

which reporting is required would be clarified to include gross proceeds for both property and services. The present law regulatory exception for payments to exempt or governmental organizations, international organizations and retirement plans is not affected by this provision. In addition, the Secretary would be authorized to promulgate regulations necessary to avoid duplicative information reporting.

Effective Date

The Chairman's Mark is effective for payments made in taxable years beginning after December 31, 2011.

Requirements for Section 501(c)(3) Hospitals

Current Law

Tax Exemption. Charitable organizations, i.e., organizations described in section 501(c)(3), generally are exempt from Federal income tax, are eligible to receive tax deductible contributions,⁸⁴ have access to tax-exempt financing through state and local governments (described in more detail below),⁸⁵ and generally are exempt from state and local taxes. A charitable organization must operate primarily in pursuit of one or more tax-exempt purposes constituting the basis of its tax exemption.⁸⁶ The Code specifies such purposes as religious, charitable, scientific, educational, literary, testing for public safety, to foster international amateur sports competition, or for the prevention of cruelty to children or animals. In general, an organization is organized and operated for charitable purposes if it provides relief for the poor and distressed or the underprivileged.⁸⁷

The Code does not provide a *per se* exemption for hospitals. Rather, a hospital qualifies for exemption if it is organized and operated for a charitable purpose and otherwise meets the requirements of section 501(c)(3).⁸⁸ The promotion of health has been recognized by the Internal Revenue Service (IRS) as a charitable purpose that is beneficial to the community as a whole.⁸⁹ It includes not only the establishment or maintenance of charitable hospitals, but clinics, homes for the aged, and other providers of health care.

Since 1969, the IRS has applied a "community benefit" standard for determining whether a hospital is charitable.⁹⁰ According to Revenue Ruling 69-545, community benefit can include,

⁸⁴ Sec. 170.

⁸⁵ Sec. 145.

⁸⁶ Treas. Reg. sec. 1.501(c)(3)-1(c)(1).

⁸⁷ Treas. Reg. sec. 1.501(c)(3)-1(d)(2).

⁸⁸ Although nonprofit hospitals generally are recognized as tax-exempt by virtue of being "charitable" organizations, some might qualify for exemption as educational or scientific organizations because they are organized and operated primarily for medical education and research purposes.

⁸⁹ Rev. Rul. 69-545, 1969-2 C.B. 117; see also Restatement (Second) of Trusts secs. 368, 372 (1959); see Bruce R. Hopkins, *The Law of Tax-Exempt Organizations*, sec. 6.3 (8th ed. 2003) (discussing various forms of health-care providers that may qualify for exemption under section 501(c)(3)).

⁹⁰ Rev. Rul. 69-545, 1969-2 C.B. 117. From 1956 until 1969, the IRS applied a "financial ability" standard, requiring that a charitable hospital be "operated to the extent of its financial ability for those not able to pay for the

for example: maintaining an emergency room open to all persons regardless of ability to pay; having an independent board of trustees composed of representatives of the community; operating with an open medical staff policy, with privileges available to all qualifying physicians; providing charity care; and utilizing surplus funds to improve the quality of patient care, expand facilities, and advance medical training, education and research. Beginning in 2009, hospitals generally are required to submit information on community benefit on their annual information returns filed with the IRS.⁹¹ Present law does not include sanctions short of revocation of tax-exempt status for hospitals that fail to satisfy the community benefit standard.

Although section 501(c)(3) hospitals generally are exempt from Federal tax on their net income, such organizations are subject to the unrelated business income tax on income derived from a trade or business regularly carried on by the organization that is not substantially related to the performance of the organization's tax-exempt functions.⁹² In general, interest, rents, royalties, and annuities are excluded from the unrelated business income of tax-exempt organizations.⁹³

Charitable Contributions. In general, a deduction is permitted for charitable contributions, including charitable contributions to tax-exempt hospitals, subject to certain limitations that depend on the type of taxpayer, the property contributed, and the donee organization. The amount of deduction generally equals the fair market value of the contributed property on the date of the contribution. Charitable deductions are provided for income, estate, and gift tax purposes.⁹⁴

Tax-exempt Financing. In addition to issuing tax-exempt bonds for government operations and services, state and local governments may issue tax-exempt bonds to finance the activities of charitable organizations described in section 501(c)(3). Because interest income on tax-exempt bonds is excluded from gross income, investors generally are willing to accept a lower pre-tax rate of return on such bonds than they might otherwise accept on a taxable investment. This, in turn, lowers the cost of capital for the users of such financing. Both capital expenditures and limited working capital expenditures of charitable organizations described in section 501(c)(3) of the Code generally may be financed with tax-exempt bonds. Private, non-profit hospitals frequently are the beneficiaries of this type of financing.

Bonds issued by state and local governments may be classified as either governmental bonds or private activity bonds. Governmental bonds are bonds the proceeds of which are primarily used to finance governmental functions or which are repaid with governmental funds. Private activity bonds are bonds in which the state or local government serves as a conduit providing financing to nongovernmental persons (e.g., private businesses or individuals). For these purposes, the term "nongovernmental person" generally includes the Federal government and all other individuals and entities other than states or local governments, including section 501(c)(3) organizations. The exclusion from income for interest on state and local bonds does not apply to

services rendered and not exclusively for those who are able and expected to pay." Rev. Rul. 56-185, 1956-1 C.B. 202.

⁹¹ IRS Form 990, Schedule H.

⁹² Secs. 511-514.

⁹³ Sec. 512(b).

⁹⁴ Secs. 170, 2055, and 2522, respectively.

private activity bonds, unless the bonds are issued for certain permitted purposes (“qualified private activity bonds”) and other Code requirements are met.

Reporting and Disclosure Requirements. Exempt organizations are required to file an annual information return, stating specifically the items of gross income, receipts, disbursements, and such other information as the Secretary may prescribe.⁹⁵ Section 501(c)(3) organizations that are classified as public charities must file Form 990 (Return of Organization Exempt From Income Tax),⁹⁶ including Schedule A, which requests information specific to section 501(c)(3) organizations. Additionally, an organization that operates at least one facility that is, or is required to be, licensed, registered, or similarly recognized by a state as a hospital must complete Schedule H (Form 990), which requests information regarding charity care, community benefits, bad debt expense, and certain management company and joint venture arrangements of a hospital.

An organization described in section 501(c) or (d) generally is also required to make available for public inspection for a period of three years a copy of its annual information return (Form 990) and exemption application materials.⁹⁷ This requirement is satisfied if the organization has made the annual return and exemption application widely available (e.g., by posting such information on its website).⁹⁸

Chairman’s Mark

Additional Requirements for Section 501(c)(3) Hospitals.⁹⁹ The Chairman’s Mark would establish new requirements applicable to section 501(c)(3) hospitals. The new requirements are in addition to, and not in lieu of, the requirements otherwise applicable to an organization described in section 501(c)(3). The requirements generally would apply to any section 501(c)(3) organization that operates at least one hospital facility. For purposes of the provision, a hospital facility generally includes: (1) any facility that is, or is required to be, licensed, registered, or similarly recognized by a state as a hospital; and (2) any other facility or organization the Secretary of the Treasury (hereinafter “Secretary”), in consultation with the Health and Human Services Secretary and after public comment, determines has the provision of hospital care as its principal purpose. An organization subject to the provision would be required to comply with the following requirements with respect to each hospital facility operated by such organization.

Community health needs assessment

Each hospital facility would be required to conduct a community health needs assessment at least once every three years and adopt an implementation strategy to meet the community needs

⁹⁵ Sec. 6033(a). An organization that has not received a determination of its tax-exempt status, but that claims tax-exempt status under section 501(a), is subject to the same annual reporting requirements and exceptions as organizations that have received a tax-exemption determination.

⁹⁶ Social welfare organizations, labor organizations, agricultural organizations, horticultural organizations, and business leagues are subject to the generally applicable Form 990, Form 990-EZ, and Form 990-T annual filing requirements.

⁹⁷ Sec. 6104(d).

⁹⁸ Sec. 6104(d)(4); Treas. Reg. sec. 301.6104(d)-2(b).

⁹⁹ No inference is intended regarding whether an organization satisfies the present law community benefit standard.

identified through such assessment. The assessment may be based on current information collected by a public health agency or non-profit organizations and may be conducted together with one or more other organizations, including related organizations. The assessment process must take into account input from persons who represent the broad interests of the community served by the hospital, including those with special knowledge or expertise of public health issues. The hospital must disclose in its annual information report to the IRS (i.e., Form 990 and related schedules) how it is addressing the needs identified in the assessment and, if all identified needs are not addressed, the reasons why (e.g. lack of financial or human resources). Each hospital facility would be required to make the assessment widely available. Failure to complete a community needs assessment in any applicable three-year period would result in a penalty on the organization of up to \$50,000. Failure to disclose how it is meeting needs identified in the assessment would be subject to existing incomplete return penalties.

Financial assistance policy

Each hospital facility would be required to adopt, implement, and widely publicize a written financial assistance policy. Each hospital facility would be required to adopt and implement a policy to provide emergency medical treatment to individuals. The policy must prevent discrimination in the provision of emergency medical treatment, including denial of service, against those eligible for financial assistance under the facility's financial assistance policy or those eligible for government assistance. The financial assistance policy should indicate the eligibility criteria for financial assistance and whether such assistance includes free or discounted care. For those eligible for discounted care, the policy should indicate the basis for calculating the amounts that will be billed to such patients. The policy should also indicate how to apply for such assistance. If hospital does not have a separate billing and collections policy, the financial assistance policy must also indicate what actions the hospital may take in the event of non-response or non-payment, including collections action and reporting to credit rating agencies.

Limitation on charges

Each hospital facility would be required to bill patients who qualify for financial assistance no more than the amount generally billed to insured patients. A hospital facility may not use gross charges(i.e., chargemaster rates), when billing individuals who qualify for financial assistance. Amounts billed to those who qualify for financial assistance may be based on either the best, or an average of the three best, negotiated commercial rates, or Medicare rates.

Collection processes

The Chairman's Mark provides that a hospital facility (or its affiliates) generally would be required to follow current Medicare law and regulations regarding collection of debts, but may not undertake certain extraordinary collection actions (even if otherwise permitted by law) against a patient without first making reasonable attempts to inform the patient about the hospital's financial assistance policy. Such extraordinary collection actions would include lawsuits, liens on residences, arrests, body attachments, or other similar collection processes. The Secretary shall issue guidance concerning what attempts to determine eligibility for financial assistance constitute "reasonable attempts." It is intended that for this purpose, "reasonable attempts" would include notification by the hospital of its financial assistance policy upon

admission and in written and oral communications with the patient regarding the patient's bill, including invoices and telephone calls, before collection action or reporting to credit rating agencies is initiated.

Reporting and Disclosure Requirements. The Chairman's Mark would include new reporting and disclosure requirements. Under the Mark, the IRS would be required to review information about a hospital's community benefit activities (currently reported on Form 990, Schedule H) at least once every three years. Such review is intended to be similar to review of companies registered with the Securities and Exchange Commission.¹⁰⁰ The Mark would require each organization to which the Mark applies to make its audited financial statements widely available. If an organization or facility is included in consolidated financial statements, the consolidated entity's audited financial statements must also be widely available.

The Chairman's Mark would require the Secretary and the Secretary of Health and Human Services to annually report to Congress the levels of charity care, bad debt expenses, unreimbursed costs of means-tested government programs, and unreimbursed costs of non-means tested government programs incurred by private tax-exempt, taxable, and governmental hospitals as well as the cost of community benefit activities incurred by private tax-exempt hospitals. In addition, the Secretary, in conjunction with the Secretary of Health and Human Services, must conduct a study of the trends in these amounts with to the results of the study provided to Congress five years from date of enactment.

Effective Date

The Chairman's Mark would be effective for taxable years beginning after the date of enactment.

Annual Fee on Manufacturers and Importers of Branded Drugs

Current Law

There are two Medicare trust funds under current law, the Hospital Insurance (HI) fund and the Supplementary Medical Insurance (SMI) fund.¹⁰¹ The HI trust fund is primarily funded through payroll tax on covered earnings. Employers and employees each pay 1.45 percent of wages, while self-employed workers pay 2.9 percent of a portion of their net earnings from self-employment. Other HI trust fund revenue sources include a portion of the Federal income taxes paid on Social Security benefits, and interest paid on the U.S. Treasury securities held in the HI trust fund. For the SMI trust fund, transfers from the general fund of the Treasury represent the largest source of revenue, but additional revenues include monthly premiums paid by beneficiaries, and interest paid on the U.S. Treasury securities held in the SMI trust fund.

Current law does not impose an annual sector fee creditable to the Medicare trust funds on companies that manufacture or import branded prescription drugs for sale in the United States.

¹⁰⁰ See <http://www.sec.gov/divisions/corpfin/cffilingreview.htm> for SEC procedures.

¹⁰¹ See 2009 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds, available at <http://www.cms.hhs.gov/ReportsTrustFunds/downloads/tr2009.pdf>.