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IRS issues Fact Sheet to clarify/expand guidance for tax-exempt organizations participating in ACOs

By Richard T. Frazier

SUMMARY

The IRS has provided tax-exempt hospitals and other organizations with some additional clarity to guide them in structuring their participation in Medicare Shared Savings Program (“MSSP”) and NonMSSP ACOs.

In conjunction with CMS’s release of the final regulations applicable to Accountable Care Organizations (“ACOs”), the IRS issued a Fact Sheet (<http://www.irs.gov/newsroom/article/0,,id=248490,00.html>) providing additional information for tax-exempt organizations contemplating participation in an ACO. (Other Alerts regarding ACOs may be found at http://www.saul.com/common/publications/pdf_3052.pdf, http://www.saul.com/common/publications/pdf_3056.pdf and http://www.saul.com/common/publications/pdf_3046.pdf.) On April 18, 2011, the IRS had issued Notice 2011-20 (<http://www.irs.gov/pub/irs-drop/n-11-20.pdf>) (“Notice”) which summarized how it expects existing guidance to apply to exempt 501(c)(3) organizations participating in ACOs. The Fact Sheet confirms that the Notice continues to reflect the IRS’ general positions and provides some additional thoughts from the IRS. The most significant clarifications and additions to the IRS’ positions are the following:

- Even though there are changes in the final CMS regulations, the guidance issued in the Notice, as expanded by the Fact Sheet, still reflects the IRS’ current position.
- There are no special federal income tax rules that apply to tax-exempt hospitals participating in the MSSP through an ACO.
- The IRS expects that a tax-exempt hospital’s participation in the MSSP through an ACO will further its charitable purpose.
- While an ACO is intended to be a separate legal entity, the IRS has reiterated what CMS has said in its final regulation – that a clinically integrated organization may not

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need to create a separate entity but that a tax-exempt hospital (or similar organization) itself may be the ACO.

- It is not necessary for the tax-exempt hospital to control the partnership (or LLC) in order to ensure that the ACO's participation in the MSSP further a charitable purpose. This is a very significant conclusion, and one which tax-exempt practitioners have hoped the IRS would adopt.
- The IRS expects that, absent private inurement/benefit, any MSSP payments the tax-exempt hospital receives from the ACO will not be regarded as unrelated business income. Instead, these payments will be treated as related to the performance of the charitable purpose of lessening the burdens of government.
- If the ACO in which the hospital participates conducts other activities (such as participation in a commercial shared savings program), it may be possible that those additional activities will not jeopardize the tax-exempt status of the hospital. This is a significant additional conclusion by the IRS, since it means that some ACOs may be structured to participate in both the MSSP and in commercial programs. While these other activities may further the charitable purposes of the hospital, it is also possible that they will not. However, even if they are not regarded as furthering the charitable purposes of the hospital, those activities may not adversely affect the tax status of the hospital. In addition, the nature of the income derived from those activities may be related or unrelated, depending upon the circumstances. These additional conclusions are welcome guidance and consistent with the IRS' overall position on ACOs.
- It is possible that a stand-alone ACO may qualify on its own for tax-exempt status, whether it is exclusively

engaged in MSSP activities or if it is engaged in a combination of MSSP and NonMSSP activities.

- A tax-exempt charitable organization (e.g. a hospital) does not need to meet all five factors described in the Notice in order for it to avoid the private inurement/benefit proscription.
- The May 2007 IRS Memorandum regarding electronic health records will apply to a hospital participating in the MSSP through an ACO, thus providing protection to the hospital as though it had done so directly.

With the additional guidance provided in the Fact Sheet, tax-exempt hospitals now can structure or participate in ACOs with greater certainty as to the effect on their tax-exempt status and whether the income generated by participating in the ACO will be regarded as unrelated business income.

This Alert was written by Richard T. Frazier, a member of the firm's Health Practice Group. Richard is a member of the joint task force of the ABA Health Law Section and Section of Taxation which is preparing comments in response to the Notice, and he was part of a similar joint task force which prepared comments on the new requirements imposed on tax-exempt hospitals by section 501(r) of the Internal Revenue Code. Richard may be reached at 215.972.7828 or rfrazier@saul.com. This publication has been prepared by the Health Practice Group for information purposes only.

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