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Additional Guidance for Public Hospitals on the Paycheck Protection Program

The Coronavirus Aid, Relief and Economic Security (CARES) Act created the Paycheck Protection Program (PPP) to provide organizations with fewer than 500 employees with loans that could be used to maintain their workforce through the economic downturn caused by COVID-19. Participating hospitals may use these loans to pay salaries and benefits, among other uses. Under certain circumstances, these loans (or a portion of them) may be forgiven.

Initial guidance from the Small Business Administration (SBA) was ambiguous about the eligibility of public hospitals. However, subsequent guidance has clarified that they may be able to participate under certain circumstances. The following information, which was prepared for the AHA by JonesDay, may help public hospitals in applying this guidance.

Public Hospital Eligibility for the PPP

Section 501(c)(3) nonprofit organizations are eligible to borrow funds through the PPP provided that they (together with any affiliates determined under SBA's affiliation rules) have 500 or fewer employees and are able to make the certifications required on the loan application. Public hospitals that do not have Internal Revenue Service (IRS) determination letters recognizing them as described in section 501(c)(3) and exempt from tax under section 501(a) have had questions about whether they qualify as section 501(c)(3) organizations for purposes of this program. On May 3, the Treasury Department issued Question and Answer 42 (Q/A 42) providing further guidance on when a public hospital will be considered a section 501(c)(3) nonprofit organization for purposes of the PPP. Q/A 42 says in part, "The Administrator will treat a nonprofit hospital exempt from taxation under section 115 of the Internal Revenue Code as meeting the definition of 'nonprofit organization' under section 1102 of the CARES Act if the hospital reasonably determines, in a written record maintained by the hospital, that it is an organization described in section 501(c)(3) of the Internal Revenue Code and is therefore within a category of organization that is exempt from taxation under section 501(a)."

Section 115 of the Internal Revenue Code

Section 115 provides exemption from tax for the income of an organization that meets these requirements:

1. Be separately organized from the state or local government

Different public hospitals will be organized in different ways. Those that are established as nonprofit corporations under the state nonprofit corporation law or are chartered by statute or local ordinance as corporate bodies should be considered to be organized separately from the state or local government. A hospital that is operated by a government agency or department rather than a legal entity that is separate from the government would not fall under section 115.

2. Generates its income from performance of an essential governmental function

The IRS has repeatedly ruled that public hospitals are performing an essential governmental function.

3. The income accrues to a state or local government.

The IRS applies this requirement by looking to whether the income and assets of the organization are transferred to a state or local government upon dissolution. For purposes of issuing private letter rulings, the IRS looks for governing documents specific to the organization that contain a dissolution clause. There may be other ways of satisfying the income accrual requirement, such as language in applicable statutes or laws.

Organizations Described in Section 501(c)(3)

An organization is described in section 501(c)(3) if it meets four criteria:

1. It is organized exclusively for charitable or other exempt purposes.

The IRS looks at the governing documents to determine whether an organization meets this requirement. Promotion of health for the benefit of the community is a charitable purpose for section 501(c)(3). Satisfying this test also requires that there is a binding commitment in governing documents or law that upon dissolution, the organization's assets go to another section 501(c)(3) organization or a governmental entity.

2. It is operated exclusively for charitable or other exempt purposes.

The IRS looks to how the organization is actually operated. A hospital that accepts Medicare and Medicaid patients, has an open emergency room and an open medical staff, and treats all patients regardless of ability to pay would generally be viewed as operating for charitable purposes within the meaning of section 501(c)(3).

3. The organization does not intervene in campaigns for public office either for or against any candidate.

No amount of campaign intervention is permissible.

4. The organization limits any lobbying it may do on legislation or referenda to an insubstantial part of its overall activities.

Advocacy on legislation either directly with the legislature or its staff or through mass media or advocacy on a ballot referendum is permissible provided that it remains an insubstantial part of the organization's overall activities. Whether an activity is substantial depends on all facts and circumstances, including expenditures, time spent or other resources deployed on the activity.

Section 501(r) Disregarded

Generally, a hospital must satisfy the requirements of section 501(r) in order to be exempt as an organization described in section 501(c)(3). These requirements include, among others, performance of a community health needs assessment once every three years, restrictions on billing and collection practices, and limitations on charges for patients eligible for financial assistance. A hospital that has an IRS determination letter recognizing it as a section 501(c)(3) organization is required to comply with section 501(r). However, according to Treasury's Q/A 42, a public hospital that does not have an IRS determination letter does **not** have to satisfy the requirements of section 501(r) to qualify as a nonprofit organization for purposes of the PPP.

Further Questions

If you have questions, please contact AHA at 800-424-4301.