

# Now & Next

## Healthcare Alert

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### Revisiting Section 501(r) compliance in 2025

By Jennifer Jovcevski, Valerie Breslin Montague, Anita Pelletier, and April Schweitzer<sup>1</sup>

Tax-exempt hospitals continue to be scrutinized for alleged disproportionate benefits they receive through their tax-exempt status compared to the benefits provided to the community.



#### What's the impact?

- Tax-exempt hospitals should remain vigilant to avoid slipping into noncompliance with the Section 501(r) requirements.
- Half of the hospitals in the US are categorized as tax-exempt and a threat to that status is a significant risk.

The Internal Revenue Services' (IRS) Tax Exempt and Government Entities division (TE/GE) recently shared in the TE/GE's 2025 Program Letter that its focus on strategic enforcement of highly complex or emerging issues will include examination of tax-exempt hospitals and whether they are complying with applicable federal requirements for maintaining their tax-exempt status.

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<sup>1</sup> Lindsay Vaughn (Legal intern—Healthcare practice) assisted with the preparation of this article.

As hospitals assess their practices, leadership should engage experienced counsel in Section 501(r) compliance, as well as similar state requirements for not-for-profit healthcare providers. Proactively addressing these requirements will help ensure continued tax-exempt status while fulfilling a hospital's commitment to serving their community.

## What is Code Section 501(r)?

The Patient Protection and Affordable Care Act (ACA), enacted on March 23, 2010, added new requirements for hospital organizations treated as Internal Revenue Code Section 501(c)(3) tax-exempt organizations. Such ACA requirements formally codified IRS [requirements](#) and [Revenue Ruling 69-545](#), often referred to as the "community benefit" standard, under Code Section 501(r) with an effective date of December 29, 2015.

Code Section 501(r) established a clear federal standard for a tax-exempt hospital's continued qualification as exempt under Code Section 501(c)(3). These requirements provide additional measures to ensure that tax-exempt hospitals are serving their community, with a focus on transparency and accountability.

## The four key requirements for compliance

Hospital organizations must meet four key requirements under Section 501(r) on a facility-by-facility basis to maintain their tax-exempt status:

### **COMMUNITY HEALTH NEEDS ASSESSMENT (CHNA)**

- / Complete a CHNA every three years and adopt an implementation strategy to meet the identified community health needs through input from individuals who represent the community's broad interest, including those with special knowledge or public health expertise.
- / The CHNA report must be made widely available to the public.

### **CREATE AND IMPLEMENT A WRITTEN FINANCIAL ASSISTANCE POLICY (FAP) AND A WRITTEN EMERGENCY MEDICAL CARE POLICY**

- / The FAP, its application form, and a plain language summary must be widely publicized in the community being served by making it available on a website, offering printed copies upon request at the facility, and be available in multiple languages, depending on the community served.
- / The FAP must include eligibility criteria for financial assistance, whether free or discounted care is included in financial assistance, the basis for calculating amounts charged to patients, the method for applying for financial assistance, and any extraordinary collection actions that

the organization may take in the event of nonpayment (e.g., reporting to credit agencies, selling debt to another party, and actions requiring judicial or legal processes, such as seizing personal property, garnishing wages, or foreclosing on an individual's property).

- / The emergency medical care policy must include the requirement that the organization will provide emergency care without discrimination based on FAP eligibility.

#### **MAINTAIN LIMITS ON THE AMOUNT CHARGED FOR FINANCIAL ASSISTANCE**

- / For patients eligible for financial assistance, hospitals must ensure that charges for emergency and medically necessary care do not exceed what the hospital typically charges insured patients for the same care. This is known as the "amount generally billed" (AGB) rule.
- / Hospitals can use the [look-back method](#) or the [prospective method](#) to determine the AGB.

#### **FOLLOW FAIR BILLING AND COLLECTION PROCEDURES**

- / Create and implement billing and collections procedures that will ensure reasonable efforts are made to determine whether an individual is eligible for financial assistance under the hospital's FAP before engaging in extraordinary collection actions.
- / Extraordinary collection actions include, but are not limited to, selling an individual's debt to another party; reporting adverse information to consumer credit reporting agencies or credit bureaus; deferring, denying, or requiring a payment before providing medically necessary care because of an individual's non-payment for previously provided care; and garnishing an individual's wages.

## **Failure to satisfy Section 501(r)'s requirements**

The ultimate penalty for noncompliance with Section 501(r)'s requirements is revocation of the hospital's Code Section 501(c)(3) tax-exempt status. Exempt hospitals may also be assessed financial penalties. For example, failure to meet the CHNA and implementation strategy requirements could result in a \$50,000 excise tax imposed on each noncompliant facility within a hospital organization regardless of whether tax-exempt status also has been revoked.

Tax-exempt hospitals may avoid revocation for "minor omissions and errors" that are inadvertent or due to reasonable cause and "certain failures" that are corrected and disclosed.

The TE/GE published its first revocation of a hospital's tax-exempt status for failure to satisfy Section 501(r)'s requirements in [August 2017](#). The hospital involved was a "dual status" entity due to its tax exemption as a charitable organization under Section 501(c)(3) and as a governmental unit or affiliate of a governmental unit. Additionally, the hospital served "several small communities," implying that it may have been operating in a rural community. The reasons

provided for the revocation included failure to conduct a CHNA, failure to adopt an implementation strategy, and failure to make the CHNA report widely available to the public.

## **Revisiting Section 501(r) in 2025**

Despite no published revocations since 2017, tax-exempt hospitals should remain vigilant to avoid slipping into noncompliance with the Section 501(r) requirements. The TE/GE 2025 Program Letter underscores the continued scrutiny and enforcement efforts, which heighten the importance of compliance. With rising operating costs and tight margins, 2025 may be the perfect time for hospitals to review their policies and procedures and ensure full compliance. Nearly half of the hospitals in the US are categorized as tax-exempt and a threat to that status is a significant risk, as the value of these hospitals' federal tax exemptions were estimated to be as much as \$14.4 billion in 2020.

Nixon Peabody attorneys have experience reviewing CHNAs, preparing implementation strategies, drafting FAPs, developing emergency medical care policies, and negotiating agreements with collections agencies, to ensure compliance with Section 501(r) as well as relevant state laws and regulations.

For more information on the content of this alert, please contact your Nixon Peabody attorney or:

**Jennifer A. Jovcevski**

585.263.1344

[jjovcevski@nixonpeabody.com](mailto:jjovcevski@nixonpeabody.com)

**Valerie Breslin Montague**

312.977.4485

[vbmontague@nixonpeabody.com](mailto:vbmontague@nixonpeabody.com)

**Anita L. Pelletier**

585.263.1164

[apelletier@nixonpeabody.com](mailto:apelletier@nixonpeabody.com)

**April E. Schweitzer**

312.977.4365

[aeschweitzer@nixonpeabody.com](mailto:aeschweitzer@nixonpeabody.com)

