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Firm Suggests Ways for Public Hospitals to Relinquish Exemption.

T.J. Sullivan of Drinker Biddle & Reath LLP, in comments on proposed regulations (REG-106499-12) that provide guidance to charitable hospital organizations on the community health needs assessment requirements and related excise tax and reporting obligations, has suggested ways that a governmental entity could voluntarily terminate its section 501(c)(3) status.

October 17, 2013

Internal Revenue Service

Office of Chief Counsel

CC:PA:LPD:PR (REG-106499-12)

Room 5203

PO Box 7604

Ben Franklin Station

Washington, DC 20044

RE: Public Hospital Relinquishment of Exemption Under Section 501(c)(3)

Dear Sir or Madam:

I am writing on behalf of East Alabama Healthcare Authority (EAHA) and similarly situated public hospitals, all of the income of each of which is excluded from federal income tax under Section 115 of the Internal Revenue Code of 1986, as amended (the "Code") and which have, voluntarily at some point in the past, sought and received recognition of exemption as a hospital described in Section 501(c)(3) of the Code. EAHA appreciates this opportunity to comment on the proposed regulations implementing new Code Section 501(r). EAHA believes some of the requirements imposed by Code Section 501(r) on all Section 501(c)(3) hospitals may be unnecessarily burdensome if applied to public hospitals and requests that the Internal Revenue Service ("IRS") adopt an administrative mechanism to allow EAHA and similarly situated public hospitals to voluntarily relinquish their Section 501(c)(3) recognition if they so choose.

Although already effectively exempt from federal and state income taxation as a governmental entity, or instrumentality thereof, under the intergovernmental immunity doctrine, many local governmental hospital organizations like EAHA previously obtained determinations from the IRS that they were tax-exempt organizations described in Section 501(c)(3) of the Code. A common reason for voluntarily seeking Section 501(c)(3) recognition (in addition to the entity's exclusion from gross income through intergovernmental immunity as a governmental entity) was to allow the

organization's employees to participate in Section 403(b) qualified retirement plans. Many such organizations, including EAHA, also have been determined to be exempt from the Form 990 filing obligation which, prior to enactment of Section 501(r), was the only real disadvantage to Section 501(c)(3) status for such organizations. Enactment of Section 501(r), however, has placed a substantial burden on these governmental hospital organizations that, like EAHA, have obtained Section 501(c)(3) determinations. Since they have a solid alternate exemption to rely on, such governmental hospital organizations likely will reconsider whether the additional Section 501(c)(3) recognition is necessary or even advisable. Unfortunately, it appears that there presently is no effective process for a public hospital to voluntarily relinquish Section 501(c)(3) status after it has been recognized.

In addition to requesting that such a process be adopted in the final Section 501(r) regulations, if not beforehand, the remainder of this comment letter is intended to offer possible suggestions for a process under which a governmental entity, or an affiliate or instrumentality thereof, could voluntarily terminate its Section 501(c)(3) recognition as seemingly contemplated by Rev. Proc. 2013-4, Section 7.04(14).

In Rev. Proc. 2012-4, the IRS added the following as Section 7.04(14):

In exempt organization matters, the Exempt Organizations Determinations office issues determination letters involving: Government entity voluntary termination of § 501(c)(3) recognition (must include documentation of tax-exempt status other than under § 501(a)).

This exact same language appeared again in Rev. Proc. 2013-4, Section 7.04(14). However, the IRS apparently has never fully implemented a procedure to permit governmental entities with Section 501(c)(3) recognition to voluntarily terminate their Section 501(c)(3) recognition. Without a specific procedure in place, it appears that a governmental hospital organization with a Section 501(c)(3) determination may be treated like all other Section 501(c)(3) recognized entities in that it may not voluntarily relinquish its Section 501(c)(3) status absent some organizational or operational change in character sufficient to remove it from the description of Section 501(c)(3). See, e.g., Gen. Couns. Mem. 37165 (June 14, 1977).

We would like to propose three alternative procedures under which the IRS could allow a governmental entity to pursue the course of action apparently contemplated in Section 7.04(14) of Rev. Proc. 2013-4. Initially, we would suggest a clarification that Section 7.04(14) applies not only to governmental entities but also to affiliates and instrumentalities of governmental entities. Certain affiliates and instrumentalities of governmental entities are exempt organizations through both the intergovernmental immunity doctrine and Section 501(c)(3) recognition by virtue of their relationship with a governmental entity. Therefore, it makes sense to permit such public hospital organizations to voluntarily terminate their Section 501(c)(3) recognition as well.

The first alternative proposed procedure is for the IRS to amend Part II of Form 8940, Request for Miscellaneous Determination Under Section 507, 509(a), 4940, 4942, 4945, and 6033 of the Internal Revenue Code. This amendment would provide the option for such organizations to request a determination letter in accordance with Rev. Proc. 2013-4, Section 7.04(14) by checking the applicable box on the revised Form 8940. This is the most efficient procedure in our opinion for both the taxpayer and the IRS and the most likely to produce a timely result.

A second alternative proposed procedure is for the IRS to permit such organizations to submit a determination letter request pursuant to the current procedures provided in Rev. Proc. 2013-4, but as amended as described below. This procedure would allow the Exempt Organizations Determinations office to issue determination letters to taxpayers submitting properly formatted and

documented requests with the applicable user fee provided in the Rev. Proc. In connection with this proposal, we would propose an amendment to the current language of the Rev. Proc. requiring the governmental entity to include documentation of tax-exempt status other than under Section 501(a). Instead, we propose requiring the requesting taxpayer to certify (under penalties of perjury) that all of its income is excluded under Section 115 within its determination letter request.

Since governmental entities are effectively exempt from federal income taxation under the intergovernmental immunity doctrine, many do not have written documentation from the IRS to establish their tax-exempt status or gross income exclusion other than under Section 501(a). Instead, these entities have made their own determination of their tax-exempt status. If their determination is found by the IRS to be incorrect, the entity is deemed taxable. Requiring a taxpayer requesting a determination letter under Section 7.04(14) of Rev. Proc. 2013-4 to certify its tax-exempt status other than under Section 501(a) provides the IRS with assurance that entity assets will remain devoted to tax-exempt or governmental purposes. If an entity's certification is erroneous, the entity would be treated as any other taxable entity that misclassified itself as tax-exempt. Requiring more determinative evidence of alternate tax-exempt status other than under Section 501(a) seems unnecessary for an entity requesting voluntary termination of its Section 501(c)(3) recognition when such evidence is not required absent previously obtaining a Section 501(c)(3) determination, and likely would be costly and fraught with delay.

The third alternative proposed procedure is to permit such organizations to submit a determination letter request pursuant to the procedure provided in Rev. Proc. 2013-4. This would allow the Exempt Organizations Determinations office to issue determination letters to taxpayers submitting properly formatted and documented requests with the applicable user fee provided in the Rev. Proc. As the current language of the Rev. Proc. requires the governmental entity to include documentation of tax-exempt status other than under Section 501(a), we would propose that the IRS incorporate an expedited process for obtaining a private letter ruling to fulfill this requirement. The private letter ruling could be processed by the Chief Counsel's office, but requested by the taxpayer submitting one overall determination letter request that also contains an expedited private letter ruling request.

This comment letter proposes three alternative suggestions for a governmental entity, or an affiliate or instrumentality thereof, that operates a public hospital to voluntarily terminate its Section 501(c)(3) recognition. The administrative burden of each of these options for the taxpayer and the IRS varies. We prefer, and therefore recommend, the first alternative. However, all three would provide a viable method to allow a governmental entity, or an affiliate or instrumentality thereof, to voluntarily terminate its Section 501(c)(3) recognition.

We appreciate your consideration and would be happy to answer any questions.

Very truly yours,

T.J. Sullivan

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