

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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POSTS-145204-12

Third Party Communication: None
Date of Communication: Not Applicable

UILC: 61.00-00; 6041.00-00

date: January 14, 2013

to:
Director, Indian Tribal Governments

Attn:

from: Michael J. Montemurro
Branch Chief
(Income Tax & Accounting)

subject: Electronic Health Records Incentive Payments, POSTS-145204-12

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUES

- (1) Whether recipients must include in gross income electronic health record incentive payments paid by the Centers for Medicare and Medicaid Services (CMS) pursuant to the American Recovery and Reinvestment Act.
- (2) Whether CMS has a reporting requirement with regard to payments made under the EHR Incentive Program.
- (3) Whether the reporting requirement is altered if the payment is assigned to a third party.

CONCLUSIONS

- (1) The recipients must include the incentive payments in gross income unless they receive the payments as a conduit or an agent of another and are thus unable to keep the payments.

- (2) CMS has a reporting requirement under section 6041 of the Internal Revenue Code with respect to the eligible providers.
- (3) In the event of an assignment by the eligible providers to a third party, CMS would be obligated to report a payment to the eligible provider, even if the payment is assigned to a third party. The eligible provider would then likely bear a reporting obligation with respect to the assignment to a third party. CMS would not have a reporting obligation with respect to the third-party assignee unless CMS exercised managerial oversight with respect to, or had a significant economic interest in, the assignment.

FACTS

The American Recovery and Reinvestment Act of 2009 (ARRA) authorizes the Centers for Medicare and Medicaid Services (CMS) to make incentive payments to eligible professionals and hospitals that are meaningful electronic health record (EHR) users. An EHR allows health care providers to record patient information electronically instead of using paper records. "Meaningful use" entails more than merely maintaining EHRs. To be eligible for incentive payments, CMS requires that providers demonstrate that they are using their EHRs in ways that can positively affect their patients' care. For example, providers must record patient data electronically and share that data either with the patient or with other healthcare professionals. Providers may also employ the EHRs to issue prescriptions electronically or to update immunization records.

Under the Medicare EHR incentive program, CMS makes incentive payments to individual providers, not to practices or groups. According to the payor, CMS, the incentive payment is based on the provider's meaningful use of the EHRs and does not constitute reimbursement for the expenses incurred in establishing EHRs. You also indicated that prior to actual receipt of an incentive payment, a recipient may assign the payment to a third party, typically, the practice group of which the recipient is a member.

LAW AND ANALYSIS

Issue 1

Except as otherwise provided in the Internal Revenue Code (Code), a taxpayer must include in gross income "all income from whatever source derived." I.R.C. § 61(a). The Supreme Court has long recognized that the definition of gross income sweeps broadly and reflects Congress' intent to exert the full measure of its taxing power and to bring within the definition of income "all accessions to wealth." *Commissioner v. Schleier*, 515 U.S. 323, 327 (1995). Any receipt of funds is presumed to be gross income unless the taxpayer can demonstrate that the accession fits into one of the exclusions created by other sections of the Code. *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955). Exclusions from gross income are construed narrowly to maximize the taxation of any accession to wealth. *United States v. Burke*, 504 U.S. 229, 248 (1992) (Souter J., concurring).

As in the case of exclusions, a taxpayer generally is not required to include in gross income a payment that constitutes a return of capital. *Doyle v. Mitchell Brothers Co.*, 247 U.S. 179, 187 (1918). Thus, a recipient must include an incentive payment in gross income unless the recipient can demonstrate that it fits within an exclusion provided by the Code or constitutes a nontaxable return of capital. As discussed below, the CMS incentive payments neither come within an exclusion provided by the Code nor constitute a return of capital to the recipients.

In enacting ARRA, Congress did not address the taxation of incentive payments. Accordingly, the taxability of an incentive payment must be determined by applying well-established principles of taxation. According to the payor, CMS, the incentive payment is based on the provider's meaningful use of EHRs and does not constitute reimbursement for the expenses incurred in establishing EHRs. Thus, an incentive payment is a clear accession to wealth and not a return of capital. Further, the payments do not fall within any exclusion provided by the Code. Consequently, a recipient must include incentive payments in gross income under section 61 of the Code unless he or she receives the payments as a conduit or an agent of the recipient's practice group, or someone else, and is thus not allowed to keep the payments.

Under the anticipatory assignment of income doctrine, a taxpayer who earns or otherwise creates a right to receive income cannot exclude the economic gain from gross income by assigning the gain to another party because gains should be taxed to the person who earns it. *Lucas v. Earl*, 281 U.S. 111, 114 (1930); *Commissioner v. Banks*, 543 U.S. 426, 433-434 (2005). The power to dispose of income causing the income to be paid to another is equivalent of ownership for tax purposes. *Helvering v. Horst*, 311 U.S. 112 (1940).

Under the claim of right doctrine, if a taxpayer receives money under a claim of right and without restriction as to its disposition, then he has received income that he is required to report even though it may be claimed that he is not entitled to retain the money and may be ordered to restore its equivalent. *North American Oil Consolidated v. Burnet*, 286 U.S. 417 (1932). Conversely, if a person receives funds as a conduit for another or as an agent of another, then he does not have a claim of right to the funds, and the funds received are not income to him to the extent he passes them on to the person for whom the funds were intended. *Goodwin v. Commissioner*, 73 T.C. 215, 232 (1979).

In the present case, if the provider is receiving incentive payments as an agent or conduit of the provider's practice or group, or someone else, the provider is not required to include the payment in his/her gross income as long as he/she turns the payment over to the other entity or person as required. See Rev. Rul. 76-479, 1976-2 C.B. 20; Rev. Rul. 69-274, 1969-1 C.B. 36; Rev. Rul. 65-282, 1965-2 C.B. 21 and Rev. Rul. 58-220, 1958-1 C.B. 26, for instances in which the IRS has held that a recipient was not taxed on receipt of a payment because he or she was an agent of another.

Issues 2 & 3

Section 6041 requires information reporting of aggregate payments made in the course of a trade or business in excess of \$600 per year. CMS is engaged in a trade or business within the meaning of the statute because the regulations specifically include nonprofits and exempt entities within the meaning of trade or business. Treas. Reg. § 1.6041-1(b). The EHR payment is a payment of a fixed and determinable gain, profit, or income, made in the course of a trade or business, within the meaning of section 6041. Therefore, CMS has a reporting obligation with respect to the eligible providers to the extent such payments exceed \$600. Likewise, the assignment by an eligible provider of such payments to a third party would also meet this definition and therefore the eligible practitioner would have a reportable payment to the assignee under section 6041, unless an exception applies.

Payment, for the purposes of section 6041, can occur even though funds are never transferred directly to the payee. See *id.* § 1.6041-1(f). Here, CMS transfers control of the funds to the eligible provider which constitutes a payment. The eligible provider may then transfer control of the funds, by assignment, to the third party, which is also a payment. Where the eligible provider assigns the payment to a third party, CMS would be the payor with respect to the eligible provider and the eligible provider would be the payee. Then, the eligible provider would be the payor with respect to the third-party assignee, and the third-party assignee would be the payee. Under section 6041, the payor bears the obligation to report a payment.

CMS is not obligated to determine who will ultimately include the payment as income. The existence of a conduit relationship is irrelevant to CMS's reporting requirement. CMS is obligated to report the payment with respect to the eligible provider only. CMS would not be a payor with respect to a third-party assignee unless CMS makes payment directly to the third party and exercises managerial oversight with respect to, or had a significant economic interest in, the assignment. See *id.* § 1.6041-1(e)(1).

Therefore, CMS would bear the reporting obligation for the payment to the eligible provider, and the eligible provider would bear the reporting obligation, if any, with respect to the assignment to a third party. See *generally id.* § 1.6041-1.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

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