

# Nonprofit Hospitals' Community Benefits Come Under IRS Scrutiny

By Owen Racer | July 8, 2024 4:46AM ET

The IRS is getting granular in its look at whether tax-exempt hospitals are living up to their requirement to meet community benefit standards, examining whether nearly three dozen such institutions are providing a broad, loosely defined range of services.

The agency raised questions last month when it [announced it will audit](#) 35 tax-exempt hospitals this fiscal year as part of a stepped-up focus on the sector. The IRS has not historically gone after tax-exempt hospitals for their compliance of community benefit requirements. But after a \$60 billion infusion from the Democrats' 2022 tax-and-climate law, plus congressional pressure to apply greater scrutiny toward tax-exempt hospitals, the IRS is taking a closer look that could potentially ripple across an industry exempt from tens of billions of dollars in federal taxes.

"Community benefit" is described vaguely on the IRS's Form 990, but is generally understood to encompass unreimbursed Medicaid services, research, and subsidized health services. The IRS is required to review hospitals' community benefit activities at least once every three years, though a [2023 report](#) by the Government Accountability Office found the agency's enforcement on that front has been lacking.

The IRS declined to specify what triggered this new round of examinations. But the process could result in both a slap on the wrist for the few hospitals selected for audit, and also an effect of voluntary compliance from the nearly 3,000 other tax-exempt hospitals nationwide, tax experts said.

Ge Bai, an accounting and health policy professor at Johns Hopkins University, expects the hospitals being audited to receive a "do better" message. Meghan Biss, a former tax-exempt adviser at the IRS for over a decade who is now a partner in Loeb & Loeb LLP's tax-exempt practice, anticipates the IRS will see a wave of tax-exempt hospitals not under review start complying.

The estimated value of tax exemption for the country's 2,987 nonprofit hospitals totaled nearly \$28 billion in 2020, [according to KFF](#). Former IRS officials say this new round of audits could reverberate across the industry.

“When you look at 35 hospitals as a percentage of the total number of examinations, that seems like a much higher percentage and signals that this is a place where the IRS is taking things seriously and where organizations should be paying attention,” Biss said.

Preston Quesenberry, a former tax-exempt official with the IRS who is now a managing director in KPMG’s Washington National Tax Office, said he’s surprised the IRS is focusing on community benefit because he’s not seen the agency concentrate on the specific compliance category before.

### Requirement Started in 2009

Tax-exempt hospitals have been requested to provide the IRS information about how they calculate the cost of facilities reported under the community benefit section of their tax returns, particularly line seven on Schedule H of IRS Form 990, according to Quesenberry, who said he spoke with two tax practitioners involved with hospitals being audited by the IRS. Line seven is where hospitals report their “total financial assistance and means-tested government programs,” including Medicaid as well as other community benefits such as research, health professions education, subsidized health services, and cash contributions for community benefit.

“It’s not clear to me what the IRS could or would do in the end as a result of these exams,” Quesenberry said. “Even if they have an appetite to actually go around revoking the tax-exemption of hospitals, which I don’t think they do, it’s not that clear to me that they would have a legal basis to do so based on the community benefit percentage numbers.”

Keith Hearle, who assisted the IRS in drafting instructions for hospitals filling out Schedule H when that requirement went into effect in 2009, said he is aware of one medium-sized urban teaching hospital that’s among the 35 hospitals that received a request for information. Hearle, the president of Verite Healthcare Consulting, said he normally works with that hospital but is not advising it on the audit.

The IRS is trying to be constructive, not punitive, Hearle said, adding that hospitals have had longer than a decade to figure out how to report their community benefit on Schedule H, which was added to Form 990 in 2008. Hearle said the only way he could see the IRS generating revenue from these reviews is if it enforces a \$50,000 fine

looming over hospitals that don't comply with their triennial community health needs assessments. He recommended the IRS update Form 990 to include more write-in answers for hospitals to be able to explain, for example, how many people applied for charity care and why some were rejected and others accepted.

T.J. Sullivan, a former special assistant for health care at the IRS now with Potomac Law Group, said that although it is hard to examine hospitals for community benefit, 35 is a significant number of audits.

### 'Building Trust'

The IRS, which said it will verify whether tax-exempt hospitals are submitting their assessments in addition to meeting community benefit requirements, did not specify which hospitals it is auditing or plans to audit, citing taxpayer confidentiality and disclosure laws.

"We have our tax-exempt division, they are organized to make sure that they have a strong enforcement program, that organizations are operating within their exempt purpose," IRS Commissioner Danny Werfel said after addressing the Tax Policy Center's June conference. "That is not necessarily looking exclusively at the tax gap and the dollars, because the important part of tax administration is building trust."

The nonpartisan Committee for a Responsible Federal Budget said there is insufficient enforcement of nonprofit hospitals' tax-exempt requirements and no "unambiguous federal statutory or regular definition" of community benefits, in a [report](#) released in June. The American Hospital Association, which represents nearly 5,000 nonprofit and for-profit hospitals, [pushed back](#) in June on the report, saying that to repeal a nonprofit hospital's tax-exemption is irresponsible. The association declined a request for comment.

However, some wonder if the audits' scope could expand beyond hospitals' community benefit while many are skeptical about what such audits can lead to or whether the self-reported information and instructions to report it are sufficient.

"We don't know yet," Rep. David Schweikert (R-Ariz.) said, discussing whether the audits will lead to anything. "We can't do that math," he added, referencing the tax code that says community benefit needs to equate or exceed value of tax exemption.

Yet, the 35 audits still came as a surprise to some, including Jessica Lucas-Judy, the GAO director who led the 2023 report.

“I would be very interested to see what the IRS is able to do with audits of the community benefit because what they told us was that it’s not well-defined, kind of a ‘we’ll know it when we see it’ sort of thing,” Lucas-Judy said.