Journal of Contemporary Health Law & Policy (1985-2015)

Volume 26 | Issue 2 Article 7

2010

Non-Profits Under Fire: The Effects of Minimal Charity Care Requirements Legislation on Not-for-Profit Hospitals

James E. Tyrrell III

NON-PROFITS UNDER FIRE: THE EFFECTS OF MINIMAL CHARITY CARE REQUIREMENTS LEGISLATION ON NOT-FOR-PROFIT HOSPITALS

*James E. Tyrrell, III**

America's non-profit hospitals are in jeopardy. Proposed state and federal legislation that would regulate charity care requirements for non-profit hospitals[1] pose a nation-wide threat to the financial stability of these essential institutions. Opponents argue the legislation aimed at requiring non-profit hospitals to increase charity care in exchange for their tax-exempt status will further undermine their precarious financial conditions, threaten their ability to effectively provide services to their communities, and force many to drastically reduce much-needed community services.[2] Proponents of such legislation cite recent reports of drastic increases in net income at the

*James E. Tyrrell, III, is a third-year law student at the Catholic University of America, Columbus School of Law.

1. Illinois General Assembly, Bill Status of HB5000, 96th General Assembly, http://www.ilga.gov/legislation/BillStatus.asp?DocTypeID=HB&DocNum=5000&GAID=8&SessionID=50&LegID=24242 (last visited April 10, 2010). HB 5000 creates the Tax-exempt Hospital Responsibility Act, which provides, "the terms under which a hospital must provide full charity care and discounted care to Illinois residents in order to maintain the hospital's tax-exempt status under the Illinois Income Tax Act, the Use Tax Act, the Service Use Tax Act, the Service Occupation Tax Act, the Retailers' Occupation Tax Act, and the Property Tax Code; amends each of those tax Acts to provide that a hospital may qualify for an exemption from the tax imposed by the Act only if the hospital is in compliance with the Tax-Exempt Hospital Responsibility Act." *Id.* U.S. Senator Chuck Grassley of Iowa pushed for similar federal legislation, which would "require nonprofit hospitals to spend a minimum amount on free care for the poor, also known as charity care." John Carreyrou & Barbara Martinez, *Grassley Targets Nonprofit Hospitals on Charity Care*, WALL ST. J., Dec. 18, 2008, at A5, *available at* http://online.wsj.com/article/SB122957486551517519.html.

2. ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, WHY HB5000 AND HB4999 WILL HARM HOSPITALS AND THE COMMUNITIES THEY SERVE 1, http://www.mchc.com/eweb/docs/newsroom/cfc_iha3.pdf (last visited April 10, 2010) [hereinafter ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER].

fifty largest non-profit hospitals since 2001.[3] However, these advocates fail to acknowledge who will really be harmed as a result of these laws—the small, often rural, and inner-city non-profit hospitals that treat hundreds of thousands of America's sick and injured.[4] At this time of increased health care costs,[5] higher malpractice insurance rates,[6] a likely upsurge in malpractice lawsuits,[7] and a decrease in nursing and physician recruitment,[8]

---

3. John Carreyrou & Barbara Martinez, *Nonprofit Hospitals, Once For the Poor, Strike It Rich*, WALL ST. J., Apr. 4, 2008, at A4, *available at* http://online.wsj.com/article/SB120726201815287955.html.

4. Barbara Martinez, *Pursuing Charitable Mission Leaves a Hospital Struggling*, WALL ST. J., Dec. 12, 2008, at A1. Martinez explains that "[w]hile a number of nonprofit hospitals have grown into profit machines in recent years, some, like Mount Sinai, have stuck to their charitable mission but struggled financially. These institutions are usually located in inner cities and not anchored to big nonprofit systems, nor can they rely on government support the way county or state hospitals can." *Id.*; *see also* Brief for Illinois Hospital Association et al. as Amici Curiae Supporting Respondents at 17, Dep't of Revenue of Ill. v. Provena Covenant Med. Ctr., No. 04-PT-0014 (Ill. Dep't of Revenue Feb. 14, 2005), *available at* http://www.aha.org/aha/advocacy/legal/050214-amicus-brief.pdf.

5. NATIONAL COALITION ON HEALTH CARE, HEALTH CARE FACTS: COSTS 1 (2009), http://nchc.org/sites/default/files/resources/Fact%20Sheet%20-%20Cost.pdf. The National Coalition on Healthcare explains, "[n]ational health expenditures are expected to increase faster than the growth in GDP: between 2008 and 2018, the average increase in national health expenditures is expected to be 6.2 percent per year, while the GDP is expected to increase only 4.1 percent per year." *Id.*

6. Michael Lynch, Opinion, *Cost of Malpractice Insurance Forcing Doctors to Leave High-Risk Specialties*, CONCORD MONITOR, Mar. 13, 2008, at B7, *available at* http://www.concordmonitor.com/apps/pbcs.dll/article?AID=/20080313/OPINION/803130304. Dr. Michael Lynch notes that, "in New Hampshire, many physicians are leaving as malpractice insurance costs soar. Specialty physicians have experienced a 50 percent increase in premiums from five years ago. The average premium is now close to $100,000 for obstetricians and neurosurgeons." *Id.*

7. Gerald O'Malley, Op-Ed, *Thorough Exam Shows Malpractice Lawsuit Abuse Exists*, PATRIOT-NEWS, May 2, 2009, at F3, *available at* http://www.pennlive.com/editorials/index.ssf/2009/05/malpractice_lawsuit_costs_stil.html. "Nearly 40 Pennsylvania hospitals, maternity units and other major medical facilities throughout Pennsylvania have closed in just more than a decade, most under Gov. Ed Rendell's watch. Skyrocketing insurance premiums sparked by rampant medical malpractice lawsuit abuse has been the driving force behind the majority of these closures." *Id.*

the imposition of state or federal legislation creating percentage-based charity care requirements[9] might put many of these hospitals out of business.[10] State legislatures and Congress should abandon such percentage requirements, and explore other available avenues that could provide quality healthcare to the indigent and uninsured.

Part I of this Note offers a brief background on the role of non-profit hospitals and charity care in the United States. It explains both the importance of these institutions in communities throughout the country and emphasizes the necessity of maintaining their tax-exempt status. Part I also illustrates the existing dire financial condition of many non-profit hospitals, resulting from the skyrocketing costs of health care and malpractice insurance, as well as an increase in class action lawsuits fueled by the virtual elimination of charitable immunity in courts throughout the country. Part II of this Note examines current and proposed state legislation requiring non-profit hospitals to perform charity care on a percentage basis, specifically in Texas and Illinois. Part II also considers the United States Congress' attempts to create similar federal legislation. Part III will scrutinize such legislative requirements, and reveal the damaging effects they could have on the stability of non-profit hospitals, particularly in small and inner-city communities. Lastly, Part IV suggests that state legislatures and Congress should address the dilemma of providing health care for the indigent and uninsured in other ways, such as through increased funding for Medicare and Medicaid. This Note will conclude that threatening the tax-exempt status of not-for-profit hospitals will decrease the quality of health care, as

---

8. Will Dunham, *U.S. Healthcare System Pinched By Nursing Shortage*, REUTERS, Mar. 8, 2009, http://www.reuters.com/article/domesticNews/idUSTRE5270VC20090308. Dunham notes:

> The U.S. healthcare system is pinched by a persistent nursing shortage that threatens the quality of patient care even as tens of thousands of people are turned away from nursing schools, according to experts . . . . An estimated 116,000 registered nurse positions are unfilled at U.S. hospitals and nearly 100,000 jobs go vacant in nursing homes, experts said.

Id.; *see generally* NATIONAL RURAL HEALTH ASSOCIATION, RECRUITMENT AND RETENTION OF A QUALITY HEALTH WORKFORCE IN RURAL AREAS (2006), http://www.ruralhealthweb.org/go/left/health-reform-and-advocacy/policy-documents-and-statements/official-policy-positions/official-policy-positions.

9. H.B. 5000, 96th Gen. Assem., (Ill. 2006).

10. Christopher Guadagnino, Opinion, *Lawsuits Indict Hospital Charity Care*, PHYSICIAN'S NEWS DIGEST, Sept. 2004, http://www.physiciansnews.com/2004/09/23/lawsuits-indict-hospital-charity-care/.

well as the facilities in many of these hospitals, and in some cases may cause bankruptcy.

I. THE NOT-FOR-PROFIT HOSPITAL: THE LIFEBLOOD OF AMERICAN HEALTH CARE

A. Non-Profit Hospitals: A Brief Background

Currently, non-profit hospitals comprise more than sixty percent of all hospitals in the United States.[11] The American Hospital Association (AHA) determined that there are "5,708 registered hospitals in the United States. These include 4,897 community hospitals, which are defined as all nonfederal, short-term general, and other special hospitals."[12] Of these, 2,913 are classified as nongovernment non-profit community hospitals.[13] In its 2006 report on community benefit, the Congressional Budget Office (CBO) reported that 51.4 percent of non-profit hospitals were in large urban areas, 34.3 percent were in small urban or suburban areas, and 14.3 percent were in rural areas.[14]

Despite receiving sporadic scrutiny, especially in light of the current health care and financial crises, non-profit hospitals serve a crucial role in the American health care industry.[15] Non-profit hospitals provide a broad range of programs that help the communities they serve, much of which

---

11. Ceci Connolly, *Tax-Exempt Hospitals' Practices Challenged*, WASH. POST, Jan. 29, 2005, at A1; *see also Nonprofit, For-Profit, and Government Hospitals: Uncompensated Care and Other Community Benefits: Hearing Before the U.S. House Committee on Ways and Means,* 109th Cong. 4 (2005) (statement of David M. Walker, U.S. Comptroller General), *available at* http://www.gao.gov/new.items/d05743t.pdf.

12. INTERNAL REVENUE SERVICE, IRS EXEMPT ORGANIZATIONS (TE/GE) HOSPITAL COMPLIANCE PROJECT FINAL REPORT 16 (2009), *available at* http://www.irs.gov/pub/irs-tege/frepthospproj.pdf.

13. *Id.*

14. CONG. BUDGET OFFICE, NONPROFIT HOSPITALS AND THE PROVISION OF COMMUNITY BENEFITS 13 (Dec. 2006), http://www.cbo.gov/ftpdocs/76xx/doc7695/12-06-Nonprofit.pdf.

15. Robert Pear, *Nonprofit Hospitals Face Scrutiny Over Practices*, N.Y. TIMES, Mar. 19, 2006, at 18.

involves charity care to the indigent and uninsured.[16] They also offer additional services, such as community medical screening programs, immunization programs, and health education.[17] They are usually bigger than for-profit hospitals, serve more patients, and are more likely to operate as teaching hospitals.[18] Additionally non-profit hospitals are some of the most effective and comprehensive medical research institutes in the United States.[19]

Non-profit hospitals qualify for federal income tax exemptions under Section 501(c)(3) of the United States Tax Code if they provide health care that helps their surrounding communities.[20] The "community benefit" standard for nonprofit hospitals was last revised in 1969, and continues to be the topic of much debate.[21] However, the IRS set forth its current position on the "community benefit" standard in a 1983 ruling, stating that, "the promotion of health . . . is deemed beneficial to the community as a whole."[22] A September 2004 article in *Healthcare Financial Management* explains that:

> [O]n the basis of this premise, it sets forth a number of criteria for tax exemption. These criteria include the requirements that care be provided to all uninsured patients, including government sponsored patients, and that a full-time emergency department be maintained in which no one requiring emergency care can be denied treatment (although this condition may be waived). . . . However, the IRS did

---

16. ERNST & YOUNG, COMMUNITY BENEFIT INFORMATION FROM NON-PROFIT HOSPITALS: LESSONS LEARNED FROM THE 2006 IRS COMPLIANCE CHECK QUESTIONNAIRE: A REPORT PREPARED FOR THE AMERICAN HOSPITAL ASSOCIATION i-ii (2006), *available at* http://www.aha.org/aha/content/2006/pdf/061127-ErnstYcombenreport.pdf.

17. *Id.* at ii.

18. Internal Revenue Service, *supra* note 12, at 17.

19. ERNST & YOUNG, *supra* note 16, at 4.

20. *Id.* at 1; *see* 26 U.S.C. § 501(c)(3) (2006).

21. Carreyrou & Martinez, *supra* note 3.

22. Lisa Simonson Maiuro et al., *Endangered species? Not-for-Profit Hospitals Face Tax-Exemption Challenge: How Can You Maintain Your Organization's Tax-Exempt Status? One Way is to Participate in the Debate Over How to Measure Charity Care and Community Benefits, Healthcare Financial Management*, 58 HEALTHCARE FIN. MGMT., Sept. 1, 2004, at 74, *available at* http://findarticles.com/p/articles/mi_m3257/is_9_58/ai_n6210271.

> not clearly define 'community benefits' expected of not-for-profit hospitals. This imprecision has prompted researchers to investigate the commitment of not for profit hospitals to their communities and states.[23]

States have adopted similar standards. In Illinois, courts and regulators consider a number of factors in determining the "community benefit" requirement that hospitals must maintain to continue their tax-exempt status—including subsidized health services, education, government sponsored health care, donations, volunteers, research, charity care, bad debt, and language assistance services.[24]

B. The Importance of Tax-Exemption for Non-profit Hospitals

Many non-profit hospitals are having a hard time meeting their mandated charity requirements in the face of various economic strains, including a lack of entirely publicly funded hospitals, "reimbursements not keeping pace with rising costs, malpractice costs spiraling, a nursing shortage, and rising nurse and physician recruitment costs."[25] In Pennsylvania, for example, seventy percent of non-profit hospitals were not reimbursed for the total amount of money they spent on patient care and forty-eight percent lost money as a whole in 2003.[26] Moreover, health care cost inflation has continued to exceed the general inflation rate.[27] With the amount of uninsured Americans surpassing forty-six million, there is a greater demand for health care on a charity basis or at a discounted rate.[28] Although some of the larger non-profit hospitals concentrated primarily in urban areas can handle this influx, the smaller, often rural and inner-city non-profit hospitals

---

23. *Id.*

24. ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2, at 1.

25. Guadagnino, *supra* note 10.

26. *Id.*

27. Mary A. Crossley, *Non-Profit Hospitals, Tax Exemption and Access for the Uninsured: Pitt Health Law Certificate Program 10th Anniversary Symposium*, 2 PITT. J. ENVTL. & PUB. HEALTH L., 1, 3 (2007).

28. *Id.*; *see also* Ceci Connolly, *Proportion of Doctors Giving Charity Care Declines; Busy Schedules, Lower Reimbursements and High Medical-School Debt Cited as Factors*, WASH. POST, Mar. 23, 2006, at A9.

are fighting to remain solvent.[29] In Chicago, for example, Mount Sinai Hospital struggles to maintain its operations while also providing the necessary community benefit and charity care that allows the hospital to retain its tax-exempt status.[30] A 2008 *Wall Street Journal* article explains that:

> Mount Sinai has teetered between a small net income and annual losses as high as $15 million over the past five years. While some large nonprofit hospitals have amassed billions of dollars in reserves, Mount Sinai's days of cash on hand—a common gauge of a hospital's solvency—is sometimes measured in hours . . . . Mount Sinai's struggles reflect in part a paucity of government incentives for nonprofit hospitals to operate in inner cities.[31]

Mount Sinai, "spent $16.6 million on charity care [in 2007] and another $16.2 million to subsidize specialists, such as cardiologists, who wouldn't otherwise work in the neighborhood because reimbursements are so low."[32] At the same time, Mount Sinai's facilities are derelict at best, as the hospital had to delay or suspend investing in new technologies.[33] Mount Sinai is one of many smaller, less adequately funded non-profit hospitals in the country that struggle to fulfill their obligations under their tax-exempt status, at the cost of health care quality and modernizing facilities. The imposition of minimum charity care requirements would cause these institutions irreparable damage, as they would no longer be able to function in the lower socio-economic neighborhoods and communities that depend on them.

C. Class Action Lawsuits and the Death of Charitable Immunity

The financial stability of non-profit hospitals is further threatened by an increase in class action lawsuits and by plaintiffs' ability to sue these hospitals for medical malpractice and alleged predatory collection methods. Congressional hearings in the last five years on the pricing, billing, and collection practices related to the uninsured at non-profit hospitals have

29. Martinez, *supra* note 4.

30. *Id.*

31. *Id.*

32. *Id.*

33. *Id.*

triggered great interest by the plaintiffs' bar.[34] In 2004, more than fifty class action lawsuits were filed, alleging that non-profit "hospitals engage in business methods calculated to defeat the rights of uninsured patients, and that they perform 'wallet biopsies' on uninsured patients by gouging them with exorbitantly inflated prices."[35] Although some of these lawsuits have merit,[36] many are designed or undertaken to pad the pockets of trial lawyers, which ultimately serve only to threaten the financial stability of non-profit hospitals.[37] For instance, in 2004, one non-profit health system in Mississippi agreed to a 150 million dollar settlement.[38]

Class-action and medical malpractice lawsuits are further fueled by the virtual elimination of the defense of charitable immunity in state and federal courts throughout the country. Before 1940, most hospitals received protection against liability through the doctrine of charitable immunity, which shielded "hospitals from the acts of its employees by limiting the amount of damages to a minimal amount."[39] Over the past few decades,

---

34. *See generally Taking the Pulse of Charitable Care and Community Benefits at Nonprofit Hospitals, Hearing Before the U.S. Senate Finance Committee*, 109th Cong. (2006) (statement of Senator Grassley, Chairman, Senate Finance Committee); Guadagnino, *supra* note 10.

35. Guadagnino, *supra* note 10.

36. Jean Hellwege, *Class Actions Charge Nonprofit Hospitals With Unfair Billing, Collection*, TRIAL, Sep. 1, 2004, *available at* http://www.accessmylibrary.com/coms2/summary_0286-13426336_ITM. In one reported case, a 77-year-old man was still paying his dead wife's bill for cancer treatment she had received 20 years before. Even though the man was making court-ordered payments on the debt, the hospital had seized $10,000 from his bank account and had placed a lien on his house. Interest charges drove the original $20,000 bill to $39,000, although the man had paid $16,000 over the years. *Id.*

37. Guadagnino, *supra* note 10.

38. Press Release, The Scruggs Law Firm, P.A., Largest Rural Non-Profit Hospital in North America Becomes First To Reach Settlement with Uninsureds (Aug. 4, 2004), http://www.cliffordlaw.com/not-for-profit-hospital-class-action-litigation/press-releases/largest-rural-nonprofit-hospital-in-north-america-becomes-first-to-reach-settlement-with-unisureds.

39. Thuy Wagner, *Hospitals: Court Rejects Charitable Immunity Defense and Holds Hospital Liable—Keene v. Brigham & Women's Hosp., Inc.*, 26 AM. J. OF LAW & MED. 319, 319 (2000), *available at* http://www.allbusiness.com/legal/3587373-1.html.

several courts have eliminated this defense.[40] In 2000, for example, the Superior Court of Massachusetts awarded an estimated $6.5 million to the family of a boy who suffered from brain damage shortly after he was born, despite the fact that Massachusetts' charitable immunity law capped medical malpractice awards at 20,000 dollars against non-profit hospitals.[41] The court's ruling is indicative of the nationwide elimination of charitable immunity laws. The phasing out of such laws will make non-profit hospitals more vulnerable at a time when hundreds of these hospitals face financial difficulties.[42]

II. IMPOSING A LEGISLATIVE FLOOR: PERCENTAGE BASED CHARITY CARE REQUIREMENTS FOR NON-PROFIT HOSPITALS

A. State Legislation

In response to media reports that some of the larger non-profit hospitals were not performing enough public services to warrant their tax-exempt status, several state legislatures have implemented or proposed percentage-based charity care requirements.[43] In 1993, Texas was the first state to actually implement these types of charity care requirements, but the law had little impact on the overall charity care spending in that state.[44] Perhaps the most ambitious proposed legislation took place in Illinois in 2006, with Attorney General Lisa Madigan's proposed Tax-Exempt Hospital

---

40. *Id.*

41. *Id.*; *see also* Keene v. Brigham & Women's Hosp., Inc., 786 N.E.2d 824, 826-27 (Mass. 2003).

42. Guadagnino, *supra* note 10.

43. Carreyrou & Martinez, *supra* note 3. "The combined net income of the 50 largest nonprofit hospitals jumped nearly eight-fold to $4.27 billion between 2001 and 2006, according to a Wall Street Journal analysis of data from the American Hospital Directory." *Id.*; *see generally* MISSOURI FOUNDATION FOR HEALTH, ISSUE OVERVIEW: HOSPITAL CHARITY CARE IN THE UNITED STATES 7-13 (2005), http://www.mffh.net/mm/files/HospitalChairtyCareIssueBrief.pdf.

44. TEX HEALTH& SAFETY CODE ANN. § 311.031 (Vernon 2009); *see also* Frances A. Kennedy, et al, *Do Non-profit Hospitals Provide More Charity Care When Faced with a Mandatory Minimum Standard? Evidence from Texas*, J. ACCOUNT. PUBLIC POLICY (forthcoming 2009) (Draft at 4, on file with author).

Responsibility Act.[45] Although the bill stalled in the Illinois House in 2007,[46] its proposals represent a growing trend in the way state legislatures have been approaching the non-profit charity care issue.

B. The Texas Model

In response to complaints that non-profit hospitals were not living up to their charitable obligations and should not continue to receive tax-exemption, the Texas legislature passed legislation in 1993 requiring non-profit hospitals to spend a minimum four percent of their annual revenues on charity-care.[47] Specifically, a lawsuit filed by the Texas Attorney General against The Methodist Hospital in Houston generated the legislation.[48] In the suit, the Attorney General alleged that Methodist "failed as a charitable hospital 'to provide its required share of health care for poor people,'" and that "the hospital had the duty under law to provide 'charity care in an amount commensurate with its resources, the tax-exempt benefits received, and the needs of the community.'"[49] Despite the Attorney General's

---

45. Illinois General Assembly, Bill Status of HB5000, 96th General Assembly, http://www.ilga.gov/legislation/BillStatus.asp?DocTypeID=HB&DocNum=5000&GAID=8&SessionID=50&LegID=24242 (last visited April 10, 2010); *see also* Press Release, Ill. Att'y Gen. Lisa Madigan, Madigan Proposes Two Bills to Hold Hospitals Accountable for Charity Care, Stop Unfair Billing and Collection Practices (Jan. 23, 2006), *available at* http://www.illinoisattorneygeneral.gov/pressroom/2006_01/20060123.html.

46. *See* Delia D. Johnson, Comment, *The Economic Benefit of Nonprofit Hospitals: Broadening the Evaluation of Tax-Exempt Status at the State Level*, 53 WAYNE L. REV. 1583, 1592 (2007).

47. TEX. HEALTH & SAFETY CODE ANN. § 311.045 (Vernon 2009).

48. *See generally* Kevin M. Wood, *Legislatively-Mandated Charity Care for Nonprofit Hospitals: Does Government Intervention Make Any Difference?*, 20 REV. LITIG. 709, 725 (2001); *see generally* Texas v. The Methodist Hosp., No. 494,212 (126th Dist. Ct., Travis County, Tex. Feb. 19, 1993).

49. Craig E. Bain, Alan I. Blankley & Dana A. Forgione, *The Methodist Hospital System: Tax Exemption and Charitable Responsibilities of Not-for-Profit Hospitals*, 16 ISSUES IN ACCOUNTING EDUCATION 67, 71, Feb. 1, 2001, *available at* http://www.cbe.uidaho.edu/Acct592/CourseMaterials/Cases/Methodist%20Hospital%20Case.pdf; *see generally* Texas v. The Methodist Hosp., No. 494,212 (126th Dist. Ct., Travis County, Tex. Feb. 19, 1993).

arguments, the court ruled that the issue of charity care should be addressed through the legislature, rather than having the judiciary create a rule.[50]

Accordingly, in 1993, the Texas legislature became the first legislative body in the country to craft and pass such percentage-based legislation.[51] The law contained a "narrow definition of charity care, which did not include bad debts," and stated that charity care is the non-reimbursed cost of "providing, funding, or otherwise financially supporting health care services on an inpatient or outpatient basis to persons classified as 'financially or medically indigent.'"[52] Two years later, at the urging of hospital administrators, the legislature amended its 1993 requirements by including bad debts in the four percent charity care calculation.[53]

In a study published in 2009, professors from Clemson University, Mississippi State University, University of North Carolina at Charlotte, and Vanderbilt University sought to analyze the effect of this legislation on Texas' non-profit hospitals and their overall spending on charity care throughout the state.[54] What they found was alarming, and should serve as a warning to other state legislatures and Congress when they consider percentage-based charity care requirements. In fact, their empirical research and analysis confirmed their hypothesis that,

> hospitals which were initially spending below the specified threshold subsequently increased charity care spending as necessary to maintain tax-exempt status. However, [the] results also suggest the Texas law may also cause decreased spending at more affluent hospitals, which were initially spending above the benchmark. As a result, we find little impact on the overall charity care spending of NFPs targeted by the law.[55]

Clearly, this was an "unintended consequence of the legislation," as "overall, the Texas law changes did not, on average, lead to increased

---

50. Kennedy et al., *supra* note 44, at 5.

51. *Id.* at 4.

52. *Id.* at 4-5.

53. *Id.* at 5; *see also* TEX. HEALTH & SAFETY CODE ANN. § 311.031 (Vernon 1995) (implementing the Texas legislature's 1995 amendment that includes bad debts in the charity care net calculation).

54. *See generally* Kennedy et al, *supra* note 44.

55. *Id.* at 2.

charity care spending" by non-profit hospitals.[56] In fact, although the goal of 1993 and 1995 legislation was to increase "charity care spending by those hospitals that had not previously borne their fair share," the total number of dollars spent on charity care decreased.[57] Non-profits that were spending below the minimum set by the legislature increased their charity spending to ensure that they met the new requirements, whereas non-profits already spending more than the four percent requirement decreased their charity care spending to meet or come close to that four percent floor.[58] Consequently, instead of the legislation paving the way for increased overall spending on charity care, the 1993 legislation and 1995 amendment actually decreased the amount of statewide non-profit hospital charity care by 1.2 percent.[59]

Although the Texas legislature did not have this outcome in mind when it crafted the laws in the mid-1990s, the unintended consequences should be a wakeup call to state legislatures around the country and to members of Congress who may seek to implement percentage-based charity care requirements for non-profit hospitals.

C. The Illinois Proposed Model

In 2006, Illinois Attorney General Lisa Madigan proposed legislation called The Tax-Exempt Hospital Responsibility Act (the Act).[60] It is even more ambitious than Texas' 1993 law, as it sets forth charity care requirements that Illinois' non-profit hospitals must meet to ensure that they continue to receive tax-exempt status.[61] Specifically, the Act mandates that Illinois' non-profit hospitals deliver charity services that are at least equivalent to eight percent of their total annual operating cost.[62] Under the law:

---

56. *Id.* at 1.

57. *Id.* at 15.

58. *Id.*

59. *Id.*

60. H.B. 5000, 96th Gen. Assem. (Ill. 2006).

61. *Id.*; *see also* Press Release, Ill. Att'y Gen. Lisa Madigan, *supra* note 45.

62. *See generally Proposed Tax-Exempt Hospital Responsibility Act Creates Charity Care Requirements*, MCDERMOTT NEWSLETTERS (McDermott Will & Emery), Jan. 31, 2006, http://www.mwe.com/index.cfm/fuseaction/publications.nldetail/object_id/10ad7114-72e4-4be3-b8d6-5f6cbd0e4151.cfm.

> Charity care is defined as medically necessary services provided at a reduced charge or no charge to patients who meet eligibility criteria no more restrictive than the following: free care (full charity care) must be provided to uninsured Illinois residents below 150 percent of the federal poverty level (FPL), and discounted care must be provided to those between 150 percent and 250 percent of the FPL. Discounts are defined as discounts from costs, not charges, and the amount charged to financially eligible families cannot exceed 35 percent of the costs of care.[63]

Under the proposed bill, Illinois' non-profit hospitals would be required to provide percentage based "charity care," in exchange for their tax-exempt status.[64] This charity care requirement marks a significant departure from the "community benefit" standard that the Supreme Court of Illinois has consistently applied for nearly a century in determining the charitable purposes of the organization in relation to tax-exempt status.[65] Under the "community benefit" standard, courts take into account a number of factors "that contribute to the well-being of the community" in determining whether a hospital should enjoy tax-exempt status, including subsidized health services, education, government sponsored health care, donations, volunteers, research, charity care, bad debt, and language assistance services.[66] The legislation ignores all of these factors, other than charity care, in its proposed method to determine whether to grant tax-exempt

---

63. *Id.* For example:

> If a patient in a family of four with income of $45,000 to $50,000 (falling between 225 percent and 250 percent of the FPL) incurs hospital charges of $5,000 representing $3,000 in cost (depending on the hospital's Medicare cost-to-charge ratio), the patient's bill cannot exceed 35 percent of cost or $1,050. In addition, if the cost of care exceeds $10,000 in a 12-month period, the patient is eligible for full charity care for the remainder of the 12-month period.

Id.

64. *Id.*

65. Methodist Old People's Home v. Korzen, 233 N.E.2d 537, 541 (Ill. 1968); People ex. rel Hellyer v. Morton, 25 N.E. 2d 504, 506 (Ill. 1940) (noting exemptions for charitable organizations are based on the benefits that the public receives from the institution); Congregational Sunday Sch. & Publ'g Soc'y v. Board of Review, 125 N.E. 7, 10 (Ill. 1919) (finding the benefit conferred on the public is the measure of charity for the purposes of tax exemption).

66. *See* H.B. 5000, 96th Gen. Assem. (Ill. 2006); *see also* ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2, at 1.

status.[67] Conceivably, a non-profit hospital could provide much-needed community medical and immunization clinics, act as a leader in disease research, and provide numerous education programs on disease prevention, all free-of-charge to the public, and, under this proposed legislation, the hospital would not qualify for tax-exemption.[68] Such "charity care" requirements are impractical and misguided.

D. Provena Covenant Medical Center v. Department of Revenue: A Landmark Case Emerges in Illinois

In *Provena Covenant Medical Center v. Department of Revenue*,[69] a non-profit hospital's tax-exempt status as a charitable institution was challenged for the first time.[70] In *Provena*, the Illinois Department of Revenue challenged Provena Covenant's application for an exemption from property taxes on the basis that the hospital had not provided enough charity care to warrant its status as a non-profit.[71] According to a brief filed by Attorney General Lisa Madigan, in which she describes the state's position, the hospital "concealed the availability of charity care to poor patients and 'expected payment from nearly everyone who came through its doors, even if they were poor.'"[72] Despite such assertions, Provena Covenant protested its property taxes by maintaining that its charitable purposes and religious affiliation qualified the hospital for property tax exemptions.[73] Moreover,

---

67. *See generally* H.B. 5000, 96th Gen. Assem. (Ill. 2006).

68. *See* ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2, at 1.

69. *See generally* Provena Covenant Med. Ctr. v. Dep't of Revenue, 894 N.E.2d 452 (Ill. App. 2008).

70. *Id.* at 456-57.

71. *Id.* at 455; *see generally* Katie Stewart, *Property Tax Exemptions for Nonprofit Hospitals: The Implications of Provena Covenant Medical Center v. Department of Revenue*, 62 TAX L. 1157, 1172-73 (2009), *available at* http://www.abanet.org /tax/pubs/ttl/624su09/7-Stewart.html.

72. Lindsey Tanner, *Fight over hospital tax breaks goes to Illinois Supreme Court*, ST. J. REGISTER, Sep. 24, 2009, at 23, *available at* http://www.sj-r.com /breaking/x2024002366/Fight-over-hospital-tax-breaks-goes-to-Illinois-Supreme-Court.

73. *Provena*, 894 N.E.2d at 456-57; Samuel Rosenberg, *Grey Area Anatomy: Tax Exemptions for Nonprofit Hospitals*, ILL. BUS. L. J., Feb. 22, 2009, http://www.law.uiuc.

"Provena [argued] that it is a charitable organization because [it] provide[s] the community with the invaluable service of health care."[74] The appellate court, however, "[f]ocused upon the charitable purpose claim [and the determination] . . . that Covenant devoted only 0.7% of its total revenue to charity."[75] Moreover, the Illinois Court of Appeals disagreed with Provena Covenant's argument, declaring that "[b]y holding medical care to be, in and of itself, charity, we effectively would excuse charitable hospitals from their ongoing mission of giving."[76]

Provena Covenant appealed the decision of the appellate court and oral arguments were heard before the Illinois Supreme Court in September 2009.[77] In March, 2010, the Illinois Supreme Court affirmed the decision of the appellate court.[78] In doing so, the Illinois Supreme Court said that Provena Covenant "failed to show by clear and convincing evidence that it . . . dispensed charity to all who needed it and applied for it and did not appear to place any obstacles in the way of those who needed and would have availed themselves of the charitable benefits it dispenses."[79] Many believe that the Illinois Supreme Court's decision will determine how non-profit hospitals throughout the country will be treated.[80] It could set a precedent for additional state and federal percentage-based charity care requirement legislation, which would threaten the financial stability of non-profit hospitals and severely limit the resources used by them to serve their communities.

---

edu/bljournal/post/2009/02/22/Grey-Area-Anatomy-Tax-Exemoptions-for-Nonprofit-Hospitals.aspx.

74. Rosenberg, *supra* note 73; *see also* Provena Covenant Med. Ctr. v. Dep't of Revenue, 894 N.E.2d 452, 464 (Ill. App. 2008).

75. Rosenberg, *supra* note 73 (citing *Provena,* 894 N.E.2d at 456-57).

76. *Provena*, 894 N.E.2d at 465.

77. *See generally* Provena Covenant Med. Ctr. v. Dep't of Revenue, 900 N.E.2d 1126 (Ill. 2009).

78. *See generally* Provena Covenant Med. Ctr. v. Dep't of Revenue, 2010 Ill. LEXIS 289 (Ill. 2010).

79. *Provena*, 2010 Ill. LEXIS 289, at *33-34.

80. Rosenberg, *supra* note 73.

E. Federal Legislation in the Works

As a result of proposed legislation in Illinois and the enactment of percentage-based charity care requirements for non-profit hospitals in other states, the issue of non-profit hospital charity care has spurred the attention of federal lawmakers.[81] U.S. Senator Chuck Grassley of Iowa has led the movement for percentage-based requirements.[82] As is the case in Illinois, Grassley's proposed legislation "would require nonprofit hospitals to spend a minimum amount on free care for the poor, also known as charity care, and [would] set curbs on executive compensation and conflicts of interest."[83] According to Grassley, "under the new legislation, penalties would be imposed on non-profit hospitals that fail to meet the new requirements . . . penalties could escalate from taxes and fines to stripping a hospital of its federal-tax exemption if it continues to misbehave."[84] Specifically, Grassley has endorsed the idea that non-profit hospitals should be spending "at least 5 percent of their patient revenue on charity care."[85] Grassley's proposed legislation remains open-ended to date, and it was not a part of Congress' recent passage of the Patient Protection and Affordable Care Act,[86] but percentage-based charity care requirements continue to be a possibility.[87]

Furthermore, Congress has chosen to narrowly focus the debate dealing with tax-exempt non-profit hospitals on charity care alone, and has not included the wide range of services non-profit hospitals offer to their

---

81. Carreyrou & Martinez, *supra* note 3.

82. *Id.*

83. *Id.*

84. *Id.*

85. Anne Zieger, *New Measure Would Set Minimum Charity Levels for Non-profit Hospitals*, FierceHealthFinance.com, Dec. 24, 2008, http://www.fiercehealthfinance.com/story/new-measure-would-set-minimum-charity-levels-non-profit-hospitals/2008-12-24?utm_medium=nl&utm_source=internal&cmp-id=EMC-NL-FHF&dest=FHF (last visited March 22, 2010).

86. *See infra* Addendum; *see generally*, Patient Protection and Affordable Care Act, Pub. Law No. 111-148 (2009).

87. *See infra* Addendum.

surrounding communities in this discussion.[88] Such a myopic approach to the debate ignores the countless benefits that non-profit hospitals provide for their areas, beyond offering free health care. In a letter to U.S. Senator Max Baucus, Chairman of the Senate Finance Committee, Richard Clarke, president of the Heathcare Financial Management Association (HFMA), maintains that "[t]he discussion should be broadened to consider hospitals' organizational attributes, the full range of societal benefits provided, and possible negative consequences of revoking not-for-profit hospitals' tax-exempt status."[89] It is yet to be seen whether Congress will address this issue aside from the recently passed Patient Protection and Affordable Care Act,[90] but it is clear that "[f]ailure to recognize the broad basis of community benefit could lead to a specific trade-off, which would undermine important and cumulative community benefits that tax-exempt healthcare institutions deliver."[91] Accordingly, if Congress were to focus solely on charity care as the basis for determining whether a community benefit warrants tax-exemption, it would ignore crucial parts of the equation, such as non-profit hospitals' willingness to reduce the government burden, provide essential health care services, offer unprofitable services, supply public education, and serve other unmet human needs.[92]

With regard to reducing the government burden, Clarke explains that "[m]any tax-exempt hospitals provide services that federal, state, and local government otherwise would have to provide. Services especially demanded from tax-exempt healthcare providers include high-tech, high-intensity services, emergency care, chronic care, and long-term care."[93] Likewise, with respect to non-profit hospitals giving essential health care services, "[t]ax-exempt healthcare providers are often the sole providers of healthcare services that are so essential to community health that tax-exempt

88. Letter from Richard L. Clarke, President & Chief Executive Officer, Healthcare Financial Management Association, to the Honorable Max Baucus, Chairman, Senate Committee on Finance (June 18, 2009), *available at* http://www.hfma.org/library/compliance/taxexempt/400662.htm [hereinafter Richard L. Clarke Letter].

89. *Id.*

90. *See generally* Patient Protection and Affordable Care Act, Pub. Law No. 111-148.

91. Richard L. Clarke Letter, *supra* note 88.

92. *Id.*

93. *Id.*

status is warranted. Examples of essential services include emergency rooms and outpatient clinics serving low-income patients."[94] As for non-profits' willingness to engage in services that do not garner a profit, this "is commonly a provider's charitable response to a community need. Unprofitable services in this sense lose money because of high costs combined with low volume or inadequate payment rather than inefficient operations. Common examples of unprofitable services include burn, neonatal, and trauma centers and community mental health centers."[95] Education in these institutions is also not limited to teaching and training doctors and nurses: rather, "[m]ost tax-exempt healthcare providers . . . also provide a range of educational programs to enhance public health. Examples of such programs include public health education, wellness programs, and the sponsorship of educational activities."[96] Lastly, many non-profit hospitals are essential in providing services that are otherwise unavailable to the general public, such as "senior citizen education and outreach programs, care for 'boarder' babies, or the operation of a 'meals on wheels' program."[97] If Congress wants to reform the tax-exemption standards for non-profit hospitals, they must take into account these essential programs and not focus solely on the amount of so-called charity care these institutions perform.

III. PERCENTAGE-BASED CHARITY CARE REQUIREMENTS: A FINANCIAL CALAMITY FOR NON-PROFIT HOSPITALS

A. Percentage-based Requirements Would Trigger a Financial and Health Care Disaster

The imposition of percentage-based charity requirement legislation, similar to bills proposed in Illinois and by Senator Grassley, would threaten

---

94. *Id.*

95. *Id.*

96. *Id.*

97. Richard L. Clarke Letter, *supra* note 87. According to the National Abandoned Infants Assistance Resource Center, "Boarder babies are infants under the age of 12 months who remain in the hospital past the date of medical discharge. Boarder babies may eventually be claimed by their parents and/or be placed in alternative care." NATIONAL ABANDONED INFANTS ASSISTANCE RESOURCE CENTER, BOARDER BABIES, ABANDONED INFANTS, AND DISCARDED INFANTS 1 (2005), http://aia.berkeley.edu /media/pdf/abandoned_infant_fact_sheet_2005.pdf.

the financial stability of many non-profit hospitals throughout the country.[98] Although some of the larger non-profit hospital systems can bear the costs of such requirements, the majority of non-profit hospitals simply cannot afford it.[99] Professor John Colombo of the University of Illinois College of Law notes that "this approach is problematic because non-profit hospitals do not have enough resources, specifically money, to care for the estimated 46 million uninsured people throughout the country."[100] Moreover, Professor Colombo believes that a percentage-based or strict charity care standard could devolve into "a social aid system like the federal Food Stamp Program."[101]

In Illinois, for instance, the proposed Tax-Exempt Hospitals Responsibility Act would require 133 non-profit hospitals to spend 739 million dollars more on charity care, based on data from 2003.[102] This would essentially "wipe out the aggregate bottom line" of those hospitals, resulting in "expenses that are higher than their revenues."[103] Furthermore, it would cause forty-five of Illinois' non-profit hospitals to be placed into debt, and move twenty-eight already financially-strapped hospitals one step closer to bankruptcy.[104] The problem that arises when hospitals go further into debt is that they "cannot merely raise prices" because a large portion of their prices are paid for by Medicare and Medicaid, which does not even pay the fees for services provided.[105] Less financially stable non-profit hospitals

---

98. *See generally* ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2.

99. *Id.* at 2.

100. *See generally Non-Profit Hospitals' Tax-Exempt Status Under Fire From IRS, Local Governments*, ILL. BUS. L. J., Oct. 20, 2006, *available at* http://iblsjournal.typepad.com/illinois_business_law_soc/2006/10/nonprofit_hospi.html.

101. *Id.*

102. ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2, at 2.

103. *Id.*

104. *Id.* "These 28 hospitals that are already losing money have an aggregate bottom line of *negative $254 million*. HB 5000 will require these 28 hospitals to spend an additional $158 million on charity care, resulting in a new combined margin of *negative $411 million*." *Id.*

105. *Id.* According to the Illinois Hospital Association:

would be unable to sustain their operations and would ultimately be forced to eliminate valuable medical services and investments in facilities and technology merely to meet a percentage requirement of charity care for indigent patients.[106]

B. The Real Victims: Small Inner City and Rural Community Non-profit Hospitals

In theory, percentage-based charity care requirements serve a valid purpose by mandating certain amounts of much-needed health care to the indigent and uninsured.[107] In practice, however, because non-profit hospitals throughout the country vary greatly in size and purpose, an imposition of blanket percentage-based charity requirements would affect some of these hospitals more than others.[108] While some of the country's non-profit hospital systems and conglomerates could likely bear the financial brunt of such requirements, it is the smaller inner city and rural non-profit hospitals that would be hurt the most.[109]

In Illinois, twenty-eight already struggling hospitals would be forced closer to bankruptcy, as they would have to spend "an additional $158

> [i]ncreasing rates to cover these new financial burdens required by HB 5000 . . . would represent an enormous cost shift from the public sector to the private sector. If hospitals were to just break even, they would have to shift millions of dollars in costs to insured patients, at a time when more and more businesses are reducing their commitment to providing workplace insurance for employees. This is a perfect formula for bringing our present system of financing health care in this state to its knees. Therefore, if as a practical matter hospitals are unable to shift those costs, those hospitals losing money will have to reduce expenses by eliminating services (e.g., trauma, emergency care, burn units, neonatal intensive care units), reducing staff (nearly 50% of the average hospital's expense is personnel), foregoing building and equipment upgrades, postponing quality improvements (e.g., electronic health records) and other measures that directly affect the hospital's ability to serve their community.

Id.

106. *Non-Profit Hospitals' Tax-Exempt Status Under Fire From IRS, Local Governments*, *supra* note 100.

107. *See* Carreyrou & Martinez, *supra* note 3.

108. *See* Robert Pear, *Hospitals Mobilizing to Fight Proposed Charity Care Rules*, N.Y. TIMES, June 1, 2009, at A12.

109. *Id.*

million on charity care," bringing their aggregate bottom line to negative 411 million dollars.[110] Mount Sinai in Chicago is one such struggling hospital.[111] While it is a small inner city hospital that has maintained its charitable mission, it struggles to do so in light of dwindling finances due to increased health care costs and the shift of financial resources to larger non-profit hospital systems, such as the University of Chicago.[112] An additional percentage-based charity requirement could have dire consequences for the hospital, as its "days of cash on hand—a common gauge of a hospital's solvency—is sometimes measured in hours."[113]

Similarly, Swedish Providence Medical Center, a non-profit hospital outside of Seattle, has seen sharp increases in charity care expenditures.[114] A 2006 article in the *Puget Sound Business Journal* explains that "in the mid-1990s, hospitals in Washington typically paid a little more than 2 percent of their adjusted revenue (revenue minus Medicare and Medicaid charges). At the same time, their operating margins averaged around 2 percent."[115] More recently, however, hospitals like Swedish Providence have seen their expenses for charity care rise to almost five percent of their adjusted revenue.[116] In fact, in 2004, Swedish Providence spent more than sixteen million dollars in charity care.[117] Such costs at non-profit hospitals like Swedish Providence "[put] a dent in their reserves—their cash balance at the end of each year. Nonprofits use that for investing in new equipment, expanding facilities or hiring new staff."[118] It is reasonable to assume that

---

110. ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2, at 2.

111. Martinez, *supra* note 4.

112. *Id.*

113. *Id.*

114. Douglas Gantenbein, *Hospitals Giving More Charity Care—'Til It Hurts*, PUGET SOUND BUS. J., Oct. 27, 2006, at 34, *available at* http://seattle.bizjournals.com/seattle/stories/2006/10/30/focus13.html.

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.*

the imposition of a percentage-based charity requirement, such as the eight percent proposed in Illinois, would have dire financial consequences for a hospital like Swedish Providence, which is already stretched thin. An eight percent requirement would certainly limit a hospital's ability to update facilities and better its technology, things that benefit patients in the long-term.[119]

C. Revocation of Non-Profit Hospitals' Tax-Exempt Status: Dire Consequences for Communities

If States and Congress were to impose strict charity-care requirements in exchange for non-profit hospitals' tax-exempt status, hospitals and the communities surrounding them would be negatively affected.[120] In fact, if non-profit hospitals lost their tax-exempt status as a result of such narrowly centered legislation, it "would have serious implications for hospitals' operating and capital expenditures that will ultimately impact the well-being of their communities."[121] HFMA President Richard Clarke again explains, with regard to non-profit hospitals' operating expenditures, that "[h]ealthcare services by their nature are labor intensive, therefore any reduction in community benefits required to satisfy new income tax liabilities will ultimately result in job losses. This is especially deleterious in rural communities where hospitals are an important source of good jobs with stable benefits."[122] Therefore, not only would the imposition of such legislation affect smaller urban and rural non-profit hospitals' ability to pay for innovation, technology, and general upkeep of their facilities, but it would also force these institutions to cut jobs and eliminate their payroll expenses.[123] In a time of record unemployment and financial crisis, especially throughout the rural parts of the country, this is hardly the message that legislators should be sending to health care workers. Clarke goes on to explain that "individual states will further exacerbate this financial impact as they levy property taxes on all hospitals, not just profitable ones. This has the potential to push unprofitable hospitals into bankruptcy, resulting in additional job losses and reduced access to care for

---

119. *Id.*

120. Richard L. Clarke Letter, *supra* note 88.

121. *Id.*

122. *Id.*

123. *Id.*

all members of the community."[124] Therefore, not only would the federal government be able to tax non-profit hospitals freely if their tax-exemptions were revoked through such legislation, but states would also be free to impose property taxes on them, risking insolvency and ultimately resulting in countless job losses.

Moreover, with regard to capital expenditures, if non-profit hospitals were to lose their tax-exempt status as a result of minimal charity-care legislation, "access to two important sources of financing necessary to meet capital needs would either be severely reduced or eliminated."[125] First, Clarke notes, "it is widely anticipated that charitable donations used to fund both capital improvements and community programs would be redirected to other organizations that can provide donors with an income-tax shield."[126] It is foolish to believe that the majority of large donors would continue to donate to hospitals if they were no longer considered charitable institutions under Section 170 of the Internal Revenue Code, since those donors would no longer receive a tax-deduction. Second, Clarke makes clear that:

> not-for-profit hospitals would be precluded from accessing municipal capital markets. This would drive up the cost of capital (and ultimately the cost of providing care) as investors demanded higher returns to compensate for the lack of preferential tax treatment on municipal bond coupon payments. Additionally, it could also trigger call provisions embedded in existing debt covenants requiring hospitals to immediately repay outstanding debt. Under this scenario, even hospitals with strong balance sheets would struggle to meet their obligations and avoid bankruptcy.[127]

Certainly, if non-profits were to lose their tax exemption status, not only would donors no longer be allured by the possibility of receiving tax-deductions, but hospitals would also be treated as for-profit entities with obligations to repay debts sooner and satisfy investors. Consequently, their cash-on-hand would be eliminated and their ability to innovate, expand, create jobs, and effectively service patients would ultimately be finished.

Ironically, if Congress were to impose charity-based requirements that stripped non-profit hospitals of their tax-exempt status, "Congress would not only weaken the safety net that the most vulnerable in our communities rely

---

124. *Id.*

125. *Id.*

126. Richard L. Clarke Letter, *supra* note 88.

127. *Id.*

upon for health and wellness services, but would simultaneously increase the number of people dependent on the safety net and reduce services available to all citizens."[128] This cannot and should not result from any legislative effort to "fix" the health care problems in this country.

IV. EXPLORING THE ALTERNATIVES TO PERCENTAGE BASED CHARITY REQUIREMENTS

With approximately forty-six million people living without medical insurance in the United States, the health care industry needs drastic reform.[129] However, the answer cannot lie in the implementation of percentage-based charity requirements, which will harm many of the nation's non-profit hospitals that provide vital services to America's sick and injured.[130]

The most obvious solution is universal health care coverage, "negating the need for charity-care and uncompensated-care programs."[131] However, the Patient Protection and Affordable Care Act, recently passed by Congress and signed into law by President Obama, does not provide complete universal coverage, and does not include a public health insurance option.[132]

A more practical solution would be to offer increased spending on Medicare and Medicaid, incentivizing hospitals that offer charity care to receive larger reimbursements for expensive care and procedures that they provide to the elderly and indigent.[133] This would give hospitals a reason to

---

128. *Id.*

129. *See generally* CENTER ON BUDGET & POLICY PRIORITIES, THE NUMBER OF UNINSURED AMERICANS IS AT AN ALL-TIME HIGH (Aug. 29, 2006), http://www.cbpp.org/cms/?fa=view&id=628.

130. *Non-Profit Hospitals' Tax-Exempt Status Under Fire From IRS, Local Governments*, *supra* note 100.

131. *See infra* Addendum; James Gallagher, *Charity Care Costs Spiraling at Area Hospitals*, TRIANGLE BUS. J. 1, 26, Jan. 30, 2009, *available at* http://triangle.bizjournals.com/triangle/stories/2009/02/02/story1.html.

132. *See infra* Addendum; *see also* Patient Protection and Affordable Care Act, Pub. Law No. 111-148 (2009).

133. *See generally* Posting of Ken Terry to BNET.com, *AHA Figures Show Rise in Government Underpayments, Charity Care*, http://industry.bnet.com/healthcare/10001453/aha-figures-show-rise-in-government-underpayments-charity-care/ (Dec. 1, 2009).

increase their charity care, especially if elderly and indigent patients require complex and costly procedures.[134] Moreover, larger reimbursements would free up financial resources for programs on prevention and early detection, which would decrease the number of people requiring care in the long-run.[135]

Professor John Colombo also offers an alternative solution. His "increasing access" standard "enhances health care access to underserved populations by combining charity care with investments in areas not covered by for-profit hospitals such as emergency psychiatric units or the funding and establishment of AIDS Clinics."[136] Colombo believes that this standard for providing care to indigent citizens "is preferable over a charity care standard because non-profit hospitals are held more accountable and not held to the strict charity care standard which would require them to increasingly give free care to uninsured patients and potentially wipe out the hospitals' financial resources."[137] Colombo's solution has merit because it takes into account the need for charity care, but it does so without implementing percentage-based requirements. In addition, it also acknowledges some of the factors, other than charity care, typically considered in a "community benefit" analysis.[138]

V. CONCLUSION

Charity care in America's non-profit hospitals serves a vital function for the indigent and uninsured throughout the United States. The majority of non-profit hospitals provide millions of dollars every year on expensive

---

134. *Id.*

135. *Id.*

136. *Non-Profit Hospitals' Tax-Exempt Status Under Fire From IRS, Local Governments*, *supra* note 100.

137. *Id.*

138. ILLINOIS HOSPITAL ASSOCIATION POSITION PAPER, *supra* note 2. "The term 'community benefit' – as used in both state and federal law – describes a combination of hospital services and activities that contribute to the well-being of the community." *Id.* at 1. For instance, the Illinois Community Benefits Act includes pursuits such as, subsidized health services, education, government sponsored health care, donations, volunteers, research, charity care, bad debt, and language assistance services. *Id.*; *see also Non-Profit Hospitals' Tax-Exempt Status Under Fire From IRS, Local Governments*, *supra* note 100.

procedures, prevention programs, education, free clinics, research, and charity care. With few exceptions, these hospitals satisfy the "community benefit" standards necessary to warrant their much-needed tax exemptions. A percentage-based charity requirement would threaten the financial stability of these institutions and paralyze countless inner-city and rural non-profit hospitals at a time of increased health care costs and nationwide economic recession. Accordingly, state legislatures and Congress must abandon their percentage-based charity care requirement proposals and explore other avenues for a solution to this health care crisis.

ADDENDUM

Comprehensive health care reform became a reality on March 23, 2010, when President Barack Obama signed into law the Patient Protection and Affordable Care Act.[139] The prospects of passing comprehensive legislation had been bleak until this point.[140] On November 7, 2009, the U.S. House of Representatives passed the Affordable Health Care for America Act,[141] and on December 23, 2009, the U.S. Senate passed its own version, the Patient Protection and Affordable Care Act.[142] However, as both bills went to conference, the Democrats lost their sixty-vote filibuster-proof majority in the Senate with the election of Senator Scott Brown in Massachusetts.[143] Most Americans believed this meant that neither the Senate nor the House bills would ultimately be signed into law.[144] There was also a large public outcry against both bills, as a majority of Americans, fifty-four percent in a

139. Patient Protection and Affordable Care Act, Pub. Law No. 111-148 (2009).

140. *See* Carrie Budoff Brown & Patrick O'Connor, *The Fallout: Democrats Rethinking Health Care Bill*, POLITICO.COM, Jan. 19, 2010, http://www.politico.com /news/stories/0110/31693.html.

141. Affordable Health Care for America Act, H.R. 3963, 111th Cong. (1st Sess. 2009).

142. Patient Protection and Affordable Care Act, H.R. 3590 (2009).

143. *See* Paul Kane & Karl Vick, *Republican Wins Kennedy's Seat; Upset Shakes Democrats Result Could Derail Party Agenda*, WASH. POST, Jan. 20, 2010, at A1.

144. *See* Sheryl Gay Stolberg, Jeff Zeleny & Carl Hulse, *Health Vote Caps Journey Back From the Brink*, N.Y. TIMES, Mar. 20, 2010, at A1.

recent Rasmussen poll, were opposed to the legislation.[145] Nonetheless, such negative public sentiment did not faze the President and Democratic leaders in Congress, as the U.S. House of Representatives abandoned its own bill, and instead decided to pass the Senate's version, with amendments, through the budget reconciliation process.[146] The House voted to pass the Senate's bill by a 219 to 212 vote on March 21, 2010, and President Obama signed it into law two days later.[147]

The Patient Protection and Affordable Care Act is focused primarily on health care affordability and providing health insurance coverage to more Americans, with very little information on charity care and non-profit hospitals.[148] However, the policies and mandates set in place through this legislation could have an indirect effect on some of the issues discussed in this Note. That being said, it is important to note several features of the legislation, and what they could mean for non-profit hospitals' continued tax exemption and charity care requirements.

Although U.S. Senators Chuck Grassley and Max Baucus of the Senate Finance Committee continue to strive for percentage-based charity care requirements in federal legislation,[149] the Senate bill omits such requirements.[150] Instead, the Senate bill outlines, "additional requirements for non-profit hospitals that mirror requirements made by the Senate Finance Committee, including one that demands nonprofit hospitals to perform a

---

145. *See generally* RASMUSSEN REPORTS, HEALTH CARE REFORM (2010), http://www.rasmussenreports.com/public_content/politics/current_events/healthcare/september_2009/health_care_reform.

146. David M. Herszenhorn & Robert Pear, *Final Votes in Congress Cap Battle on Health Bill*, N.Y. TIMES, Mar. 26, 2010, at A17.

147. Shailagh Murray & Lori Montgomery, *Divided House Passes Health Bill; MEASURE GOES TO OBAMA No Republicans Join 219 to 212 Majority*, WASH. POST, Mar. 22, 2010, at A1.

148. *See generally* Patient Protection and Affordable Care Act, Pub. Law No. 111-148 (2009).

149. Robert Pear, *supra* note 108.

150. *See generally* Affordable Health Care for America Act, H.R. 3963, 111th Cong. (1st Sess. 2009); Patient Protection and Affordable Care Act, H.R. 3590, 111th Cong. (Dec. 24, 2009).

community needs assessment at least once every three years."[151] Although not a great departure from requirements that already exist, this language would help nonprofit hospitals identify the needs of their communities in a more uniform and transparent fashion.[152] Additional requirements of the Senate bill include "written policies for financial assistance eligibility and emergency medical care regardless of financial assistance eligibility. Hospitals that fail to comply will be slapped with a $50,000 excise tax."[153] Moreover, the Senate bill:

> requires a report on charity care levels conducted by the U.S. Secretary of the Treasury with the Secretary of Health and Human Services. The provision stipulates an annual report on issues, such as charity care levels and unreimbursed costs for services from government programs. The report isn't just aimed at nonprofit hospitals. Both public and for-profit hospitals will have to provide information. The report will be submitted to entities, such as the House of Representatives Committee on Ways and Means and the Senate Committee on Finance and Health, and study trends in charitable care.[154]

Evidently, the Senate did not want to go so far as to create minimum requirements for charity care, but rather chose to address some of these issues by disseminating more information to the indigent and uninsured on how they may obtain financial assistance, as well as providing Congress and federal agencies with additional oversight of the charity care matter. Surely, this is a far cry from Grassley and Baucus' goal of percentage-based charity care requirements.

Interestingly, some financial experts and investors believe that the recently passed legislation will mean much greater profitability for non-profit hospitals.[155] In fact, less than a week after President Obama signed the Patient Protection and Affordable Care Act into law, "two major deals

---

151. Michele Donohue, *Healthcare Reform and Nonprofits*, NONPROFIT TIMES, Jan. 15, 2010, at 1, *available at* http://www.nptimes.com/10Jan/npt-100115-1.html.

152. *Id.*

153. *Id.*

154. *Id.*

155. *See* Lindsey Dunn, *For-Profit Firms Eyeing Non-Profit Hospitals: A Growing Trend?*, HOSPITAL REVIEW, Mar. 26, 2010, at 1, *available at* http://www.hospitalreviewmagazine.com/news-and-analysis/business-and-financial/for-profit-firms-eyeing-non-profit-hospitals-a-growing-trend.html?format=pdf.

involving the possible acquisition of large non-profit hospital systems by for-profit firms have been announced: Vanguard Health Systems' acquisition of eight-hospital Detroit Medical Center and private equity firm Cerberus Capital's acquisition of Boston's Caritas Christi Health Care."[156] In the coming years, specifically in 2014, when Americans will be required to have at least some form of health insurance, it is reasonable to predict that non-profit hospitals will have greater revenues because their patients can reimburse the hospitals through their insurers.[157] A recent *Wall Street Journal* article explains:

> [h]ospitals that serve the poor and previously uninsured are expected to benefit from Obama's plan, which is expected to extend insurance to 32 million previously uninsured Americans. That means such hospitals are likely to have more patients who can actually pay their bills. It is hard not to see how that new cash-flow stream wouldn't have private equity licking its chops.[158]

If more people have insurance, it is likely that the need for charity care will decrease substantially. However, increased profitability at these institutions, whether they remain non-profit or change to for-profit entities, is far from a foregone conclusion at this point. The article continues:

> Obama's plan isn't a total boon for hospitals like Caritas. The plan calls for cutting annual increases to Medicaid reimbursement rates, which would affect the hospitals and doctors who treat the poorest patients. The new legislation also won't allow illegal immigrants to buy coverage on the insurance exchanges. Charity hospitals still are required by law to provide emergency-room care to illegal immigrants, regardless of whether they can afford to pay.[159]

Clearly, it is too early to tell how the Patient Protection and Affordable Care Act will affect charity care at non-profit hospitals and proposed percentage-based state and federal legislation regulating the issue of charity care. Although the bill does not squarely address most of these contentious issues, the non-profit hospital industry, investors, Congress, and the economy, in general, will be evaluating the indirect effects of the legislation under a microscope for years to come. Congress and state legislatures would

---

156. *Id.*

157. *Id.*

158. Posting of Michael Corkery to WSJ Blogs, *Obamacare: Are Charity Hospitals Now a Hot Commodity?*, http://blogs.wsj.com/deals/2010/03/25/obamacare-are-charity-hospitals-now-a-hot-commodity/ (Mar. 25, 2010, 11:04 EST).

159. *Id.*

be ill-advised to shape legislation on the charity care issue before witnessing these indirect effects from the implementation of the Patient Protection and Affordable Care Act.