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The Great Wall of CHNA: Interpreting New IRS Guidance for Tax-Exempt Hospitals and Hospital Districts

By Richard Croghan
Partner
Moss Adams LLP



By Karl Rebay
Director
Moss Adams LLP



As you may be aware, deadlines and guidelines surrounding the Affordable Care Act (ACA) continue to be in flux. For up-to-the-minute news about the ACA, Moss Adams recommends that you refer to Healthcare.gov or the Kaiser Family Foundation.

Hospitals and hospital districts committed to a charitable purpose are exempt from income taxes. But how to confirm that these tax-exempt hospitals are actually living

up to their mission—promoting health in and providing appropriate services to their community? Enter the community health needs assessment (CHNA).

Created as part of the Affordable Care Act, CHNAs must be conducted by not-for-profit hospitals and health systems periodically to maintain their tax exemption under Section 501(c)(3) of the Internal Revenue Code. To complete a CHNA, hospitals and health

systems are to collaborate with local leaders to analyze the community's health needs. They then must adopt an implementation strategy based on the needs identified in the assessment.

CHNAs don't look or feel like something one would normally submit to the IRS, but that's who will be monitoring compliance. On April 5 the IRS issued additional proposed guidance and clarification for complying with CHNA requirements. The guidance also outlines penalties for noncompliance, including a \$50,000 yearly excise tax for hospitals with outstanding CHNAs and the possible revoking of not-for-profit status. However, the new guidance also provides several relief provisions for hospitals that make an effort to comply.

Applicable hospitals should have either already conducted a CHNA or must do so by the end of their current fiscal year to avoid any penalties. CHNAs are required once every three years, starting with tax years beginning after March

23, 2010. For organizations with a calendar year-end, the first CHNA must be completed by December 31, 2013. Thus, with the first CHNA deadline rapidly approaching, let's review the IRS requirements.

Who Must Complete a CHNA?

Hospitals recognized as exempt from tax under Section 501(c)(3) are subject to the CHNA requirement. A hospital is defined as an organization that operates a state-licensed hospital facility or that has the provision of hospital care as its principal function. This includes certain government-operated hospital facilities recognized as exempt under Section 501(c)(3).

The proposed guidance further defines hospital organizations recognized under Section 501(c)(3) to include hospitals operated by single-member LLCs (disregarded entities) as well as those operated through a joint venture or partnership. There are exceptions to this definition, including if the organization doesn't have sufficient control over the hospital facility and if the 501(c)(3) organization treats the hospital facility as an unrelated trade or business.

If you've completed a CHNA for state purposes, you should compare that assessment with the IRS requirements. It's also a good idea to make sure you've documented all the IRS requirements.

What Are the CHNA Requirements?

The primary components of the CHNA written report are:

- A definition of the community the hospital serves, including target populations and specialty care areas

- An outline of the process and methods used to conduct the assessment
- The data used in the assessment and the sources of that information
- Prioritization of the significant health needs of the community, including a description of the process and criteria used in identifying certain health needs as significant
- An explanation of the input the hospital received from stakeholders who represent the broad interests of the community
- A description of actions the hospital facility plans to take and how their impact will be evaluated

A CHNA is considered to be completed on the date that all the steps outlined above have been addressed and the report is made widely available to the public, including posting the report on the hospital's Web site.

The proposed guidelines also include a provision requiring hospital facilities to retain links to the current CHNA report and at least two subsequent CHNA reports on their Web site. Additionally, the new regulations allow hospital facilities to collaborate and issue joint CHNA reports, but only if:

- All hospitals adopting the joint CHNA are clearly identified
- The CHNA process is conducted jointly
- Each hospital defines the community it serves in the same terms

- Each hospital's authorized body adopts the joint CHNA

Implementation Requirements

The proposed rules require a hospital to adopt an implementation strategy in the same tax year it conducts a CHNA. The strategy, in the form of a written plan, should describe how the hospital plans to address—or why it doesn't intend to address—the community's identified health needs. The strategy must be adopted by the hospital's board of directors, and the hospital is required to attach its most recent implementation strategy to its Form 990 annually.

Facilities that collaborate on joint CHNA reports may also adopt a joint implementation strategy but must:

- Clearly identify that the CHNA applies to the hospital facility
- Distinguish the hospital facility's particular role and responsibilities in taking the actions described in the implementation strategy and the programs and resources the hospital facility plans to commit in taking those actions
- Format the document to help the reader easily locate those portions of the joint implementation strategy that relate to each hospital facility

Noncompliance Implications

The IRS may penalize nonconforming hospitals by assessing them a \$50,000 excise tax, revoking their tax-exempt status, and subjecting them to income tax. However, the proposed

regulations provide relief for minor or inadvertent omissions or errors if they're corrected immediately after detection.

Strategic Implications

The CHNA can be a valuable strategic planning tool. If done correctly, it will involve obtaining a fairly in-depth understanding of a hospital's marketplace. The process is not unlike other market assessments that organizations complete as part of both short- and long-term planning.

Hospitals can take advantage of

the requirement to complete these assessments by gleaning valuable insight from community leaders and others knowledgeable about health needs in the community. It's a way to gauge the reputation of your organization and tailor your business strategy to address important issues in the community—which in turn could serve to enhance the hospital's reputation and market position.

Karl Rebay has built consulting, finance, and operational experience in the health care arena since 1994. He leverages his expertise in strategic business planning and provider operations to help health

care organizations strengthen their operations and succeed in the current environment. You can reach him at (949) 623-4193 or karl.rebay@mossadams.com.

Richard Croghan has been in public accounting since 1991, serving large integrated health systems, stand-alone hospitals, managed care organizations, physician groups, and ancillary service organizations, with a focus on providing tax services to tax-exempt health care organizations. You can reach him at (415) 677-8282 or richard.croghan@mossadams.com.

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