

# Hospitals' Tax-exempt Status

## Background

America's hospitals provide compassion, care and curing 24 hours a day, seven days a week. But not-for-profit community hospitals do more than care for the injured and infirm; they promote and protect the health and well-being of the entire community through responsive programs and services. Not-for-profit hospitals are distinguished by certain charitable obligations that have evolved over time to keep pace with the needs of the American people.

Over the past several years, policymakers and the public have raised concerns about hospitals' tax-exempt status and the lack of uniformity with regard to charity care and financial assistance. A number of congressional hearings focused on what not-for-profit hospitals do to meet their charitable obligations and whether the current rules are sufficient. In addition, the governance and executive compensation practices of charitable organizations, including tax-exempt hospitals, have been scrutinized.

Until the Internal Revenue Services' (IRS) recent efforts to update the reporting forms for tax-exempt organizations and create a reporting form unique to hospitals, there was no uniform approach or format for tax-exempt hospitals to follow in reporting the "community benefit" they provide, and no requirement for hospitals to make such reports public. With the December 2007 release of the IRS' final revised Form 990 and a new Schedule H for hospitals, tax-exempt hospitals now have a uniform approach and format for reporting the community benefit provided to their communities and making it available to their communities. Beginning in tax year 2009 tax-exempt hospitals that file a Form 990 will be required to file a newly created schedule for hospitals (Schedule H) as an attachment to their core Form 990.

## AHA View

The AHA has adopted policies and guidelines on billing, collection practices and tax-exempt status. These guidelines call for greater accountability and transparency of hospitals, increased financial assistance for uninsured patients of limited means and fair and transparent billing and collection practices. For not-for-profit hospitals, the AHA Board of Trustees recommended the public reporting of community benefit activities and increased financial accountability. The combination of the revised Form 990 and the new Schedule H will provide the public an unprecedented amount of information.

**Encourage Public Reporting.** IRS' finalized new Schedule H for hospitals represents an important step in the hospital field's ongoing efforts to increase transparency by providing a standard reporting format for many of the benefits that hospitals provide to the communities they serve.

The AHA vigorously advocated with IRS for a reporting form that would provide a comprehensive picture of the value of services hospitals provide to and for their communities. The final Schedule H reflects many, but not all, of the improvements recommended by the AHA and the hospital community. For example, the IRS added a new section for reporting Medicare underpayment and patient bad debt and the costs of those activities that benefit the community. This inclusion, along with additional space for hospitals to calculate and describe the full value of their programs and activities, should promote greater transparency and community accountability. The AHA championed these positions, as well as successfully urged restoration of reporting community building activities (e.g., economic development, community support and workforce development).

To help hospitals understand and prepare for Schedule H, the AHA partnered with Ernst & Young to collect and analyze information from “mock” or “dry run” Schedule Hs from tax-exempt hospitals. The AHA will use the information from this Schedule H project to provide feedback and best practices to the field that will help improve Schedule H filings for tax year 2009. In addition, the AHA's new resource, *Telling the Hospital Story – Going Beyond Schedule H*, will help non-profit hospitals communicate the full scope of their community benefit, including a range of programs, services and activities that hospitals provide everyday. It includes a strategy checklist for leaders, a worksheet for completing a community benefit report, sample community benefit reports and communications strategies.

**Retain the Community Benefit Standard.** Since 1969, not-for-profit hospitals have been able to fulfill their charitable obligations through an appropriate mix of charity care, financial assistance to low-income patients, subsidized health care, research, health professions education and other community-building activities that are tailored to the needs of the communities they serve. As even the IRS' own General Counsel staff has noted, the IRS' community benefit standard continues to work well for not-for-profit hospitals and, more importantly, the communities they serve. The standard permits hospitals to satisfy their community benefit obligations by providing the right mix of programs and services to their communities. While Schedule H does not technically alter the existing community benefit standard, the near absence of questions relating to the factors that comprise the standard raises significant questions about the schedule. Those include how a court would view the schedule's relevance in the event of a dispute over a hospital's tax-exempt status, and whether the IRS will use the data collected as a basis to propose formal changes to the community benefit standard.

**The AHA will work with Congress and the IRS to ensure that the current community benefit standard is retained because it provides hospitals with the flexibility to best tailor their programs to effectively target the needs and unique conditions of their local community.**

**Increase Financial Accountability.** The AHA Board also recommends that not-for-profit hospitals increase financial accountability using the IRS Form 990. Recommended steps include having the CEO, chief financial officer or highest ranking officer sign off on the Form 990. In addition, loans to board members or executives should be prohibited. The revised Form 990 now includes questions about the existence of a conflict-of-interest policy and availability to the public. We were pleased that a 2006 Government Accountability Office survey on executive compensation practices at not-for-profit hospitals found widespread adoption of best practices, such as appointment of an executive compensation committee with primary responsibility for approving salary and bonuses, conflict-of-interest policies that extend to all members of the executive compensation committee and consultants, and reliance on market data to make compensation decisions. In addition, in the IRS' recent report on its compliance check project, the Service noted that nearly all of those hospitals surveyed complied with its protocol for determining that compensation is fair and reasonable. The AHA will continue to monitor and engage with the IRS as needed on its general tax-exempt organization compliance activities that affect hospitals.



*Dollars alone can never communicate the complete story of how communities benefit from the programs and services that not-for-profit hospitals provide.*

The AHA's **Community**

**Connections** initiative helps

*our members effectively inform policymakers and the public of the full value hospitals provide. Today, hospitals of all kinds – urban and rural, large and small – are making their communities healthier in ways that are as diverse as the needs of each community.*

*The following programs exemplify the tremendous good being done every day by America's not-for-profit hospitals. They illustrate where and how hospitals are meeting their communities' many needs and why they merit broad public support.*

#### ■ **La Rabida Community Asthma Program for Children (LCAPC)**

LCAPC was formed by the hospital in response to startling statistics about asthmatic children – asthma is the number one cause of pediatric hospitalizations, resulting in as many as 14 million lost school days each year. Working with the public schools, LCAPC identifies at-risk children, screens and diagnoses them, and then educates parents and teachers on the signs and triggers of asthma, how to respond in an emergency and how to improve physical environments to reduce asthma triggers. LCAPC then helps connect students with the proper medical resources to help manage their conditions.

*La Rabida Children's Hospital  
Chicago, Illinois*

#### ■ **Operation Safety Net (OSN)**

An innovative street outreach program for the unsheltered and transient homeless population, OSN consists of 14 teams that perform medical rounds by walking the city's streets, alleys

and riverbanks providing prenatal care, health counseling, TB and HIV testing, and protection from severe weather conditions through an organized shelter. The program trains approximately 100 residents and medical and nursing students annually in street medicine.

*The Mercy Hospital of Pittsburgh  
Pittsburgh, Pennsylvania*

#### ■ **Perinatal HIV: Know Your Status, Protect Your Baby**

This multi-faceted program ensures women to know their HIV status and receive preventative treatment before giving birth. The program uses patient classes, the hospital magazine, physician and staff training, case management and hospital protocols to educate patients and staff. Brochures and teaching materials also are distributed through various community outreach programs. Baton Rouge has one of the nations' highest rates of AIDS cases. Without intervention, as many as 20-30 percent of HIV-infected pregnant woman could transmit the virus to their infants. But with appropriate treatments, the rate can be reduced to 1-2 percent.

*Woman's Hospital  
Baton Rouge, Louisiana*

#### ■ **Ready-Set-Go**

Ready-Set-Go is an annual back-to-school event organized by the hospital and The Salvation Army. The event provides low-income children in grades K-12 with sports physicals and the supplies they need to start the school year. Each child receives a health kit; a school backpack filled with school supplies; coupons or vouchers to local retail, shoe and clothing stores; haircut vouchers; hearing, vision and dental screens; a public library card; and information on topics ranging from diabetes education to health insurance.

*Beatrice Community Hospital and Health Center  
Beatrice, Nebraska*