

Nonprofit Hospitals Exempt From Taxes, Not From Hill Scrutiny (1)

By Shira Stein

Posted Feb. 13, 2019, 5:40 AM Updated Feb. 13, 2019, 3:35 PM

- IRS will be in spotlight with evaluation of tax-exempt status
- Committee chairman has investigated nonprofit hospitals before

The Senate Finance Committee is planning to review how nonprofit hospitals are earning their tax-exempt status and how the Internal Revenue Service is enforcing those standards, according to multiple sources familiar with the committee's plans.

In a Congress, where most of the scrutiny of health care is expected to be led by House Democrats, Finance Committee Chairman Chuck Grassley (R-Iowa) is gearing up for his own investigations, as he has typically done over his career in the Senate. Scrutiny of high drug prices is on his agenda, these sources say, but so are issues like tax-exempt hospitals that he has worked on in the past.

Grassley started his chairmanship this Congress by looking at the U.S. Olympic Committee's response to sexual abuse. The committee is a tax-exempt group. "It's a demonstration that he will not shy away from engaging with large, prominent tax-exempt organizations," Michael Peregrine, a partner at McDermott Will & Emery who represents corporations, said in an interview.

The investigations could bring new attention to an issue that has been on the back burner in the Trump administration. Health-care system executives have tuned out the IRS as a compliance concern for the past several years, Peregrine said. The IRS used to provide substantive guidance on these issues, but there has been a lack of it recently.

These health-care executives need to know if the tax code and regulations are flexible enough to deal with innovation in their industry, Peregrine said. Some of their new compensation arrangements, like the shift away from inpatient care, may not comply with their original tax-exempt arrangements.

Over 2,845 hospitals are operating as nonprofits, according to the American Hospital Association. A 2018 report commissioned by the AHA found nonprofit hospitals forwent \$6 billion in taxes in 2013—\$3.2 billion from the federal corporate income tax, \$2.5 billion from tax-exempt bond financing, and \$300 million from the federal unemployment tax. The report also found nonprofit hospitals provided \$67.4 billion in community benefits.

Grassley has tried to crack down on abuses of tax-exempt status by hospitals in the past, but with limited success, Shawn Gremminger, senior director of federal relations at the health-care advocacy group Families USA, said in an interview.

Scrutiny of tax-exempt hospitals will happen after the committee finishes its work to understand the high cost of prescription drugs, Grassley told reporters.

Grassley said he plans to review whether hospitals are correctly complying with a regulation that requires them to post their prices online starting Jan. 1. There is currently no enforcement mechanism for the Centers for Medicare & Medicaid Services on that regulation, Administrator Seema Verma recently told reporters.

Potential Outcomes

The aim of this scrutiny of tax-exempt hospitals may not always be to legislate, said Christopher Armstrong, a partner at Holland & Knight. Grassley's oversight goals tend to be to call out bad actors.

Grassley previously has used oversight to prod organizations into benefiting the public more, Armstrong said. For example, in an investigation with former Sen. Max Baucus (D-Mont.), he worked to get universities to spend more on tuition assistance simply through public pressure.

The scrutiny could result in some hospitals having their tax-exempt status revoked, Avalere Health consultant Dan Mendelson said. But it's unlikely all nonprofit hospitals would lose the treasured tax status.

The last time Grassley worked on this issue was in 2007 in a former stint as Finance Committee chairman. His work led states to re-evaluate their property tax exemptions for hospitals, Dean Zerbe, a former senior counsel for the committee from 2001 to 2008, said in an interview.

Grassley historically has had a staff that knows what to look for in these types of investigations, Peregrine said. And the veteran Iowa lawmaker has expanded his investigations staff this Congress.

Areas of Interest

Grassley has always been interested in ensuring that organizations that enjoy a tax exemption are acting in a way that benefits the public, said Armstrong, who was the chief oversight counsel on the Senate Finance Committee. Health care and tax exemption are big oversight issues this year, and "his oversight staff has a deep tax expertise in both areas."

Grassley will likely explore how hospitals are earning their tax-exempt status, which would include reviewing the charity care they perform and how the hospitals act when patients are unable to pay their bills, Armstrong said.

Grassley could also follow up on oversight he started last year exploring how the IRS is examining tax-exempt hospitals, and he likely will ask agency officials to testify on that matter.

In a 2018 letter, Grassley and former chairman Orrin Hatch (R-Utah) asked the IRS how it evaluates compliance with tax-exempt status code, what guidance the IRS has provided on the definition of charity work, and the agency's previous reviews of hospitals' compliance. Those are potential avenues for scrutiny now.

Hospitals need a firmer definition of what counts as a community benefit, Gremminger said.

Large Profit Margins

Some tax-exempt hospitals have large profit margins. After giving raises to senior executives, they tend to take that money and use it to buy up physician practices and other health-care facilities in their area to get more revenue, Gremminger said.

The Affordable Care Act added more requirements to qualify for tax-exempt status, one of which was that hospitals need to widely publicize policies about assistance for low-income patients.

Grassley may be interested in looking at how widely publicized those policies are, said Stephanie Kennan, senior vice president of federal public affairs at McGuireWoods Consulting. Kennan was a senior health policy adviser to Sen. Ron Wyden (D-Ore.) for more than a decade.

Grassley also has asked about the compensation of executives at tax-exempt hospitals, and he will likely include that in any review of this area, Peregrine said.

(Updates with comments from Grassley in eighth and ninth paragraphs.)

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