Part III – Administrative, Procedural, and Miscellaneous

Proposed Procedures for Charitable Hospitals to Correct and Disclose Failures to Meet § 501(r)

Notice 2014-3

PURPOSE AND BACKGROUND

This notice contains a proposed revenue procedure that provides correction and disclosure procedures under which certain failures to meet the requirements of § 501(r) of the Internal Revenue Code will be excused for purposes of § 501(r)(1) and 501(r)(2)(B).

Section 9007 of the Patient Protection and Affordable Care Act, Public Law 111-148 (124 Stat. 119 (2010)), enacted § 501(r), which imposes additional requirements on charitable hospital organizations. Section 501(r)(1) provides that a hospital organization will not be treated as described in § 501(c)(3) unless the organization meets the requirements of § 501(r)(3) through (r)(6). Similarly, § 501(r)(2)(B)(ii) provides that a hospital organization operating more than one hospital facility will not be treated as described in § 501(c)(3) with respect to any such hospital facility for which the requirements of § 501(r) are not separately met.

On June 26, 2012, the Department of the Treasury ("Treasury Department") and the Internal Revenue Service (IRS) published a notice of proposed rulemaking in the Federal Register (REG-130266-11, 2012-32 I.R.B. 126 [77 FR 38148]) ("2012 proposed

regulations") that contains proposed regulations regarding the requirements of § 501(r)(4), (r)(5), and (r)(6). On April 5, 2013, the Treasury Department and the IRS published a notice of proposed rulemaking in the Federal Register (REG-106499-12, 2013-21 I.R.B. 1111 [78 FR 20523]) ("2013 proposed regulations") that contains proposed regulations regarding the requirements of § 501(r)(3) and the consequences for failing to meet any of the § 501(r) requirements.

To provide an incentive for hospital organizations to take steps not only to avoid failures but to remedy and disclose them when they occur, the 2013 proposed regulations specify that, for purposes of § 501(r)(1) and 501(r)(2)(B), a hospital organization's failure to meet one or more of the requirements described in § 501(r) and § 1.501(r)–3 through § 1.501(r)–6 that is neither willful nor egregious will be excused if the hospital organization corrects the failure and makes disclosure in accordance with the rules set forth in additional guidance to be issued by the Treasury Department and the IRS.

This notice provides a proposed revenue procedure that if adopted would contain that additional guidance.

REQUEST FOR COMMENTS

The Treasury Department and the IRS invite comments regarding the procedures set forth in the proposed revenue procedure, including what additional examples, if any, would be helpful to include and whether hospitals should be required to make disclosure in ways other than reporting on Schedule H, *Hospitals*, of its Form 990, *Return of Organization Exempt From Income Tax*, such as on their Web sites.

Comments should refer to Notice 2014-3 and be submitted by March 14, 2014, to:

Internal Revenue Service
CC:PA:LPD:PR (Notice 2014-3)
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

CC:PA:LPD:PR (Notice 2014-3)
Courier's Desk
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Alternatively, comments may be submitted electronically via e-mail to the following address: Notice.Comments@irscounsel.treas.gov. Please include "Notice 2014-3" in the subject line.

All comments submitted by the public will be available for public inspection and copying.

DRAFTING INFORMATION

The principal author of this notice is Garrett Gluth of the Exempt Organizations, Tax Exempt and Government Entities Division. For further information regarding this notice, contact Garrett Gluth at 202-317-8413 (not a toll-free call).

PROPOSED REVENUE PROCEDURE

SECTION 1. PURPOSE

This revenue procedure provides guidance regarding correction and disclosure procedures for hospital organizations to follow so that certain failures to meet the requirements of § 501(r) of the Internal Revenue Code will be excused for purposes of § 501(r)(1) and 501(r)(2)(B).

SECTION 2. BACKGROUND

Section 9007 of the Patient Protection and Affordable Care Act, Public Law 111-148 (124 Stat. 119 (2010)), enacted § 501(r), which imposes additional requirements on charitable hospital organizations. Section 501(r)(1) provides that a hospital organization described in § 501(r)(2) will not be treated as described in § 501(c)(3) unless the organization meets the requirements of § 501(r)(3) through (r)(6).

Section 501(r)(2)(A) defines a hospital organization as including any organization that operates a facility required by a state to be licensed, registered, or similarly recognized as a hospital.

Section 501(r)(2)(B) requires a hospital organization that operates more than one hospital facility to meet the requirements of § 501(r) separately with respect to each hospital facility and provides that such a hospital organization will not be treated as described in § 501(c)(3) with respect to any hospital facility for which the requirements of § 501(r) are not separately met.

Section 501(r)(3) requires a hospital organization to conduct a community health needs assessment (CHNA) every three years and adopt an implementation strategy to meet the community health needs identified through such assessment. Section 4959

imposes a $50,000 excise tax on a hospital organization that fails to meet the CHNA requirements of § 501(r)(3).

Section 501(r)(4) requires a hospital organization to establish a financial assistance policy (FAP) and a policy relating to emergency medical care.

Section 501(r)(5) requires a hospital organization to limit amounts charged for emergency or other medically necessary care that is provided to individuals eligible for assistance under the organization's FAP (FAP-eligible individuals) to not more than the amounts generally billed to individuals who have insurance covering such care. Section 501(r)(5) also prohibits the use of gross charges.

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 statutory requirements of § 501(r) (except for § 501(r)(3)) are effective for a hospital organization's first taxable year beginning after March 23, 2010. Section 501(r)(3) is effective for a hospital organization's first taxable year beginning after March 23, 2012.

On June 26, 2012, the Department of the Treasury ("Treasury Department") and the Internal Revenue Service ("IRS") published a notice of proposed rulemaking in the Federal Register (REG-130266-11, 2012-32 I.R.B. 126 [77 FR 38148]) ("2012 proposed regulations") that contains proposed regulations regarding the requirements of § 501(r)(4), (r)(5), and (r)(6). On April 5, 2013, the Treasury Department and the IRS published a notice of proposed rulemaking in the Federal Register (REG-106499-12, 2013-21 I.R.B. 1111 [78 FR 20523]) ("2013 proposed regulations") that contains

proposed regulations regarding the CHNA requirements of § 501(r)(3) and the consequences for failing to meet any of the § 501(r) requirements.

Under section 1.501(r)-2(c) of the 2013 proposed regulations, a hospital facility's failure to meet the requirements of § 501(r) and § 1.501(r)-3 through § 1.501(r)-6 of the regulations that is neither willful nor egregious shall be excused for purposes of § 501(r)(1) and 501(r)(2)(B) if the hospital facility corrects and makes disclosure of the failure in accordance with a revenue procedure, notice, or other guidance to be published in the Internal Revenue Bulletin.

Under section 1.501(r)-2(b) of the 2013 proposed regulations, a hospital facility's omission of required information from a report or policy described in § 1.501(r)-3 or § 1.501(r)-4, or error with respect to the implementation or operational requirements described in § 1.501(r)-3 through § 1.501(r)-6, will not be considered a failure to meet a requirement of § 501(r) if (1) such omission or error was minor, inadvertent, and due to reasonable cause; and (2) the hospital facility corrects such omission or error as promptly after discovery as is reasonable given the nature of the omission or error. Because minor and inadvertent omissions and errors due to reasonable cause that are corrected in accordance with the requirements of § 1.501(r)-2(b) of the 2013 proposed regulations are not considered failures to meet a requirement of § 501(r), hospitals do not need to use the correction and disclosure procedures described in this revenue procedure for such omissions and errors. However, an organization that wants to correct a minor and inadvertent omission or error may rely on the principles regarding

correction described in section 5 of this revenue procedure in meeting the correction requirements of § 1.501(r)-2(b)(2).[1]

SECTION 3. EFFECT

.01 In general. The IRS will not treat a hospital organization's failure to meet a requirement of § 501(r) as a failure for purposes of § 501(r)(1) and 501(r)(2)(B) if the failure falls within the scope of section 4 and the hospital organization corrects the failure in accordance with section 5 and discloses the failure in accordance with section 6.

.02 Excise tax under § 4959. Notwithstanding the treatment of a failure to meet a requirement of § 501(r) as not a failure under section 3.01 for purposes of § 501(r)(1) and 501(r)(2)(B), a hospital organization may be subject to excise tax under § 4959 for failures to meet the requirements of § 501(r)(3).

SECTION 4. SCOPE

.01 In general. A hospital organization may rely upon this revenue procedure to correct and disclose any failure to meet a requirement of § 501(r) that is not willful or egregious, provided that the hospital organization has begun correcting the failure in accordance with section 5 and that it has disclosed the failure in accordance with section 6 before the hospital organization is first contacted by the IRS concerning an examination of the organization. If the annual return for the tax year in which the failure is discovered is not yet due (with extensions), then the hospital organization need only

[1] In addition, § 1.501(r)-2(a)(8) of the 2013 proposed regulations provides that, for purposes of determining whether to continue to recognize the § 501(c)(3) status of a hospital organization, the IRS will consider whether a hospital organization corrected a failure as promptly after discovery as was reasonable given the nature of the failure. A hospital organization that cannot or does not have an error or omission excused by following the correction and disclosure procedures outlined in this revenue procedure may nevertheless use these principles in demonstrating that they satisfy the factor described in § 1.501(r)-2(a)(8).

to have begun correcting the failure in accordance with section 5 before the hospital organization is first contacted by the IRS concerning an examination.

.02 Willful or egregious. A failure that is willful includes a failure due to gross negligence, reckless disregard, or willful neglect. A hospital organization's correction and disclosure of a failure does not create a presumption that the failure was not willful or egregious. However, the fact that correction and disclosure in accordance with this revenue procedure were made will be considered as a factor and may tend to indicate that an error or omission may not have been willful or egregious.

SECTION 5. CORRECTION

.01 Correction principles. Correction must be made in accordance with the following principles:

(1) Restoration of affected persons. To the extent reasonably feasible, the correction should be made with respect to each affected person, if any, and should restore the affected person(s) to the position they would have been in had the failure not occurred, regardless of whether the harm suffered by the affected person(s) occurred in a prior year and regardless of whether such prior year is a closed taxable year.

(2) Reasonable and appropriate correction. The correction should be reasonable and appropriate for the failure. Depending on the nature of the failure, there may be more than one reasonable and appropriate correction.

(3) Timing. The correction should be made as promptly after discovery as is reasonable given the nature of the failure.

(4) Implementation/modification of safeguards. If the hospital organization has not established practices and procedures (whether informal or formal) for its hospital facility

or facilities that are reasonably designed to achieve each facility's compliance with the requirements of § 501(r), the hospital organization should establish such practices and procedures as part of its correction. If the hospital organization has established practices and procedures for its hospital facility or facilities to achieve compliance with § 501(r) but those practices and procedures failed to anticipate the particular type of failure that occurred, the hospital organization should determine if changes to its practices and procedures are needed to reduce the likelihood of that type of failure recurring and to assure prompt identification and correction of any such failures that do occur. If it identifies any such changes to its practices and procedures, it should implement those changes.

.02 Examples. The provisions of section 5.01 may be illustrated by the following examples. For purposes of these examples, assume that the hospital facility corrected the failure with respect to all affected persons as promptly after discovery as is reasonable given the nature of the failure and put into place revised or newly established practices and procedures to minimize the likelihood of the failure recurring.

(1) A hospital facility that has failed to adopt a CHNA report that contains all of the elements required by § 1.501(r)-3 may correct the failure by preparing and adopting a CHNA report containing all of the required elements and making the corrected CHNA report widely available on a Web site within the meaning of § 1.501(r)-1(c)(4) of the 2013 proposed regulations.

(2) A hospital facility that has failed to adopt a FAP that contains all of the elements required by § 1.501(r)-4 may correct the failure by establishing a FAP containing all of

the required elements, including making the corrected FAP widely available on a Web site within the meaning of § 1.501(r)-1(c)(4) of the 2013 proposed regulations.

(3) A hospital facility has failed to meet the requirements of § 1.501(r)-5 because, due to processing errors, it charged FAP-eligible individuals more than an amount permitted under that section. The errors were discovered during the month-end accounting period closing. The hospital facility may correct the failure by providing all of the affected FAP-eligible individuals with an explanation of the error, a corrected billing statement, and a refund of any payments the individuals made to the hospital facility (or any third party) in excess of the amount they are determined to owe as FAP-eligible individuals.

(4) If a hospital facility fails to properly implement a policy required under § 1.501(r)-4 and that failure does not involve over-charging a FAP-eligible individual or engaging in an ECA (for example, a failure to widely publicize a FAP in the manner described in the FAP), the hospital facility may correct the failure by beginning to implement the policy correctly and taking reasonable actions to compensate for the failure (such as doing additional outreach or advertising of the FAP in local media in the case of a failure to widely publicize the FAP).

SECTION 6. DISCLOSURE

A failure is disclosed for purposes of this revenue procedure if the hospital organization reports the following information on Schedule H, *Hospitals*, of its Form 990, *Return of Organization Exempt From Income Tax*, for the tax year in which the failure is discovered:

(1) A description of the failure, including the type of failure, the hospital facility or facilities where the failure occurred, the date(s) of the failure, the number of occurrences, and, in the case of failures to meet the operational requirements in § 1.501(r)-5 or § 1.501(r)-6, the number of persons affected and the dollar amounts involved. In addition, a hospital organization must describe the cause of the failure and the practices and procedures (if any) that were in place prior to the occurrence of the failure to detect or prevent the type of failure that occurred.

(2) A description of the discovery, including how it was made and the timing of discovery.

(3) A description of the correction made, including the method of correction, the date of correction, and whether all persons were restored to the position they would have been in had the failure not occurred and, if not, the reasons why.

(4) A description of the practices and procedures, if any, that were revised or newly established by the hospital organization for its hospital facility or facilities to minimize the likelihood of the type of failure recurring and to promptly identify and correct any such future failures that do occur; or, if no practices and procedures were revised or newly established by the hospital organization, an explanation of why no changes in practices and procedures were needed.

SECTION 7. EFFECTIVE DATE

This revenue procedure is effective on and after [INSERT DATE OF PUBLICATION OF THE FINAL REVENUE PROCEDURE IN THE INTERNAL REVENUE BULLETIN].

SECTION 8. DRAFTING INFORMATION

The principal author of this Revenue Procedure is Garrett Gluth of the Exempt Organizations, Tax Exempt and Government Entities Division. For further information regarding this revenue procedure, contact Garrett Gluth at 202-317-8413 (not a toll-free call).