effective date is taxable years after March 23, 2012.</p> <p>Hospital organizations are responsible for defining their community on Schedule H, <i>Hospitals</i>, of Form 990, <i>Return of Organization Exempt From Income Tax</i>. The IRS has determined that hospital organizations do not define their communities consistently. In July 2011, the IRS issued Notice 2011-52, <i>Notice and Request for Comments Regarding the Community Health Needs Assessment Requirements for Tax-exempt Hospitals</i>, describing specific provisions related to the Community Health Needs Assessment requirements and requesting comments on these provisions. Hospital organizations could submit comments on or before September 23, 2011. The IRS is considering the comments it received in response to Notice 2011-52 as it works on further guidance on the Community Health Needs Assessment requirements.</p> <p>Hospital organizations that fail to meet the Community Health Needs Assessment requirements for any taxable year will be subject to a \$50,000 excise tax.²</p>

¹ Pub. L. No. 111-148, 124 Stat. 119 (2010), (codified as amended in scattered sections of the U.S. Code), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029.

² § 9007(b) of the ACA added § 4959 to the Internal Revenue Code, which imposes an excise tax for failures to meet the Community Health Needs Assessment requirement of § 501(r)(3). Hospital organizations will be charged for each violation, on a facility by facility basis.



Affordable Care Act: While Much Has Been Accomplished, the Extent of Additional Controls Needed to Implement Tax-Exempt Hospital Provisions Is Uncertain

Requirement #2	
Policies for Financial Assistance and Emergency Medical Care	<p>Hospital organizations are required to establish a written financial assistance policy that includes the following:</p> <ul style="list-style-type: none"> • Eligibility criteria for financial assistance and whether such assistance includes free or discounted care. • The basis for calculating amounts charged to patients. • The method of applying for financial assistance. • In the case of an organization that does not have a separate billing and collections policy, the actions the organization may take in the event of nonpayment, including collections action and reporting to credit agencies. • Measures to widely publicize the policy within their hospital community. <p>Additionally, hospital organizations are required to have a written policy requiring the organization to provide, without discrimination, care for emergency medical conditions to individuals regardless of their eligibility under the financial assistance policy.</p>
Requirement #3	
Limitation on Charges	<p>Hospital organizations are required to limit amounts charged for emergency or other medically necessary care that is provided to individuals eligible for assistance under the organization’s financial assistance policy to not more than the amounts generally billed to individuals who have insurance covering such care. Additionally, hospital organizations are prohibited from using gross charges.</p>
Requirement #4	
Billing and Collection	<p>Hospital organizations are required to forego extraordinary collection actions against an individual before the organization has made reasonable efforts to determine whether the individual is eligible for assistance under the hospital organization’s financial assistance policy. Extraordinary collection actions include lawsuits, liens on residences, arrests, or other similar collection processes.</p>

Source: Treasury Inspector General for Tax Administration analysis of ACA provisions impacting tax-exempt hospitals.



Affordable Care Act: While Much Has Been Accomplished, the Extent of Additional Controls Needed to Implement Tax-Exempt Hospital Provisions Is Uncertain

Figure 2: ACA Provisions Impacting the IRS

Requirement #1	
Community Benefit Activities	The IRS must review the community benefit activities of each hospital organization at least once every three years. In Revenue Ruling 69-545, ³ the IRS recognized that the promotion of health is considered to be a charitable purpose under the general law of charity. The community benefit standard is the test used by the IRS for determining whether a hospital is organized and operated for the charitable purpose of promoting health. A hospital generally will meet the community benefit standard if it has a board of directors composed of prominent citizens drawn from the community; has a medical staff consistent with the size and nature of its facilities that is open to all qualified physicians in the area; operates a full-time emergency room open to all persons without regard to their ability to pay; and provides hospital care for everyone in the community able to pay the cost either themselves, through private health insurance, or with the aid of public programs such as Medicare.
Requirement #2	
Charity Care Report	The Secretary of the Treasury, in consultation with the Secretary of Health and Human Services, shall submit an annual report to Congress on the levels of charity care, bad-debt expenses, and the unreimbursed costs for services provided with respect to means-tested and non-means-tested government programs; and information with respect to private tax-exempt hospitals regarding costs incurred for community benefit activities. Additionally, no later than five years after enactment of the ACA (March 23, 2010), the Secretary of the Treasury, in consultation with the Secretary of Health and Human Services, shall conduct a study and submit a report on trends identified from the annual reports.

Source: Treasury Inspector General for Tax Administration analysis of ACA tax-exempt hospital provisions impacting the IRS.

³ Rev. Rul. 69-545, 1969-2 C.B. 117.



Affordable Care Act: While Much Has Been Accomplished, the Extent of Additional Controls Needed to Implement Tax-Exempt Hospital Provisions Is Uncertain

Appendix V

Revised Return of Organization Exempt From Income Tax, Schedule H, Hospitals, Part V

Schedule H (Form 990) 2011

Page **3**

Part V Facility Information

Section A. Hospital Facilities

(list in order of size, from largest to smallest)

How many hospital facilities did the organization operate during the tax year? _____

Name and address	Licensed hospital	General medical & surgical	Children's hospital	Teaching hospital	Critical access hospital	Research facility	ER-24 hours	ER-other	Other (describe)
1									
2									
3									
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									
16									

Schedule H (Form 990) 2011



**Affordable Care Act: While Much Has Been Accomplished, the
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Part V Facility Information (continued)

Section B. Facility Policies and Practices

(Complete a separate Section B for each of the hospital facilities listed in Part V, Section A)

Name of Hospital Facility: _____

Line Number of Hospital Facility (from Schedule H, Part V, Section A): _____

	Yes	No
Community Health Needs Assessment (Lines 1 through 7 are optional for tax year 2011)		
1 During the tax year or any prior tax year, did the hospital facility conduct a community health needs assessment (Needs Assessment)? If "No," skip to line 8	1	
If "Yes," indicate what the Needs Assessment describes (check all that apply):		
a <input type="checkbox"/> A definition of the community served by the hospital facility		
b <input type="checkbox"/> Demographics of the community		
c <input type="checkbox"/> Existing health care facilities and resources within the community that are available to respond to the health needs of the community		
d <input type="checkbox"/> How data was obtained		
e <input type="checkbox"/> The health needs of the community		
f <input type="checkbox"/> Primary and chronic disease needs and other health issues of uninsured persons, low-income persons, and minority groups		
g <input type="checkbox"/> The process for identifying and prioritizing community health needs and services to meet the community health needs		
h <input type="checkbox"/> The process for consulting with persons representing the community's interests		
i <input type="checkbox"/> Information gaps that limit the hospital facility's ability to assess the community's health needs		
j <input type="checkbox"/> Other (describe in Part VI)		
2 Indicate the tax year the hospital facility last conducted a Needs Assessment: 20__ __		
3 In conducting its most recent Needs Assessment, did the hospital facility take into account input from persons who represent the community served by the hospital facility? If "Yes," describe in Part VI how the hospital facility took into account input from persons who represent the community, and identify the persons the hospital facility consulted	3	
4 Was the hospital facility's Needs Assessment conducted with one or more other hospital facilities? If "Yes," list the other hospital facilities in Part VI	4	
5 Did the hospital facility make its Needs Assessment widely available to the public?	5	
If "Yes," indicate how the Needs Assessment was made widely available (check all that apply):		
a <input type="checkbox"/> Hospital facility's website		
b <input type="checkbox"/> Available upon request from the hospital facility		
c <input type="checkbox"/> Other (describe in Part VI)		
6 If the hospital facility addressed needs identified in its most recently conducted Needs Assessment, indicate how (check all that apply):		
a <input type="checkbox"/> Adoption of an implementation strategy to address the health needs of the hospital facility's community		
b <input type="checkbox"/> Execution of the implementation strategy		
c <input type="checkbox"/> Participation in the development of a community-wide community benefit plan		
d <input type="checkbox"/> Participation in the execution of a community-wide community benefit plan		
e <input type="checkbox"/> Inclusion of a community benefit section in operational plans		
f <input type="checkbox"/> Adoption of a budget for provision of services that address the needs identified in the Needs Assessment		
g <input type="checkbox"/> Prioritization of health needs in its community		
h <input type="checkbox"/> Prioritization of services that the hospital facility will undertake to meet health needs in its community		
i <input type="checkbox"/> Other (describe in Part VI)		
7 Did the hospital facility address all of the needs identified in its most recently conducted Needs Assessment? If "No," explain in Part VI which needs it has not addressed and the reasons why it has not addressed such needs	7	
Financial Assistance Policy		
Did the hospital facility have in place during the tax year a written financial assistance policy that:		
8 Explained eligibility criteria for financial assistance, and whether such assistance includes free or discounted care?	8	
9 Used federal poverty guidelines (FPG) to determine eligibility for providing free care?	9	
If "Yes," indicate the FPG family income limit for eligibility for free care: __ __ %		
If "No," explain in Part VI the criteria the hospital facility used.		



**Affordable Care Act: While Much Has Been Accomplished, the
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Part V Facility Information (continued)

		Yes	No
10	Used FPG to determine eligibility for providing <i>discounted</i> care? If "Yes," indicate the FPG family income limit for eligibility for discounted care: ___ % If "No," explain in Part VI the criteria the hospital facility used.	10	
11	Explained the basis for calculating amounts charged to patients? If "Yes," indicate the factors used in determining such amounts (check all that apply): a <input type="checkbox"/> Income level b <input type="checkbox"/> Asset level c <input type="checkbox"/> Medical indigency d <input type="checkbox"/> Insurance status e <input type="checkbox"/> Uninsured discount f <input type="checkbox"/> Medicaid/Medicare g <input type="checkbox"/> State regulation h <input type="checkbox"/> Other (describe in Part VI)	11	
12	Explained the method for applying for financial assistance?	12	
13	Included measures to publicize the policy within the community served by the hospital facility? If "Yes," indicate how the hospital facility publicized the policy (check all that apply): a <input type="checkbox"/> The policy was posted on the hospital facility's website b <input type="checkbox"/> The policy was attached to billing invoices c <input type="checkbox"/> The policy was posted in the hospital facility's emergency rooms or waiting rooms d <input type="checkbox"/> The policy was posted in the hospital facility's admissions offices e <input type="checkbox"/> The policy was provided, in writing, to patients on admission to the hospital facility f <input type="checkbox"/> The policy was available on request g <input type="checkbox"/> Other (describe in Part VI)	13	

Billing and Collections

14	Did the hospital facility have in place during the tax year a separate billing and collections policy, or a written financial assistance policy (FAP) that explained actions the hospital facility may take upon non-payment?	14	
15	Check all of the following actions against an individual that were permitted under the hospital facility's policies during the tax year before making reasonable efforts to determine the patient's eligibility under the facility's FAP: a <input type="checkbox"/> Reporting to credit agency b <input type="checkbox"/> Lawsuits c <input type="checkbox"/> Liens on residences d <input type="checkbox"/> Body attachments e <input type="checkbox"/> Other similar actions (describe in Part VI)	15	
16	Did the hospital facility or an authorized third party perform any of the following actions during the tax year before making reasonable efforts to determine the patient's eligibility under the facility's FAP? If "Yes," check all actions in which the hospital facility or a third party engaged: a <input type="checkbox"/> Reporting to credit agency b <input type="checkbox"/> Lawsuits c <input type="checkbox"/> Liens on residences d <input type="checkbox"/> Body attachments e <input type="checkbox"/> Other similar actions (describe in Part VI)	16	
17	Indicate which efforts the hospital facility made before initiating any of the actions checked in line 16 (check all that apply): a <input type="checkbox"/> Notified patients of the financial assistance policy on admission b <input type="checkbox"/> Notified patients of the financial assistance policy prior to discharge c <input type="checkbox"/> Notified patients of the financial assistance policy in communications with the patients regarding the patients' bills d <input type="checkbox"/> Documented its determination of whether patients were eligible for financial assistance under the hospital facility's financial assistance policy e <input type="checkbox"/> Other (describe in Part VI)	17	



**Affordable Care Act: While Much Has Been Accomplished, the
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Part V Facility Information (continued)

Policy Relating to Emergency Medical Care

		Yes	No
18 Did the hospital facility have in place during the tax year a written policy relating to emergency medical care that requires the hospital facility to provide, without discrimination, care for emergency medical conditions to individuals regardless of their eligibility under the hospital facility's financial assistance policy? If "No," indicate why: a <input type="checkbox"/> The hospital facility did not provide care for any emergency medical conditions b <input type="checkbox"/> The hospital facility's policy was not in writing c <input type="checkbox"/> The hospital facility limited who was eligible to receive care for emergency medical conditions (describe in Part VI) d <input type="checkbox"/> Other (describe in Part VI)	18		

Individuals Eligible for Financial Assistance

19 Indicate how the hospital facility determined, during the tax year, the maximum amounts that can be charged to FAP-eligible individuals for emergency or other medically necessary care. a <input type="checkbox"/> The hospital facility used its lowest negotiated commercial insurance rate when calculating the maximum amounts that can be charged b <input type="checkbox"/> The hospital facility used the average of its three lowest negotiated commercial insurance rates when calculating the maximum amounts that can be charged c <input type="checkbox"/> The hospital facility used the Medicare rates when calculating the maximum amounts that can be charged d <input type="checkbox"/> Other (describe in Part VI)			
20 Did the hospital facility charge any of its patients who were eligible for assistance under the hospital facility's financial assistance policy, and to whom the hospital facility provided emergency or other medically necessary services, more than the amounts generally billed to individuals who had insurance covering such care? If "Yes," explain in Part VI.	20		
21 Did the hospital facility charge any of its FAP-eligible patients an amount equal to the gross charge for any service provided to that patient? If "Yes," explain in Part VI.	21		



**Affordable Care Act: While Much Has Been Accomplished, the
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Part V Facility Information *(continued)*

Section C. Other Health Care Facilities That Are Not Licensed, Registered, or Similarly Recognized as a Hospital Facility

(list in order of size, from largest to smallest)

How many non-hospital health care facilities did the organization operate during the tax year? _____

Name and address	Type of Facility (describe)
1	
2	
3	
4	
5	
6	
7	
8	
9	
10	

Schedule H (Form 990) 2011



**Affordable Care Act: While Much Has Been Accomplished, the
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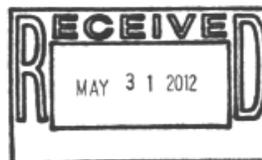
Appendix VI

Management's Response to the Draft Report

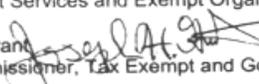


DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

May 31, 2012



MEMORANDUM FOR MICHAEL R. PHILLIPS
ACTING ASSISTANT INSPECTOR GENERAL FOR AUDIT
(Management Services and Exempt Organizations)

FROM: Joseph H. Grant 
Acting Commissioner, Tax Exempt and Government Entities

SUBJECT: Draft Audit Report - Affordable Care Act: While Much Has Been
Accomplished, the Extent of Additional Controls Needed to
Implement Tax-Exempt Hospital Provisions Is Uncertain
(Audit # 201110317)

Thank you for the opportunity to review your report on our implementation of the provisions of the Affordable Care Act (ACA) related to tax-exempt hospitals.

We appreciate your acknowledgement of the progress we have made to implement section 9007 of the ACA. We are focused on timely implementing this provision. To that end, we have made changes to computer systems, created a special group to conduct community benefit activity reviews of tax-exempt hospitals, and carried out internal training and customer education and outreach. As your report notes, we have published Notices and developed draft guidance which has advanced to the review stage. In addition, since March 2011, we have been conducting the reviews of community benefit activities of tax-exempt hospitals that are mandated by the ACA. To date, we have completed more than one-third of these reviews.

We agree with your recommendation. By March 31, 2013, we expect to enter into a Memorandum of Understanding with HHS addressing the format for information for future reports, and specifying when this information should be received.

Our response to your recommendation is attached.

If you have questions, please call me at (202) 283-2700.

Attachment



***Affordable Care Act: While Much Has Been Accomplished, the
Extent of Additional Controls Needed to Implement Tax-Exempt
Hospital Provisions Is Uncertain***

Attachment

RECOMMENDATION:

The Director, EO, should work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services. The Memorandum of Understanding should take into consideration when information for the annual report to Congress should be received and the proper format of the data to ensure it will be timely and usable for the report to Congress.

CORRECTIVE ACTION:

We will work with the Department of the Treasury to establish a Memorandum of Understanding with the Department of Health and Human Services that takes into consideration when information for the annual report to Congress should be received and the proper format of the data to ensure it will be timely and usable for the report to Congress.

IMPLEMENTATION DATE:

March 31, 2013

RESPONSIBLE OFFICIAL(S):

Acting Commissioner, Tax Exempt and Government Entities