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of Bond Lawyers

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January 22, 2015

Internal Revenue Service
CC:PA:LPD:PR (Notice 2014-67)
PO Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Comments to the Interim Guidance Provided in Notice 2014-67 Regarding Participation in Accountable Care Organizations and the Amplification of the Private Business Use Safe Harbors in Revenue Procedure 97-13

Ladies and Gentlemen:

The National Association of Bond Lawyers (NABL) respectfully submits the enclosed comments in response to Notice 2014-67 regarding the interim guidance provided for the participation by governmental persons or 501(c)(3) organizations in accountable care organizations under the Medicare Shared Savings Program of the Patient Protection and Affordable Care Act and regarding the amplification of the private business use safe harbors in Revenue Procedure 97-13. The enclosed comments were prepared by an ad hoc task force comprising those individuals listed in Exhibit A and approved by the NABL Board of Directors.

NABL exists to promote the integrity of the municipal market by advancing the understanding of and compliance with the law affecting public finance. We respectfully provide this submission in furtherance of that mission.

If NABL can provide further assistance, please do not hesitate to contact Bill Daly in our Washington, D.C. office at (202) 503-3303.

Sincerely,

Antonio D. Martini

COMMENTS BY THE NATIONAL ASSOCIATION OF BOND LAWYERS TO THE INTERIM GUIDANCE IN NOTICE 2014-67 REGARDING PARTICIPATION IN ACCOUNTABLE CARE ORGANIZATIONS AND THE AMPLIFICATION OF THE PRIVATE BUSINESS USE SAFE HARBORS IN REVENUE PROCEDURE 97-13

The following comments are submitted on behalf of the National Association of Bond Lawyers (NABL) in response to the interim guidance contained in Notice 2014-67, 2014-46 I.R.B. 822 ("Notice 2014-67"), regarding the participation by governmental persons or organizations described in section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the "Code"), in accountable care organizations ("ACOs"), and the amplification of the private business use safe harbors in Revenue Procedure 97-13, 1997-1 C.B. 632 ("Revenue Procedure 97-13").

I. ACCOUNTABLE CARE ORGANIZATIONS

Background

The Patient Protection and Affordable Care Act (Pub. L. 111-148, 124 Stat. 119) (the "Affordable Care Act") directs the Centers for Medicare and Medicaid Services ("CMS") to establish and operate the Medicare Shared Savings Program (the "MSSP"). Pursuant to section 1899 of the Social Security Act (42 U.S.C. § 1395 et seq.), CMS approves ACOs that participate in the MSSP to share in savings that are achieved when an ACO meets certain quality-of-care and savings benchmarks. An ACO may include both taxable and tax-exempt participants. According to CMS, more than 405 ACOs are currently participating in the MSSP, and ACOs are serving over 7.2 million beneficiaries.[1]

In Notice 2011-20, 2011-16 I.R.B. 652 ("Notice 2011-20"), and in the subsequent Fact Sheet 2011-11 related thereto ("FS-2011-11"), the Treasury Department ("Treasury") provided guidance regarding when a tax-exempt organization can avoid prohibited inurement or impermissible private benefits that may result from the participation in the MSSP through an ACO.

In a request for guidance addressed to Treasury dated March 29, 2013 (the "2013 Request"), NABL noted that participation in an ACO by tax-exempt organizations and governmental entities raises questions concerning the tax-exempt status of debt issued by or for the benefit of such organizations. The 2013 Request sought guidance regarding these questions. We commend the Internal Revenue Service (the "IRS") and Treasury for releasing Notice 2014-67 and offering guidance that begins to respond to these questions, and we submit this commentary in order to solicit additional clarifying guidance, with a view to ensuring that there is a clear regulatory framework under which the private business use requirements of section 141 of the Code can be squared with the mandates of the Affordable Care Act.

[1] Centers for Medicare and Medicaid Services, *ACOs Moving Ahead*, THE CMS BLOG, December 22, 2014, http://blog.cms.gov/2014/12/22/acos-moving-ahead/.

General Comments

As a threshold matter, we recommend that the IRS and Treasury Department confirm that (1) the six-prong standard described in section 3.01 of Notice 2014-67 (the "ACO Safe Harbor") is in fact a safe harbor for purposes of determining whether participation in an ACO results in private business use; and (2) the ACO Safe Harbor does not displace the general facts and circumstances approach set forth in the Code and Treasury Regulations or other existing guidance, such as Revenue Procedure 97-13, for purposes of determining whether an arrangement gives rise to private business use.

With respect to the former request, we note that Notice 2014-67 does not expressly use the term "safe harbor" in describing the ACO Safe Harbor, although the ACO Safe Harbor borrows heavily from the safe harbor set forth in Notice 2011-20 and references Revenue Procedure 97-13, which provides safe harbors for private business use purposes. Clarification that the ACO Safe Harbor is a safe harbor for private business use purposes would be helpful.

Regarding the latter request, we recommend clarification that the failure to satisfy the ACO Safe Harbor does not, by itself, mean that participation in an ACO results in private business use, but rather that the arrangement should be subject to the general facts and circumstances analysis described in section 141 of the Code, section 1.141-3 of the Treasury Regulations and other published guidance. Under the ACO Safe Harbor, participation by a qualified user[2] in an ACO with for-profit participants would not result in private business use if all six requirements of the ACO Safe Harbor are met. The first five requirements mirror the standards established in Notice 2011-20. Notice 2011-20, however, does not require all standards to be met, and FS-2011-11 in fact clarifies that all five standards need not be met to conclude that no private benefit arises. We request this same clarification for Notice 2014-67.[3] This will ensure that the ACO Safe Harbor does not create a negative implication that non-conforming arrangements result in private business use without regard to the longstanding private business use rules.

Given the need for broad guidance in analyzing the private business use implications of arrangements contemplated by the Affordable Care Act, we are also concerned that the scope of Notice 2014-67 is too narrow. Notice 2014-67 affects a minority of value-based healthcare arrangements. We understand that there are alternate delivery arrangements in place throughout the country for which there is no guidance at all. As NABL describes in the 2013 Request, it is important to recognize that these other arrangements reflect ongoing changes that are occurring throughout the healthcare industry and are likely to increase in variety and scope over time.

[2] The term "qualified user" is as defined in Revenue Procedure 97-13, and includes a state or local governmental unit or any instrumentality thereof and a section 501(c)(3) organization if the financed property is not used in an unrelated trade or business.

[3] Private benefit and private inurement are measured on a facts and circumstances basis, and the consequences thereof may be the loss of tax-exempt status. The test is applied to the totality of an organization's operations, and the consequences are that the organization is tax-exempt or not. Private business use, in contrast, usually applies only to a portion of an entity's operations (i.e., not everything is bond-financed), and must be quantified so that it may be reported to the IRS annually and so that bond counsel may give an unqualified opinion that no more than a *de minimis* amount of private business use exists or is expected to exist for the life of the bonds.

Guidance may be helpful to confirm that these arrangements, similar to ACO arrangements accepted into the MSSP, can avoid private business use issues.

Clarification is also needed regarding the use in Notice 2014-67 of the word "participation." In these comments, we refer to participation because that is the term used in Notice 2014-67, but we believe there are significant interpretive issues with the term that should be addressed. According to the regulations relating to the MSSP at 42 CFR 425.20 (the "MSSP Regulations"), an "ACO participant" means an individual or group of providers or suppliers that, together with other participants, compose the ACO. A participant does not need to be an owner of the ACO or partake in the governance of the ACO. A physician group is an "ACO participant" when it provides services even if those services are rendered pursuant to a qualified management contract under Revenue Procedure 97-13 to a tax-exempt hospital that has established and "owns" an ACO. An ACO is fundamentally a physician-based organization because beneficiaries are assigned to ACOs based on their primary care providers. Unless a 501(c)(3) organization or governmental entity employs all of its physicians, all ACOs, even those exclusively owned by, and themselves treated as, governmental entities or 501(c)(3) organizations, will have nongovernmental "participants" for purposes of the MSSP Regulations. Similarly, an ACO may be established and owned solely by a nongovernmental taxable entity. Such an ACO may have contractual arrangements with one or more tax-exempt hospitals, making the hospitals "ACO participants." The hospitals would have no ownership interest in the ACO, and would not be required to have a role in the governance of the ACO.

We are concerned that the language of Notice 2014-67 referring to "participation" could be interpreted to suggest that private business use may arise from contractual agreements between a tax-exempt ACO and a nongovernmental taxable entity (or between a nongovernmental taxable ACO and a tax-exempt entity) even if such agreements are structured to be in full compliance with Revenue Procedure 97-13 (in the case of a tax-exempt ACO) or have been found not to be an unrelated trade or business (in the case of a nongovernmental taxable ACO).[4] We do not believe that this is the intent of Notice 2014-67 and request confirmation of this point. In addition, we request additional guidance to clarify the use of the term "participation" for purposes of the ACO Safe Harbor.

Specific ACO Safe Harbor Requirements

Written Agreement. The first ACO Safe Harbor requirement states that the terms of the qualified user's participation in the MSSP through an ACO must be set forth in advance in a written agreement negotiated at arm's length. Such terms must include the share of the user's MSSP payments or losses and expenses. NABL understands that, while there usually is an agreement in place between CMS and the ACO when the ACO is approved to participate in the MSSP, certain of the terms of such an agreement may not be developed until a later time. This is consistent with the final regulations released by CMS, which provide for flexibility in how the ACO may operate. For example, while the regulations require the ACO in its application for admission to describe the general plans for how shared savings payments are to be used, the MSSP Regulations do not prescribe how savings are to be allocated and distributed. Frequently, the particular mechanics of distribution are decided by the parties only when and if savings are

[4] 501(c)(3) organizations that provide services to other entities, whether taxable entities or other 501(c)(3) organizations, may, depending on the particular facts and circumstances, be viewed as engaging in an unrelated trade or business within the meaning of section 513(a) of the Code.

achieved. Sometimes the agreement negotiated at the outset will establish a range of payments that may be made to (in the case of moneys received from CMS) or by (in the case of moneys owed to CMS) the members of the ACO. As drafted, the requirement raises questions concerning the level of specificity that is needed to satisfy the ACO Safe Harbor. In FS-2011-11, relating to Notice 2011-20, the IRS specifically stated that "[i]t is sufficient for the written agreement to set forth the *methodology* for determining an ACO's allocation of Shared Savings payment to the tax-exempt participant and the other Medicare-enrolled providers and suppliers participating in the Shared Savings Program through the ACO." We request that this clarification be included in subsequent guidance relating to Notice 2014-67.

Proportionality/Equivalence. The third ACO Safe Harbor requirement provides that the qualified user's share of the economic benefits derived from the ACO (including its share of shared savings payments) must be proportional to the benefits (e.g., services) or contributions the qualified user provides to the ACO. If the qualified user receives an ownership interest in the ACO, the ownership interest received must be proportional and equal in value to its capital contributions to the ACO, and all ACO returns of capital, allocations and distributions must be made in proportion to ownership interests. The fourth requirement states that the qualified user's share of the ACO's losses (including its share of shared savings losses) may not exceed the share of ACO economic benefits to which the qualified user is entitled. We request that these requirements be clarified to confirm that the determination of the share of economic benefits to be received by a qualified user may be separate from the determination of the share of losses allocated to a qualified user, and may also be separate from the determination of the proportion of ownership interest received and the return of capital, allocations and distributions.[5] For example, participants in an ACO should be permitted to determine the allocation of benefits based on the amount of savings attributable to a particular participant or services (benefits) provided by that participant, regardless of any ownership the participant may or may not have in the ACO. Allocations of member distributions and member losses could be based on ownership interests and not shared savings.

The third and fourth ACO Safe Harbor requirements are not flexible enough to address ACOs that are structured as "upside-only" ACOs in which no losses are to be shared. In addition, it may often be challenging to measure economic benefits derived from ACO participation and benefits or contributions provided to an ACO. Many tax-exempt hospitals that are ACO participants will have economic benefits from ACO participation that are not readily quantifiable or established by the ACO documentation, such as increases in market share due to greater patient satisfaction. These measurement challenges not only make it difficult to conclude that the third ACO Safe Harbor requirement is met but may make compliance with the fourth ACO Safe Harbor requirement especially challenging. For example, a tax-exempt hospital that is an ACO participant may be entitled to 20 percent of shared savings payments, but may be responsible for 50 percent of shared savings program losses because the hospital expects that the increased market share from ACO participation will increase total revenues, regardless of any shared savings payments or losses. In this scenario, the hospital may be willing to take on a disproportionate share of losses because of the additional revenues generated from the increase

[5] It should be noted that, although the Notice contemplates the provision of benefits and contributions by the participant, the proportionality of any ownership interest is limited to the amount of capital contributions of the participant. This requirement seems to ignore arrangements in which a participant would derive compensation or economic benefits beyond what may be contributed by such participant as capital (e.g., the provision of services).

in market share. Conversely, a private physician group participating in the same ACO may not expect any increase in market share as a result of the ACO, and may therefore desire a greater percentage of any shared savings payments.

We believe that separating the evaluation of shared savings losses from shared savings payments and allowing for a broader evaluation of economic benefits and costs of ACO participation more closely reflects the economic realities underlying ACO arrangements.

Fair Market Value. The fifth ACO Safe Harbor requirement provides that 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, be at fair market value. This requirement is difficult to implement, given that there is not an established market for shared savings arrangements. Even assuming that fair market value could be determined, there are uncertainties as to the level of documentation that would be required in order for bond counsel to provide an unqualified opinion and whether a separate fair market value opinion should be obtained. Accordingly, we suggest that this requirement be modified to provide only that a qualified user must negotiate at arm's-length the terms of any such contract or transaction that affect its interests.

Transfer Limitations. The sixth ACO Safe Harbor requirement prohibits the qualified user from contributing or otherwise transferring the bond-financed property to the ACO unless the ACO is an entity that is a governmental person, or in the case of qualified 501(c)(3) bonds, either a governmental person or a 501(c)(3) organization. We would appreciate confirmation that this requirement would not prohibit the qualified user from permitting an ACO to use space within a bond-financed facility pursuant to a qualified management contract or to lease space to the ACO within the limits of the qualified user's private business use and private payment limits.

II. REVENUE PROCEDURE 97-13

NABL greatly appreciates the guidance recently provided by the IRS in Notice 2014-67 applicable to the private business use safe harbors for management and service contracts ("management contracts"). NABL believes the amplification of Revenue Procedure 97-13 to include an additional five-year safe harbor (the "Management Contract Safe Harbor"), as well as the revision to the permitted productivity rewards, will assist healthcare and other borrowers with ensuring compliance with the federal tax law limitations imposed on management contracts impacting tax-exempt bond financed facilities. NABL suggests the following amendments, which would clarify the application of the Management Contract Safe Harbor.

Define the Term "Stated Amount"

The Management Contract Safe Harbor provides that all of the compensation for services may be based on, among other available options, a "stated amount." Unlike the other available compensation methods described in the Management Contract Safe Harbor, the term "stated amount" is not defined in Revenue Procedure 97-13 or Notice 2014-67. NABL recommends that Revenue Procedure 97-13 or Notice 2014-67 be amended to include a definition of the term "stated amount".

Extend the Management Contract Safe Harbor to Apply to Incentive Payments Based on Maximizing Revenue or Minimizing Expense (But Not Both)

The Management Contract Safe Harbor applies to contracts that include compensation based on a percentage of gross revenues, adjusted gross revenues, or expenses of the facility (but not both revenues and expenses). One variation of this type of compensation that arises, particularly in the healthcare context, is compensation of a fixed amount if gross or adjusted gross revenues exceed a certain threshold or expenses are below a certain threshold. Such a provision may be an "all or nothing" incentive based on a single threshold (e.g., a payment of $X if gross revenues exceed $Y) or may be layered (e.g., a payment of $X if gross revenues exceed $Y and a payment of $X plus $100 if gross revenues exceed $Z). If compensation based on a percentage of revenue or expenses is covered by the Management Contract Safe Harbor, incentive payments based on exceeding revenue threshold(s) or falling below expense threshold(s) (but not both) should also be covered. For these purposes, NABL suggests the following amendment to the Management Contract Safe Harbor (NABL's recommended language is underlined):

> Arrangements in certain 5-year contracts. All of the compensation for services is 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 both revenues and expenses) <u>or incentive payments based on exceeding one or more specified levels of gross revenues or adjusted gross revenues or falling below one or more specified levels of expenses of the facility (but not incentive payments based on both revenues and expenses)</u>. The term of the contract, including all renewal options, does not exceed five years. Such contract need not be terminable by the qualified user prior to the end of the term. For purposes of this section 5.03(7), a tiered productivity award as described in section 5.02(3) will be treated as a stated amount or a periodic fixed fee, as appropriate.

Exhibit A

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