The Basics of Community Benefit Accounting

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- Experience at KPMG, The Lewin Group, and San Francisco Department of Public Health
- Lead architect of CHA’s community benefit accounting framework, (Social Accountability Budget, 1989)
- Contributor to “what counts as community benefit” guidelines; serve on What Counts Task Force
- Drafted sections of IRS Form 990, Schedule H instructions; contributed to subsequent updates
- Specialize in all 501(r)-related topics: policy and practice
- Broad practice in strategic and financial planning
- Board President of FQHC in Alexandria, Virginia

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Outline

- Community benefit reporting principles
- Community benefit accounting, by category
  - Definitions
  - Accounting methodologies
  - Issues and opportunities
- Summary

IRS Form 990, Schedule H “Community Benefit Table”
Community Benefit Reporting: What Counts and Accurate Accounting

Programs and Activities Meeting What Counts Criteria

Accurate Revenue and Cost Accounting

Community Benefit Reporting

IRS: What Counts as Community Benefit?

- To count, a program or activity must respond to a demonstrated health/related community need and seek to achieve at least one community benefit objective:
  - Improve Access to Health Services
  - Enhance Public Health
  - Advance Generalizable Knowledge
  - Relief of a Government Burden to Improve Health
IRS: Demonstrating Community Need

- Community need may be demonstrated through:
  - A community health needs assessment (CHNA), or
  - Documentation that a request from a public agency or community group was the basis for initiating or continuing the activity or program, or
  - The involvement of unrelated, collaborative tax-exempt or government organizations as partners

IRS: Programs that should not be counted

- Activities or programs may not be reported:
  - if they are provided primarily for marketing purposes
  - if the program is more beneficial to the organization than to the community; for instance,
    - if the activity or program is designed primarily to increase referrals of patients with third-party coverage,
    - required for licensure or accreditation, or
    - restricted to individuals affiliated with the organization.
Not IRS: Programs that should not be counted

- An objective, “prudent layperson” would question whether the program truly benefits the community

- The program represents a community benefit that does not involve a reportable expense by the organization, e.g.
  - Benefits provided by employees on their own time
  - Benefits provided by other entities (expense is not on the EIN’s Form 990, Part IX)

Not IRS: Programs that should not be counted

- The initiative is designed only to benefit the organization’s own patients or covered lives, e.g.
  - Programs to prevent or reduce readmissions for hospital’s own discharged patients
  - Programs to reduce PMPM costs exclusively for patients/ members for whom the organization bears risk (or might participate in shared savings)
Key Community Benefit Accounting Principles

- Only report expense actually incurred (borne) by the hospital organization (and also on Core Form) – including joint venture proportionate shares
- Report actual (auditable) expense and not “opportunity costs”
- Include indirect (overhead) costs for every category
- Use “most accurate” cost accounting methods
- Avoid double-counting community benefit expense

Key Community Benefit Accounting Principles

- If in doubt, follow generally accepted accounting principles (GAAP)
- Apply the “matching principle”
- Monitor and assure compliance with any instructions changes
- Maintain an audit trail
- Disclose accounting methods (e.g., in footnotes to community benefit reports and in Part VI of Schedule H)
Some Cross-Cutting Issues

- Negative net community benefit expense (gains)
  - No negatives allowed in column (e), but
  - Any gains should flow into rows (d), (j), and (k)

- Accounting for restricted grants received
  - Value = amounts used during year
  - Value ≠ total amount of grant received during year

- Accounting for capital expenditures (buildings, equipment)
  - “Expense” ≠ “Expenditures”
  - Expenditures are amortized (depreciated) over time

- Alignment with financial statements (e.g., Medicaid revenue)

Schedule H, Part I, Line 7
Financial Assistance means free or discounted health services provided to persons who meet the organization’s criteria for financial assistance and are thereby deemed unable to pay for all or a portion of the services.

“Financial Assistance” does not include:

- bad debt or uncollectible charges;
- Medicaid or Medicare shortfalls;
- Self-pay or prompt-pay discounts; or
- contractual adjustments with any third party payors.

Worksheet 1: Financial Assistance

<table>
<thead>
<tr>
<th>Description</th>
<th>Formula/Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross patient charges</td>
<td></td>
</tr>
<tr>
<td>1. Amount of gross patient charges written off under financial assistance policies</td>
<td>1.</td>
</tr>
<tr>
<td>Total community benefit expense</td>
<td></td>
</tr>
<tr>
<td>2. Ratio of patient care costs to charges (from Worksheet 2, if used)</td>
<td>2.</td>
</tr>
<tr>
<td>3. Estimated cost (multiply line 1 by line 2, or obtain from cost accounting)</td>
<td>3.</td>
</tr>
<tr>
<td>5. Total community benefit expense (add lines 3 and 4, enter on Part I, line 7a, column (f))</td>
<td>5.</td>
</tr>
<tr>
<td>Direct offsetting revenue</td>
<td></td>
</tr>
<tr>
<td>6. Revenue from uncompensated care pools or programs</td>
<td>6.</td>
</tr>
<tr>
<td>7. Other direct offsetting revenue</td>
<td>7.</td>
</tr>
<tr>
<td>8. Total direct offsetting revenue (add lines 6 and 7, enter on Part I, line 7a, column (g))</td>
<td>8.</td>
</tr>
<tr>
<td>9. Net community benefit expense (subtract line 8 from line 5, enter on Part I, line 7a, column (g))</td>
<td>9.</td>
</tr>
<tr>
<td>10. Total expense (enter amount from Form 990, Part IX, Line 25, column (A), including the organization’s share of joint venture expenses, and excluding any bad debt expense included in Part IX, line 26)</td>
<td>10.</td>
</tr>
<tr>
<td>11. Percent of total expense</td>
<td>(divide line 9 by line 10, enter on Part I, line 7a, column (i))</td>
</tr>
</tbody>
</table>
Issues and Opportunities: Financial Assistance

- Issues:
  - Aligning write-offs with the financial assistance policy (FAP)
  - Aligning interim data with year-end audit

- Opportunities:
  - Comparative ratio: charity / (charity + bad debt)
  - FAP eligibility criteria
  - Reclassifying bad debt to charity
  - Predictive modeling for patients without completed applications
  - Reverse self-pay discounts for accounts with any financial assistance (count all discounts as charity care)

Worksheet 2: Ratio of Patient Care Cost to Charges

<table>
<thead>
<tr>
<th>Patient care cost</th>
<th>1. Total operating expense</th>
<th>1.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3. Medicaid provider taxes, fees, and assessments</td>
<td>3.</td>
</tr>
<tr>
<td></td>
<td>4. Total community benefit expense</td>
<td>4.</td>
</tr>
<tr>
<td></td>
<td>5. Total community building expense</td>
<td>5.</td>
</tr>
<tr>
<td></td>
<td>6. Total adjustments (add lines 2 through 5)</td>
<td>6.</td>
</tr>
<tr>
<td></td>
<td>7. Adjusted patient care cost (subtract line 6 from line 1)</td>
<td>7.</td>
</tr>
<tr>
<td></td>
<td>10. Adjusted patient care charges (subtract line 9 from line 8)</td>
<td>10.</td>
</tr>
<tr>
<td>Calculation of ratio of patient care costs to charges</td>
<td>11. Ratio of patient care cost to charges (divide line 7 by line 10; report on the applicable lines of Worksheets 1, 3, or 8)</td>
<td>11.</td>
</tr>
</tbody>
</table>
Issues and Opportunities: Ratio of Patient Care Cost to Charges

- Issues:
  - Assuring the ratio is adjusted to address double-counting
  - Similar adjustments advised if using alternative cost accounting methods

- Opportunities:
  - Cost out “nonpatient care activities” rather than using “other operating revenue” as a proxy
  - Consider using a “more accurate cost accounting method,” as allowed by instructions

Schedule H, Part I, Line 7

<table>
<thead>
<tr>
<th>Financial Assistance and Certain Other Community Benefits at Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Financial Assistance and Means-Tested Government Programs</strong></td>
</tr>
<tr>
<td>a. Financial Assistance at cost (from Worksheet 1)</td>
</tr>
<tr>
<td>b. Federally financed medical assistance programs at cost (from Worksheet 2)</td>
</tr>
<tr>
<td>c. Federally financed medical assistance non-medical services at cost (from Worksheet 3)</td>
</tr>
<tr>
<td>d. Nonmedical services at cost (from Worksheet 4)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>e. Community health department services and community benefit programs (from Worksheet 5)</td>
</tr>
<tr>
<td>f. Technical assistance (from Worksheet 6)</td>
</tr>
<tr>
<td>g. Subsidized health services (from Worksheet 7)</td>
</tr>
<tr>
<td>h. Other (from Worksheet 8)</td>
</tr>
</tbody>
</table>

| i. Cash and in-kind contributions for community benefit (from Worksheet 9) |
| j. Total: Other Benefits                                              |
| k. Total: Add lines 7d and 7j |
Line 7b - Medicaid and Line 7c - Other Means Tested Government Programs

- “Medicaid” means the United States health program for individuals and families with low incomes and resources.
- “Other Means Tested Government Programs” means government sponsored health programs where eligibility for benefits or coverage is determined by income and/or assets. Examples include:
  - State Children’s Health Insurance Program (SCHIP)
  - Other federal, state, or local health/indigent care programs that are means-tested
Issues and Opportunities: Medicaid and Other Means-Tested Government Programs

- Issues:
  - Exclude government health programs that are not means-tested
  - Include both Medicaid fee for service and Medicaid managed care activities – from all states
  - Align offsetting revenue with financial statements; exclude direct GME revenue and include any IME revenue

- Opportunities:
  - Include expense of provider tax, fees, assessments used to maximize federal Medicaid matching funds
  - Assure that Medicaid managed care recipients are accounted for as Medicaid
  - Use “most accurate” cost accounting method

Schedule H, Part I, Line 7

<table>
<thead>
<tr>
<th>Financial Assistance and Certain Other Community Benefits at Cost</th>
<th>Number of activities or programs (optional)</th>
<th>Persons served (optional)</th>
<th>Total community benefit expense</th>
<th>Direct offsetting revenue</th>
<th>Net community benefit expenses</th>
<th>Percent of total expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Assistance at cost (from Worksheet 1)</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Medicaid (from Worksheet 2, column 1)</td>
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</tr>
<tr>
<td>Costs of other means-tested government programs (from Worksheet 2)</td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>Total Financial Assistance and Means-Tested Government Programs</td>
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</tr>
<tr>
<td>Community health experiment service or program benefit operations (from Worksheet 3)</td>
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<tr>
<td>Health professions education (from Worksheet 5)</td>
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<tr>
<td>Babcockized health services (from Worksheet 6)</td>
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<tr>
<td>Research (from Worksheet 7)</td>
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</tr>
<tr>
<td>Cash and in-kind contributions for community benefit (from Worksheet 8)</td>
<td></td>
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</tr>
<tr>
<td>Total Other Benefits</td>
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<td></td>
</tr>
<tr>
<td>Total, Add lines 7d and 7j</td>
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</tr>
</tbody>
</table>
### Line 7e – Community Health Improvement Services and Community Benefit Operations

- “Community health improvement services” means activities or programs carried out or supported for the express purpose of improving community health that are subsidized by the health care organization.
  - Such services do not generate inpatient or outpatient bills, although there may be a nominal patient fee or sliding scale fee for these services.

### Community Health Improvement Categories

1. Community health education, including classes and education campaigns, support groups, and self-help groups
2. Community-based clinical services, such as screening, annual flu vaccine clinics, and mobile units
3. Health care support services, such as transportation, case management, and enrollment into Medicaid and exchanges
4. Social and environmental activities with evidence-based association with health improvement, such as violence prevention, improving access to healthy foods in “food deserts,” and removal of asbestos and lead in public housing
Line 7e – Community Health Improvement Services and Community Benefit Operations

- “Community benefit operations” means activities associated with community health needs assessments as well as community benefit planning and administration.
  - Community benefit operations also include the organization’s activities associated with fund raising or grant-writing for community benefit programs.

Worksheet 4: Community Health Improvement Services and Community Benefit Operations
Issues and Opportunities: Community Health Improvement Services and Operations

Issues:

- Assure "what counts" criteria are met
- Assure all costs can be found in “total operating expense” (Core Form)

Opportunities:

- Assure that all programs and activities that can be reported are identified (comprehensive inventory)
- Assess whether certain community building programs (Part II) qualify as community health improvement (Part 1, Line 7e)
- Assure that total expense includes both direct cost and indirect cost
- Include an auditable portion of “system-office” cost (management fee/corporate allocation) in “community benefit operations”
- Don’t omit costs to help people become eligible for Medicaid and/or the marketplace

Schedule H, Part I, Line 7

<table>
<thead>
<tr>
<th>Financial Assistance and Cost Sharing of Government Programs</th>
<th>% Number of Items or Programs (Optional)</th>
<th>% Persons Served (Optional)</th>
<th>% Total Community Benefit Expenses</th>
<th>% Direct Operating Revenue</th>
<th>% Indirect Community Benefit Expenses</th>
<th>% Percent of Total expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Financial Assistance at cost (from Worksheet 1)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Medicaid (from Worksheet 2, column d)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>c. Costs of other revenue-funded government programs (from Worksheet 2, column e)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>d. Total Financial Assistance and Cost Sharing of Government Programs</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>e. Community health improvement services and community benefit</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>f. Health professions education (from Worksheet 2)</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>g. Other benefits (from Worksheet 3)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>h. Health sciences (from Worksheet 4)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>i. Cash and in-kind contributions for community benefit (from Worksheet 4)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>j. Total Other Benefits</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>k. Total Add lines 7d and 7f</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
“Health professions education” means:

- educational programs that result in a degree, certificate, or training that is necessary to be licensed to practice as a health professional, as required by state law; or
- continuing education that is necessary to retain state license or certification by a board in the individual’s health profession specialty.

“Health professions education” does not include education or training programs available only to the organization’s employees and medical staff or scholarships provided to those individuals.

- However, it does include education programs if the primary purpose of such programs is to educate health professionals in the broader community.
- Costs for medical residents and interns may be included, even if they are considered “employees” for purposes of Form W-2 reporting.
### Issues and Opportunities: Health Professions Education

#### Issues:
- Only include education aligned with instructions
- Avoid over-reporting costs associated with precepting nursing and other students
- Exclude programs restricted to hospital staff (including medical staff, but excluding interns and residents)

#### Opportunities:
- Include expenses for all reportable health professions education programs (e.g., pharmacy techs, medical students, others)
- Assess affiliation agreements between teaching hospital(s) and school(s)
- Exclude IME revenue from offsetting revenue
Line 7g - Subsidized Health Services

- "Subsidized health services" means clinical services provided despite a financial loss to the organization.
  - The financial loss is measured after removing losses, measured by cost, associated with bad debt, charity care, Medicaid and other means tested government programs.
- In addition, in order to qualify as a subsidized health service, the organization must provide the service because it meets an identified community need.
Line 7g - Subsidized Health Services

- If the organization no longer offered the service,
  - it would be unavailable in the community,
  - the community’s capacity to provide the service would be below the community’s need, or
  - the service would become the responsibility of government or another tax-exempt organization.

- Subsidized health services include …
  - physician clinics and
  - skilled nursing facilities

  … if such clinics or facilities satisfy the general criteria for subsidized health services …

Line 7g - Subsidized Health Services

- An organization that includes any costs associated with physician clinics … must describe that it has done so and report in Part VI the amount of such costs …

- (Tax Year 2013) Only report physician clinics as subsidized health services if the hospital generates losses on the “technical side” in addition to the “professional side” of the service

- Subsidized health services generally exclude ancillary services
**Issues and Opportunities: Subsidized Health Services**

- **Issues:**
  - Include subsidized health services, if any are reportable during the tax year
  - Use care reporting “physician clinics”
  - Subtract Medicare-related revenues and expenses from Schedule H Part III

- **Opportunities:**
  - Exclude services with gains during the tax year (even if previously reported)
  - Rely on “most accurate” cost accounting methodology available
Schedule H, Part I, Line 7

### Line 7h - Research

- “Research” means any study or investigation that receives funding from a tax-exempt or governmental entity of which the goal is to generate generalizable knowledge that is made available to the public, such as about
  
  - underlying biological mechanisms of health and disease, natural processes or principles affecting health or illness;
  - evaluation of safety and efficacy of interventions for disease such as clinical trials and studies of therapeutic protocols;
  - laboratory based studies;
  - epidemiology, health outcomes and effectiveness;
  - behavioral or sociological studies related to health, delivery of care, or prevention;
  - studies related to changes in the health care delivery system;
  - and communication of findings and observations (including publication in a medical journal).
Worksheet 7: Research

Issues and Opportunities: Research

Issues:
- Only report studies that have been funded by government or a tax-exempt entity (including the organization itself)
- Expense = direct and indirect cost of qualifying studies
- Expense ≠ total research expense minus industry funding

Opportunities:
- Assure all studies funded by a tax-exempt source (and on the books of the organization) have been identified
- Base indirect costs on NIH guidelines and not necessarily the actual, indirect cost factor negotiated between the organization and NIH
- Consider which entity (EIN) should bear the cost of research studies
Schedule H, Part I, Line 7

```
<table>
<thead>
<tr>
<th>Financial Assistance and Certain Other Community Benefits at Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Assistance at cost from Worksheet 1</td>
</tr>
<tr>
<td>Medicaid from Worksheet 3, column a</td>
</tr>
<tr>
<td>Direct other means-tested government programs from Worksheet 3, column b</td>
</tr>
<tr>
<td>Total Financial Assistance and Means-Tested Government Programs</td>
</tr>
<tr>
<td>Other Benefits</td>
</tr>
<tr>
<td>Community health improvement services and community benefit operations (from Worksheet 4)</td>
</tr>
<tr>
<td>Health professions education (from Worksheet 5)</td>
</tr>
<tr>
<td>Subsidized health services (from Worksheet 6)</td>
</tr>
<tr>
<td>Cash and in-kind contributions (from Worksheet 7)</td>
</tr>
<tr>
<td>Total, Other Benefits</td>
</tr>
<tr>
<td>Total, add lines 7d and 7j</td>
</tr>
</tbody>
</table>
```

Line 7i - Cash and In-Kind Contributions

- “Cash and in-kind contributions” means contributions made by the organization to health care organizations and other community groups that are **restricted, in writing**, to one or more of the community benefit activities described in the Table in Part I, line 7 (or the Worksheets thereto).
Line 7i - Cash and In-Kind Contributions

- Do not report:
  - cash or in-kind contributions contributed by employees
  - emergency funds provided by the organization to employees;
  - loans, advances, or contributions to the capital of another organization; or
  - unrestricted grants or gifts to another organization

Line 7i - Cash and In-Kind Contributions

- New instruction for Part I, Line 7i (Tax Year 2012):
  Do not report as cash or in-kind contributions any payments that the organization makes in exchange for a service, facility, or product, or that the organization makes primarily to obtain an economic or physical benefit; for example, payments made in lieu of taxes that the organization makes to prevent or forestall local or state property tax assessments, and a teaching hospital's payments to its affiliated medical school for intern or resident supervision services by the school’s faculty members.
Worksheet 8: Cash and In-Kind Contributions

Issues and Opportunities: Cash and In-Kind Contributions

**Issues:**
- Place restrictions *in writing* on cash contributions *for community benefit*
- Describe unrestricted donations/sponsorships in Part VI
- Value in-kind donations based on “book value” (GAAP)
- Only report amounts not involving a *quid pro quo*

**Opportunities:**
- Track time spent by staff supporting community benefit activities
- Assure that all contributions being made by the system and its affiliates are accounted for as expense by the hospital organization(s)
### Frequent Issues

- Assuring interim data = year-end results
- Adjusting ratio of patient care cost to charges (and cost accounting-based expenses)
- Over-reporting costs associated with precepting nursing and other students
- Assuring “physician clinic” costs are reported appropriately
- Subtracting Medicare revenues and expenses reported in Part I, Line 7 from amounts reported in Part III
- Placing restrictions on cash contributions

### Frequent Opportunities

- Applying techniques to increase financial assistance (charity care) reported, within instructions and GAAP
- Including Medicaid provider taxes
- Reporting all community health improvement services and community benefit operations expenses (e.g., Medicaid-eligibility work and system-office costs)
- Including indirect costs
- Omitting health professions education costs for allied health professions programs
- Not reporting subsidized health services
- Full accounting of qualifying research studies
- Assuring hospital organization makes contributions, rather than non-hospital affiliates