

## **PRIVATE USE OVERHAUL: IRS EXPANDS REV. PROC. 97-13 SAFE HARBORS; PROVIDES GUIDANCE FOR PARTICIPATION IN ACOS**

On Friday, October 24, 2014, the IRS released an advance version of [Notice 2014-67](#), (1) adding a new 5-year safe harbor to Revenue Procedure 97-13 ("Rev. Proc. 97-13") and providing for the inclusion of quality-based incentive payments in management and service contracts for facilities financed with tax-exempt bond proceeds; and (2) offering interim guidance for determining whether a state or local government entity or 501(c)(3) organization with outstanding tax-exempt bonds will be considered to have private business use of its bond-financed facilities as a result of its participation in the Medicare Shared Savings Program ("MSSP") through an Accountable Care Organization ("ACO").

### **EXPANSION OF REV. PROC. 97-13 SAFE HARBORS**

The new Rev. Proc. 97-13 safe harbor dramatically increases flexibility for health care providers when entering into management and service contracts. The new safe harbor allows for contracts of up to 5 years, with no need for the agreement to be terminable prior to the end of 5 years. Compensation may be based on "a stated amount; periodic fixed fee; a capitation fee; a per-unit fee; or a combination of the preceding. The compensation for services also may include a percentage of gross revenues, adjusted gross revenues or expenses of the facility (but not revenues and expenses)."

In addition, the notice expands Section 5.02(3) of Rev. Proc. 97-13 to permit annual incentive payments, either as a stated dollar amount or a tiered system of stated dollar amounts, based on the level of performance achieved, so long as they are based on "the quality of the services provided...rather than increases in revenues or decreases in expenses of the facility." For purposes of the new safe harbor, a tiered productivity award will be treated as a stated amount or a periodic fixed fee as appropriate (i.e., such payments will not cause an agreement to fall outside the safe harbors).

The changes to Rev. Proc. 97-13 are effective for contracts entered into or amended on or after January 22, 2015, but may be applied to contracts entered into before such date.

### **PRIVATE USE GUIDANCE FOR ACOS PARTICIPATING IN THE MEDICARE SHARED SAVINGS PROGRAM**

The IRS has also provided interim guidance for qualified users, including 501(c)(3) hospitals, participating in the MSSP through ACOs with for-profit participants, such as physicians, post-acute care providers and insurers. Pursuant to such guidance, participation in the MSSP through an ACO will not, in and of itself, result in private business use if:

1. The terms of the qualified user's participation in the MSSP through the ACO are set forth in advance in a written agreement negotiated at arm's length.
2. CMS has accepted the ACO into, and has not terminated the ACO from, the MSSP.
3. The qualified user's share of economic benefit derived from the ACO is proportional to the benefits or contributions the qualified user provides to the ACO.
4. The qualified user's share of the ACO's losses, including its share of the MSSP losses, does not exceed the share of ACO economic benefits to which the qualified user is entitled.
5. All contracts and transactions entered into by the qualified user 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.
6. The qualified user does not contribute or otherwise transfer the property financed with tax-exempt bond proceeds to the ACO unless the ACO is also a qualified user.

The first five prongs of this guidance mirror those of [Notice 2011-20](#), where such provisions were provided as evidence that a tax-exempt entity's participation in the MSSP through an ACO will not result in inurement or impermissible private benefit to private party ACO

participants.

The proposed guidance does not include analogous arrangements with private payors.

The IRS has requested public comment on this proposal, which comments must be submitted by January 22, 2015.

## **PRACTICAL TAKEAWAYS**

- Borrowers with outstanding tax-exempt bonds now have a great deal more flexibility when negotiating the term and compensation for management and service contracts affecting bond-financed facilities.
- Incentive payments are now specifically approved under Rev. Proc. 97-13, but only for quality-based incentives, and not for incentives based on revenues or expenses.
- 501(c)(3) hospitals who participate in ACOs with for-profit participants need to have such arrangements reviewed by bond counsel, ideally early in the drafting process. Improper structuring of ACO documentation could jeopardize the tax-exempt status of a health system's bonds.
- Health systems who have formed ACOs with for-profit participants should consider contacting Hall Render and/or the IRS with comments about the proposed private use guidance for such arrangements.

For any questions about these proposed changes, Rev. Proc. 97-13 or private business use of facilities financed with tax-exempt bonds, please contact:

- Your regular Hall Render attorney.

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