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By Electronic Filing

Internal Revenue Service
Form 990 Redesign, SE:T:EO
1111 Constitution Avenue, NW
Washington, D.C. 20224

RE: COMMENTS ON DRAFT REDESIGNED FORM 990 AND SCHEDULES

On behalf of our nearly 5,000 member hospitals, health care systems, networks and other providers of care, and our 37,000 individual members, the American Hospital Association (AHA) appreciates the opportunity to submit comments on the draft redesigned Form 990 (core form) and new draft schedules. The AHA submitted its comments on Schedule H to the Internal Revenue Service (IRS) in a separate letter.

We appreciate the work that the IRS has put into the new form and schedules and your willingness to hear comments from the hospital community. We particularly appreciate the efforts of IRS officials who participated in our conference call about the draft redesigned Form 990 and numerous schedules.

In the wake of such an ambitious effort by the IRS, it is not surprising that the tax-exempt hospital community has numerous concerns about the draft redesigned Form 990 and many of the new schedules. We believe that the IRS should address these concerns before asking hospitals to file the Form or schedules.

Our concerns can be summarized as follows:

- The filing deadline is far too short and should be extended to tax year 2010 for Form 990 and all schedules.
- Form 990 and other schedules are rife with questions that require substantial revision before the goals the IRS set for itself can be achieved. Schedule K, Supplemental Information on Tax Exempt Bonds, is particularly problematic.

We recognize that until the questions are revised and coupled with improved instructions, it is not possible to identify all the issues that hospitals may face in implementing the new Form 990 and schedules. However, we have tried to identify as many issues as possible that we believe the IRS needs to address to assist in your process.



THE CORE FORM AND SCHEDULES NEED SUBSTANTIAL REVISION

Below is our initial list of comments on the core form and other schedules based on the preliminary review of our members. Many large hospitals and hospital systems will need to fill out as many as 14 schedules, and most will have to fill out at least 8-10. This is an enormous, expensive and time-consuming undertaking for tax-exempt hospitals.

Significant revisions and refinements must be made to the core form, schedules and instructions. We think it is critical that exempt organizations be given an opportunity to review the revised set of forms, schedules and instructions in their entirety, with another 90-day review period following the re-draft. The IRS should release the second draft with instructions in 2008, and provide another 90-day review period, with a final form release by December 31, 2008.

It would be a disservice to the entire tax-exempt sector – hospitals in particular – to undertake the first major overhaul of the Form 990 in 25 years without adequate time for review and input. A rushed implementation schedule will inevitably require revisions and modifications that will be costly both to exempt organizations and the IRS, and that will not result in the desired transparency.

1. Core Form

- The IRS asked for comments on whether “the IRS should preclude group rulings”. We understand this request was intended to elicit comments on whether hospitals and other organizations that have a “group exemption” should continue to be allowed to file a group return. Some hospital systems have received group exemptions. If group returns are eliminated, this would result in a significant burden that subverts the underlying group exemption.
- Part I (Summary), Line 6 requires an organization to enter the number of individuals receiving compensation in excess of \$100,000. This question provides information of limited use to the IRS since large organizations will likely have a larger number of individuals receiving such compensation and small organizations will likely have a smaller number.
- Part I (Summary), Line 7 requires an organization to enter the highest compensation amount reported on Part II, Section A (relating to reportable compensation paid to officers, directors, trustees, key employees, highly compensated employees and independent contractors). Requiring disclosure of the highest compensation amount paid on the summary page of the core form could mislead viewers when read outside of the context of the fuller disclosure required in Part II and Schedule J.
- Part I, Lines 8a and 8b require an organization to calculate total officer, director, trustee and other key employee compensation and then to calculate a percentage by comparing total executive compensation to total program expenses. This comparison metric

provides a misleading picture of an organization's operations and should be eliminated from the form.

- Part I, Lines 19a and 19b require an organization to calculate fundraising expenses as a percentage of total contributions and grants. This percentage does not provide helpful information about an organization's operations. Notwithstanding its limited use, organizations should be given an opportunity to explain this percentage.
- Part I, Line 24b requires an organization to calculate total expenses as a percentage of net assets. This percentage is not helpful to understanding an organization's overall operations.
- Part II (Compensation and Other Financial Arrangements with Officers, Directors, Trustees, Key Employees, Highly Compensated Employees, and Independent Contractors), Section A requires information on key employees, which term is defined in part based on the disqualified person concept from the Section 4958 intermediate sanction regulations to include a "person who manages a discrete segment or activity of the organization that represents a substantial part of the activities, assets, income or expenses of the organization, as compared to the organization as a whole." Consideration should be given to defining "substantial part" or including examples in the instructions or glossary to help large organizations determine employees who would fall under the broadened definition. Hospitals could have hundreds of "key employees" if this definition is not clear.
- Part II, Section A requires an organization to list the city and state of residence of each listed individual or organization. For hospitals and health care organizations in rural areas, providing this information could be tantamount to providing an individual's home address.
- Part II, Section A requires an organization to include reportable compensation from "related organizations" for purposes of reporting the compensation of former (within the last five years) directors, trustees, officers and key employees or highest compensated employees. It seems overly burdensome for a large filing organization to be required to track all former directors, trustees, officers, key employees or highest compensated employees over a five-year period when they have had no need to do so in the past. Combining this requirement with a need to survey all related organizations to determine whether any individual in this group is being paid compensation by such related organization requires efforts beyond the value the information would provide. Information on former directors, trustees, officers, key employees or highest compensated employees should look to current year only.
- Part II, Section A requires an organization to use the compensation figures as reported on Forms W-2 or 1099. For hospitals whose tax year is not the calendar year, Forms W-2 and 1099 reporting will result in compensation data that is much more dated than the compensation data currently required. For example, if a hospital's fiscal year ends on

June 30, the hospital would file its return on November 15, with compensation data as of December 31 of the prior year.

- Part II, Section B, Lines 5a-f require an organization to report the family and business relationships of officers, directors, trustees or key employees during a five-year look-back period. Hospital and health care organizations often have boards of directors with as many as 30 members, and hundreds of contracts. The collection and maintenance of documentation required to respond to these questions will create excessive new burdens for organizations, especially for organizations with large boards of directors. Moreover, the instructions should clarify the duties of organizations to collect such information going forward.
- Part II, Section B, Line 9 requires an organization to report whether any persons listed in Part A receive compensation from any source other than the filing organization or a related organization for services rendered to the organization. In its current form, this question requires organizations to have or acquire access to information that they may not otherwise have. This question should be clarified to address the extent to which an organization is required to seek information regarding such compensation arrangements. Also, if a listed person owns a company that is paid reasonable compensation to perform services, but the person does not receive any payment other than in his capacity as owner of the organization, what amount, if any, gets reported?
- Part III (Statements Regarding Governance, Management, and Financial Reporting), Line 2 requires an organization to report any significant changes to its organizing or governing documents. The IRS should clarify that this question would only cover changes to articles of incorporation and bylaws and not other policies of the organization.
- Part III, Line 3b requires an organization to report the number of “transactions” the organization reviewed under its conflict of interest policy. The instructions or glossary should be revised to include a definition for “transactions.” Because responding with a zero or a very high number would create a misleadingly negative connotation, and because any numerical response will have a different meaning depending on the organization and its policy, the question should be revised to ask whether the organization engaged in any transactions that were subject to the policy but were not reviewed under the policy.
- Part III, Line 10 asks whether an organization’s governing body reviewed the Form 990 before it was filed. This requirement is overly burdensome, particularly for large hospital systems, which may have dozens of hospitals and related entities for which returns are being filed. The draft form does not provide a definition of “review,” which should be added to the instructions or glossary. It is unclear whether an organization can simply provide the Form 990 to its governing body or whether it needs to receive some kind of certification that each member of its governing body has in fact reviewed the form. The instructions should clarify that review by the finance or an equivalent committee of an organization’s governing body or the governing body of its parent organization is

sufficient if the governing body delegates this function. In clarifying what is meant by “review,” the IRS also should consider that boards of directors of public companies are not required to review or certify tax filings under the Sarbanes-Oxley Act.

- Part III, Line 11 asks an organization to indicate where documents are made available to the public. There is no explanation for why this is being asked.
- Part IV (Statements Regarding General Activities), Line 1d requires an organization to report the total amount of contributions received from related organizations. The instructions include as examples of related organizations, “a parent organization or affiliates at the local, state, or regional level.” The example is confusing and the instructions should instead use the definition of related organizations from the glossary. Moreover, it is unclear whether all payments to related organizations (except for payments that clearly belong under membership dues, rentals, or sales) should be treated as contributions since there is no corresponding line item under “program service revenue” or “other revenue.”
- Part IV, Lines 2a – 2g require an organization to enter a corresponding business code from the *Codes for Unrelated Business Activity* from the 2006 Instructions for Form 990-T for the various line items of “program service revenue.” The business codes on 990-T are not broad enough to reflect accurately program service revenue.
- Part IV, Line 1c requires an organization to report contributions from fundraising events. Although the instructions use an example to show that gross income from other than contributions is to be reported on Line 11a, a reference at Line 1c to such amounts reported on Line 11a would be helpful.
- Part V (Statement of Functional Expense), Line 3 requires an organization to report expenses associated with grants and other assistance to governments, organizations, and individuals outside of the U.S. This question does not provide a reference to Schedule F or the threshold for filing Schedule F. These references should be added.
- Part VII (Statements Regarding General Activities), Line 6a requires an organization to report whether it had any tax-exempt bonds outstanding at any time during the year. The instructions should clarify whether this question is intended to encompass bond financing where the 501(c)(3) organization is not the issuer of the bonds but rather the borrower of proceeds of government-issued bonds.
- Part VII, Lines 8a (and the applicable instructions) requires an organization to report whether it conducted all or a *substantial* part of its exempt activities through or using a partnership, LLC or corporation and the aggregate exempt activities conducted through or by such entities involved a *substantial* portion of the organization’s capital expenditures or operating budget, or a discrete segment or activities of the organization that represent a *substantial* portion of the organization’s assets, income, or expenses as compared to the organization as a whole. Neither the instructions nor the glossary provide a definition,

percentage or amount for the term “substantial.” It is also unclear whether Lines 8a-8c would apply to passive investments of endowment or reserve funds in partnerships or publicly traded corporations.

- Part VII, Lines 11 and 12 require an organization to report whether it has a written policy or procedure for reviewing the organization’s investments and safeguarding its exempt status with respect to transactions and arrangements with related organizations. To the extent the IRS intends to develop sample written policies, IRS should solicit input from members of the tax-exempt sector with respect to the content and form of such written policies.
- Part IX (Statement of Program Service Accomplishments), Lines 3a – 3c require an organization to describe its exempt purpose achievements for each of its three largest program services. This question should be moved to Part I of the form, as it is a key question. Organizations should be allowed as much additional space as necessary to describe more than three key activities. As drafted, 3d also directs organizations to attach a schedule listing other program services.

2. Schedule A (Supplementary Information for Organizations Exempt Under Section 501(c)(3))

- Part 1, Line 11f requires an organization to respond whether it has a “written determination from the IRS that it is a Type I, II or III supporting organization.” Since most supporting organizations do not have written determinations from the IRS, the question as written is misleading and unfair because the IRS did not actually issue such determinations until this year. The question should allow an IRS determination or “a written opinion of counsel.”
- Part 1, Line 11h, column (vii) requires an organization to report the amount of monetary support provided by the supporting organization to the supported organization(s). This question disadvantages supporting organizations such as parent holding companies within a health care system that do not pay out monetary grants or other support payments because they are functionally integrated or otherwise undertake activities in support of their supported organizations. The question should be revised to include the value of non-monetary support.

3. Schedule C (Political Campaign and Lobbying Activities)

- Part II-B requires reporting by an exempt organization, including reporting on (b) paid staff or management and for (h) seminars, conventions, speeches, lectures or any other means. It is not clear precisely what the IRS is attempting to capture under (h) and that the category needs to be so broad. Also, instead of asking for precise amounts, the IRS should ask for a range of hours, number of employees or other proxies for amounts that

would provide the IRS with useful information while making the category less burdensome.

4. Schedule D (Supplemental Financial Statements)

- Parts I and III: Passive investments should be excluded from this schedule, and the listing of securities individually is extremely burdensome.
- Part VII (Other Liabilities) requires organizations to describe and list the book value of any other liabilities, including federal income tax liabilities, not reportable in the defined categories on Part VI (Balance Sheet) of the core form. Part VII also requires organizations to provide the text of the footnote to the organization's financial statements that report the organization's liability for uncertain tax positions under FIN 48. Disclosing the text of footnotes relating to uncertain tax positions in isolation could be misleading. Organizations should be given the opportunity to explain such footnotes or to attach their entire financial statement.
- Part XII (Endowment Funds) requires an organization that holds assets in term or permanent endowment funds to provide information for the past five years on fund balances, contributions, investment earnings or losses, program expenditures and administrative expenditures. The reporting burden associated with this question seems to outweigh the usefulness of this information. The five-year look-back period should be reduced or eliminated pending adoption by the IRS of reasonable standards.

5. Schedule F (Statement of Activities Outside the U.S.)

- It is unclear whether Schedule F requires that "captive insurance" activities be reported. Since any organization with captive insurance activity is required to complete IRS Form 5471, such reporting should be referenced here, or the organization should be specifically exempted from reporting again on this form.
- Schedule F requires the separate reporting of grants outside the U.S. from grants to domestic organizations and individuals. Many hospitals and health care organizations do not maintain records and reports in a format that would permit them to gather all of the information required to be reported on Schedule F. The required amount of recordkeeping and reporting could discourage organizations from making grants, particularly small ones, to foreign organizations or individuals. Moreover, the data required to be reported on the schedule could potentially threaten the safety and security of organizations and individual grant recipients, therefore Schedule F should not be open to public disclosure.
- It is unclear whether the activities of foreign affiliates of U.S. organizations are covered by Schedule F.

- Part I (General Information on Accounts and Activities Outside the United States), Line 2 requires an organization to describe its procedures for selecting grant recipients located outside the U.S. and monitoring the use of grant funds. The disclosure of an organization's grantmaking procedures is intrusive for a public document. This question should be similar to Schedule I, which simply asks whether the organization maintains records to substantiate its grant making process.
- Part II (Grants and Other Assistance to Organizations or Entities Outside the United States), Lines 2-3 require an organization to report the number of foreign 501(c)(3) organization grant recipients and the total number of other organizations or entities. This information seems misleading given that most foreign organizations are not formally recognized as 501(c)(3) organizations by the U.S., and the regulatory structure for charitable organizations in many countries is not easily comparable to U.S. requirements.
- Part II, line 1, column (g) requires that non-cash gifts be reported, and that the fair market value be the basis for the reporting. Hospitals should be exempted from reporting gifts of equipment and supplies since there are many such transfers of fully depreciated items.
- Part III (Grants and Other Assistance to Individuals Outside the United States) requires an organization to report grants of more than \$5,000 to individuals outside the U.S. Part II (Grants and Other Assistance to Organizations or Entities Outside the United States) requires organizations to check a box if no one recipient received more than \$5,000. Part III should include a similar check-the-box statement to clarify the guidance set forth in the instructions, i.e., that organizations are not required to complete Part III if no one recipient received more than \$5,000.

6. Statement G (Supplemental Information Regarding Fundraising Activities)

- Schedule G requires an organization to report supplemental information regarding its fundraising activities. The IRS should clarify how organizations should report fundraising activities by related entities, which is a common occurrence within a health system.

7. Schedule J (Supplemental Compensation Information)

- Schedule J requires an organization to report supplemental compensation information with respect to listed persons from Part II of the core form. There still seems to be confusion about who gets reported on Schedule J, so the instructions should further clarify the individuals for whom such information must be reported.
- Line 1, column (C) requires an organization to report non-qualified deferred compensation. The instructions should clarify, or the schedule itself should eliminate,

double-reporting of nonqualified compensation. This occurs when the amounts of unpaid, unvested deferred compensation are reported when awarded and again when they are vested. Eliminating the double reporting will give a more accurate picture of yearly compensation. The double reporting of deferred compensation is a problem under the current Form 990 and the IRS should take this opportunity to correct the confusion. This question also must address how compensation should be reported if the organization is reporting on an accrual basis.

- Line 1, column (D) requires an organization to report the amount of non-taxable fringe benefits provided to the listed persons in column (A). The instructions seem to even require reporting of de minimis fringe benefits, which by definition under the Internal Revenue Code are “so small as to make accounting for it unreasonable or administratively impracticable.” The instructions should follow the current Form 990, which allows de minimis fringe benefits to be excluded. The instructions or the compensation matrix also should include examples of nontaxable fringe benefits that physicians would typically be issued as part of providing services at a hospital, e.g., pagers, cell phones and other similar items, or this requirement should be eliminated.
- Line 1, Column (E) requires an organization to report the amount of all expense reimbursements, and allowances provided for expenses, that are not included on a recipient’s W-2. It is completely misleading to report such amounts on Schedule J, which is intended to disclose compensation amounts. Expense reimbursements under accountable plans that do not result in income to the recipient should not have to be reported on Schedule J.
- Lines 4 and 5 require an organization to report whether it paid compensation determined in whole or in part by the revenues or net earnings of the organization or a related organization. The instructions should clarify the types of compensation arrangements that would and would not be deemed to be determined in whole or in part by the revenues or net earnings of hospitals or health care organizations.

8. Schedule K (Supplemental Information on Tax Exempt Bonds)

We are particularly concerned about Schedule K; a number of hospitals have described the burden associated with this schedule as akin to a full-scale audit, costing, potentially, millions of dollars.

- Schedule K requires an organization to report supplemental information for each outstanding bond issue with an aggregate principal amount in excess of \$100,000 on the last day of the taxable year. Due to the scope of information required for reportable tax-exempt bonds, the IRS should delay implementation of Schedule K (along with all of the Form 990) until 2010 so that organizations will have sufficient time to complete the analyses required for reporting the new information on the schedule. Also, since the schedule asks for information regarding all bonds outstanding on the last day of the

taxable year, no matter how long ago the bonds were issued, organizations may not have all of the requested information because there was no notice at the time the bonds were issued that the organization would be required to report such information to the IRS. Accordingly, the IRS should provide a "grandfather" provision under which information is required to be reported only for bonds issued after the date that the redesigned Form 990 was made public. Also, in light of the IRS' recently announced post-issuance compliance check program, the IRS should consider delaying finalization of this Schedule until the IRS has analyzed the responses to the questionnaires being sent out as part of the program.

- Part I requires extensive information for each outstanding tax-exempt bond issue with a principal amount greater than \$100,000 on the last day of the tax year. This section is enormously burdensome and needs to be streamlined. First, the IRS should recognize that much of the information requested here is already available through Form 8038, Information Return for Tax-Exempt Private Activity Bond Issues, which is filed when the bonds are issued. The new schedule should be reconciled with the reporting already required to eliminate redundancy and burden. Part I, columns F and G, in particular, represent a particular burden for hospitals. For example, for bonds with large principal amounts that funded multiple projects, including buildings and equipment, requiring information on the date that a particular project was placed into service is very difficult and burdensome to provide.
- Part II requires the provision of information on bond proceeds. The instructions for this section should make it clear that when an organization is dealing with a refunding issue it is not necessary to report how the proceeds of the prior issue were spent. Alternatively, the instructions should reduce the burden associated with reporting this information by, for example, limiting how far an organization must go back when a bond is used to refund a prior issue. In addition, the current IRS regulations permit an organization that funds projects with a mixture of equity and bond proceeds to wait 18 months after facilities are placed into service to allocate the sources of those funds to particular costs. That means, at the time an organization may be required to file this schedule, there may not be a final allocation. The instructions for the form should reconcile this inconsistency in favor of delayed reporting.
- Part III requires an organization to report information about private use of tax-exempt bonds. The instructions should clarify that aggregate reporting for private business use is contemplated and the IRS should consider permitting organizations to report private business use as not exceeding a stated de minimis percentage. And, Part III could be streamlined if it allowed organizations to limit the reporting of contracts to those that do not meet the "safe harbors" described in Revenue Procedures 97-13 or 97-14. Question 4 should be re-written, as it does not take into consideration that a hospital may be meeting such "safe harbor" requirements, which would make the percentage computation unnecessary. Also, question 5a, requesting information about all other "use" by other than a 501(c)(3) organization or state or local government is overly broad, as it would presumably include use that is not treated as private use, such as incidental use or use on

the same basis as the general public. Additionally, questions 4 and 5 could result in misleading answers, as they fail to anticipate that these percentages may change from year to year and that the proper measure of usage would be the entire term of the bond.

- Part IV requires an organization to report information about the compensation of third parties who provide services related to bond issuances and whether such parties were selected using a “formal selection process.” The instructions should clarify what is meant by a “formal selection process” and should permit organizations to rely on selections that involved advice of bond counsel and/or a qualified underwriter with a reasonable review of qualifications. In addition, a threshold amount for reportable transactions should be added.

9. Schedule I (Supplemental Information on Grants and Other Assistance to Organizations, Governments, and Individuals in the U.S.)

Part III requires an organization to report grants and other assistance to individuals in the U.S., if the grant amount is \$5,000 or more. This threshold should be increased substantially for large organizations like hospitals. The instructions and the schedule should clarify whether, consistent with the instructions to Schedule F, Part III, organizations need not complete Part III if no individual received more than the new threshold.

10. Schedule L (Supplemental Information on Loans)

Schedule L requires an organization to report details on loans to and from officers, directors, trustees, key employees, *highly* compensated employees and disqualified persons. The schedule and instructions should reference “*highest* compensated employees” from Part II of the core form, which is also the defined term in the glossary. The use of the expression “*highly* compensated employee” is unnecessarily confusing in this context.

11. Schedule M (Non-Cash Contributions)

The threshold for completing this schedule should be increased to at least \$20,000.

12. Schedule N (Liquidation, Termination, dissolution or Significant Disposition of Assets)

- Clarification is needed as to whether transfers to a wholly owned limited liability company that is disregarded as separate from the tax-exempt filing organization need to be reported.

- Clarification is needed as to whether transfers for “full and adequate consideration” that are excluded from the definition of “substantial contraction” still need to be reported as a disposition of net assets.

13. Schedule R (Related Organizations)

The following comments relate to Part V – Transactions with Related Organizations.

- For multi-hospital systems, Schedule R is extremely burdensome. At a minimum, the definition of “related” needs further review and consideration, as there are many definitions of the term that might have been used.
- Part V requires an organization to report whether it engaged in certain transactions or transfers with related organizations, including related 501(c)(3) organizations. The instructions carve out transactions between 501(c)(3) organizations where the only transactions between the organizations were gifts or grants. This instruction should be revised to allow transfers that are gifts and grants to be excluded, even where the organizations have other transactions such as leasing or services arrangements.
- The definition of “transfer” in the instructions should be revised as follows: A transfer includes any conveyance of funds or property, whether or not for consideration, *except for gifts or grants between related 501(c)(3) organizations.*
- The compliance burden from this section is of great concern to our members. Tax-exempt organizations within a health system typically have numerous arrangements involving the performance of services, leasing or sharing of facilities, equipment or employees, cost reimbursement etc. By way of example, a typical 501(c)(3) health system could have hundreds of transactions to report under Part V. The AHA understands that certain questions on this schedule are in response to Section 1205 of the Pension Protection Act (PPA), but the information on transactions between related 501(c)(3) organizations should be limited to transfers that could result in UBIT under the controlled entity rule of Section 512(b)(13). Other transactions between related 501(c)(3) organizations do not raise compliance, exemption, tax or other concerns and should not need to be reported.
- Schedule R goes beyond what is required under the PPA, which at least limits reporting of transfers among “controlling and controlled” organizations. By defining “related” as including brother/sister organizations controlled by the same person or persons, Schedule R requires any exempt entity within a health care system to include all transfers between it and any other entity within the system, which completely expands the already overly broad disclosure required by the PPA. These requirements are completely unworkable in the health system setting and, again, result in the reporting of transactions that do not raise compliance, exemption, tax or other concerns.

- The instructions for column (C) require the amount involved in each transaction to be reported, which is defined as the fair market value of the services, cash and other assets provided by the organization or the fair market value received, whichever is higher. This instruction seems to require even related 501(c)(3) organizations that have cost reimbursement arrangements to determine the fair market value for these arrangements, which creates a significant valuation burden for arrangements that should not even need to be reported.

We appreciate the opportunity to submit comments; we especially appreciate the IRS' effort to reach out to the hospital community and better understand its concerns. We welcome the opportunity to work with the IRS to improve the core form and schedules. Please contact me at (202) 626-2336 or mhatton@aha.org for further assistance.

Sincerely,

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Melinda Reid Hatton
Senior Vice President and General Counsel