Tax Issues in Joint Ventures and Acquisitions for Hospitals and Academic Medical Centers

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Accountable Care Organizations Formed as Joint Ventures

- Affordable Care Act established Medicare Shared Savings Program (MSSP) that –
  - Promotes accountability for care of Medicare beneficiaries,
  - Improves the coordination of Medicare fee-for-service items and services, and
  - Encourages investment in infrastructure and redesigned care processes for high quality and efficient services delivers

- ACOs can be formed under the MSSP

- An ACO is a group of providers of services and supplies who work together to manage and coordinate care for Medicare fee-for-service beneficiaries and who meet certain criteria specified by the Centers for Medicare & Medicaid Services (CMS)

- What is the benefit of being an ACO?
  - If an ACO meets quality performance standards and demonstrates that it has achieved savings against a benchmark established by CMS, it will be eligible to receive a payment from CMS equal to a portion of the total savings (Shared Savings).
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- What is an ACO?
  - An ACO must have a formal legal structure so that it can receive and distribute payments for Shared Savings
  - It must be formed by one or more Medicare-enrolled health care service providers or suppliers
  - Among the types of entities that qualify as an ACO are partnerships or joint venture arrangements between hospitals and ACO professionals
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What are the tax issues in play with an ACO joint venture involving a tax-exempt healthcare provider?

2. Inurement and private benefit – excess benefit transaction (IRC 4958 and potential termination of tax-exempt status)
3. Unrelated business taxable income (IRC 511-515)
4. IRC 501(r) – community benefit standard – Rev. Rul. 69-545
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Continuation of Tax-Exempt Status

• A tax-exempt organization’s participation in a SSP through an ACO generally should not jeopardize its tax-exempt status

• IRS Notice 2011-20 states that the IRS expects that participation in a MSSP through an ACO generally will further the charitable purpose of lessening the burdens of government within the meaning of Treas. Reg. 1.501(c)(3)-1(d)(2), provided:
  – there is no inurement
  – there is no impermissible private benefit
  – the ACO meets all the eligibility requirements established by CMS for participation in a MSSP
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Inurement and Private Benefit

As a general rule, because of CMS regulation and oversight of MSSP, IRS expects that it will not consider a tax-exempt organization’s participation in a MSSP through an ACO to result in inurement or impermissible private benefit to a private party ACO participate, provided:

- the terms of the tax-exempt organization’s participation in the MSSP through the ACO are set forth in advance in a written agreement negotiated at arms’ length. (The agreement must include the organization’s share of MSSP payments or losses and expenses.)
- CMS has accepted the ACO into, and has not terminated the ACO from, the MSSP
- The tax-exempt organization’s share of economic benefits derived from the ACO (including its share of MSSP payments) is proportional to the benefits or contributions the tax-exempt organization provides the ACO.
- If the tax-exempt organization receives an ownership interest in the ACO, the ownership interest received is proportional and equal in value to its capital contribution to the ACO and all ACO returns of capital, allocations and distributions are made in proportion to ownership interests.
- The tax-exempt organization’s share of ACO’s losses (including its share of SSP losses) does not exceed the share of ACO economic benefits to which the tax-exempt organization is entitled
- All contracts and transactions entered into by the tax-exempt organization with the ACO and the ACO’s participants, and by the ACO with the ACO’s participants and any other parties, are at fair market value
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Unrelated Business Taxable Income

- If the requirements are met to avoid inurement and impermissible private benefit, any payments received by a tax-exempt organization will be classified as substantially related to the organization’s charitable purpose of lessening the burdens of government.

- To the extent that the tax-exempt organization participates in activities unrelated to the MSSP, such as entering into shared savings arrangements with other types of health insurance payers, the IRS anticipates there will be unrelated business taxable income because it does not think these non-SSP activities will lessen the burden of government.

- IRS requested comments on situations in which participation in non-MSSP activities will further exempt purpose its exempt purpose of providing healthcare (e.g., shared savings arrangements with healthcare funded by Medicaid).
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IRC 501(r) – Community Benefit Standard – Rev. Rul. 69-545

Who knows?

- What are the tax consequences of the overlap of the ACO requirements, the IRC 501(r) community benefit requirements, and the existing joint-venture requirements found in Rev. Rul. 98-15 and the cases decided after that ruling?
- In joint ventures between for-profit and tax-exempt partners, it is essential that the parties are aware of the IRC 501(r) requirements and include language in the joint venture documents requiring compliance with IRC 501(r) and flexibility to adjust the relationship to comply with future guidance from IRS, SSA, Treasury, Congress, and the courts
Questions or Comments?

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