Allocating bad debt and charity care to better meet IRS Form 990 Schedule H compliance
Introduction: What is IRS 990 Schedule H?

In December 2007, the Internal Revenue Service revised IRS Form 990, the form that all tax-exempt organizations, including hospitals, are required to file in order to maintain their federal tax-exempt status. In turn, state and local tax-exemption status for income, sales and property tax exemptions could also be challenged. This is the first revision to Form 990 in almost 30 years. The changes will require all tax-exempt organizations to report more detailed information about their organization and their activities.

The changes to IRS Form 990 are designed to increase transparency for all organizations that receive tax-exempt status. Non-profit hospitals in particular have been under increasing scrutiny in the past few years, for issues such as how they collect from patients, what fees they charge uninsured patients and established health plans, as well as executive compensation.

IRS Form 990 includes 16 schedules; Schedule H applies specifically to non-profit hospitals. Schedule H will require that hospitals separately classify their spending for charity care and bad debt, as well as how much of their activities should be considered as community benefit. The new schedule will be phased in for the 2008 tax year, but the entire Schedule H will need to be completed for tax years beginning in 2009.

Meeting compliance with these new requirements will be a challenge for many hospitals. Perhaps the most challenging aspect is the requirement that healthcare providers must properly allocate bad debt and charity care, as well as maintain efficient, detailed reporting on bad debt and charity care provided. This will require time and resources that many hospitals simply don’t have.

Some hospitals may have to hire additional staff whose only responsibility is managing reporting and compliance for IRS Form 990. The cost of additional staff and time would be most substantial in the first two years of reporting, as this will be the first time many hospitals are compiling and contributing this information.

This white paper explores the main challenges hospitals may face in reporting requirements for IRS Form 990 Schedule H and details five best practices that can help these facilities better prepare to meet their compliance obligations.
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New regulations require more detailed reporting of bad debt and charity care

The new requirements of IRS Form 990 Schedule H will increase transparency for hospitals, allowing the public to see the community benefit in terms of dollars and cents provided by tax-exempt hospitals, including charity care, education, immunizations, etc.

IRS Form 990 Schedule H includes five parts that require hospitals to provide information regarding:

- **Community Benefit Report**: Detailed information on charity care, means-tested government programs, research, training and education, and other activities that promote the health of the communities the hospital services.

- **Billing and Collections**: Summary of Medicare and other billing revenue information by patient category and an explanation of how the hospital calculates bad debt.

- **Management Companies and Joint Ventures**: Provide the name of entity, description, ownership percentages, executives and physicians.

- **General Information**: Includes narrative information about the hospital’s assessment of community needs, patient intake processes, emergency room policies and other information important to its tax-exempt purposes as a non-profit organization.

- **Facility Information**: Provide a list of facilities by name, address, type of service provided, and activities and programs.

Schedule H will be phased in for tax year 2008 (returns filed in 2009), with a transition period for certain requirements. The portion of new requirements non-profit hospitals must complete for tax year 2008 includes a list of facilities, types of services offered and activities and programs conducted at each location.

For the 2009 tax year, hospitals must collect and analyze data regarding their community benefit activities and the charity care they provide, and determine the value of both according to standards adopted by the IRS.

In short, hospitals will need to demonstrate a dollar amount for services they provide that never resulted in revenue. In order to do this effectively, hospitals must have the ability to:

- Identify patients who are unable to pay
- Capture public aid reimbursement shortfalls
- Distinguish charity care from bad debt

In 2010, these providers must provide detailed disclosure of their bad debt collections and policies.
In particular, hospitals may face significant expenses related to upgrading or adapting current processes in order to ensure that they can properly allocate bad debt and charity care to their appropriate accounts, as well as prepare the necessary reporting to meet the new requirements.

The top five common challenges that will make it difficult for hospitals to efficiently meet compliance with the new regulations are:

1. **Subjectivity and external data deficiency**
Hospitals that lack up-to-date decision data, analytics and externally validated data may not have the resources necessary to make more objective decisions regarding program eligibility for charity care or other financial assistance.

   For example, patients are often discharged prior to completing an interview or signing a charity application. Systems that are able to calculate Federal Poverty Level (FPL) percentages and validate against the hospital’s charity care policy can objectively report on patient populations that are not compliant with the charity interview process. Also, validating patient financial data against external data sources can add a confidence level to the up-front eligibility process and simplify the back-end recertification process.

2. **Operational inefficiency**
Many hospitals lack staff or efficient administrative processes, which can result in time and effort wasted to manually check self-reported patient data. An inability to verify accurate patient identity, address and financial information up front leads to staff reprocessing administrative tasks on the back-end. Patients move, change jobs or sometimes try to use fraudulent identity documents in medical identity theft. Hospitals also need a way to quickly and accurately authenticate patient information for IRS 990 segmentation and to help meet compliance with the Red Flag Regulations.

3. **Segmentation of bad debt and charity care.**
Hospitals that do not segment patient accounts through a defendable, objective methodology may have difficulty verifying whether their patient program eligibility data is valid for reporting and monitoring purposes. The myriad of public assistance programs, sliding discounts and granting charity care must be coordinated when considering a patient’s financing options. Bad debt accounts must also be compared continuously against a provider’s own charity care and against public assistance eligibility to make sure that accounts are segmented appropriately into the right payment programs. See Case Study 1 on the next page for how one healthcare system assessed the accuracy of their segmentation process.

Preparation to meet compliance with IRS Form 990 Schedule H will be a costly endeavor for many hospitals. It may require the hiring of additional staff whose only function is compliance. Or, it may require already over-burdened staff to take on extra responsibilities to meet compliance requirements.
4. Reporting Issues
Numerous regulatory mandates and strict scrutiny of claims make it difficult, if not impossible, for hospital staff to keep up with all of the requirements for maintaining tax-exempt status on the state, local and federal level. Complying with Schedule H will require even more diligent and accurate reporting, making it critical for hospitals to have efficient and effective tools in place for accurate reporting.

5. Qualify and recertify patient eligibility for charity care
Many hospitals struggle with an inability to qualify patients for eligibility initially and then recertify charity care status at the next visit or for annual renewal. Lack of a timely, accurate recertification process may make it difficult for staff to identify patients who are still deserving of charity care versus those who no longer qualify. This will become imperative for compliance and accurate reporting with IRS Form 990 Schedule H.

Case Study 1

North Shore/Long Island Jewish
5,965 bed system with 15 hospitals
New York

This multi-hospital system serving many counties needed to assess the validity of their initial eligibility assessments for their charity program and bad debt accounts for an upcoming external audit. They used a manual process to enroll patients in either its charity or self-pay discount program.

An automated analysis of a sample of the hospital’s patient file revealed that:

- 93% of charity patients were accurately classified
- 85% of the self-pay, uninsured and insured accounts actually qualified for either public aid or charity care
- 15% of their self-pay, uninsured and insured accounts had the ability to pay
- 39% of patient accounts had identification errors, such as incorrect addresses or Social Security numbers, which could result in returned mail processing and claim denials

North Shore/Long Island Jewish gained confidence that their program was working efficiently as designed and that they were properly prepared for the upcoming audit.
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Best practices for preparing to comply with IRS Form 990 Schedule H

Hospitals can take five steps to better allocate bad debt and charity care to meet compliance with IRS Form 990 and increase cash flow in their revenue cycle.

1. Prepare year-round.
   Hospitals should take steps to properly account for charity care throughout the year, rather than waiting until year-end. By accounting for how many patients actually received charity care periodically—even quarterly—rather than performing a rushed review at tax time along with many other pressing year-end needs—hospitals can ensure that their records are more complete and more accurate.

2. Report charity care in costs versus charges.
   To do this effectively, hospitals should have a revenue cycle that can calculate charity care both in costs and charges. An automated revenue cycle solution can provide the reporting capabilities hospitals need to correctly identify and track charity care patients—whether the charity is a discount or complete cost write-off—throughout their treatments.

3. Assess your charity care policy.
   It’s important for hospitals to evaluate their patient mix and adjust policies to fit any changes. For example, a hospital that has a higher population of underinsured and uninsured patients would need to re-evaluate their charity care policy to ensure that eligible patients are matched with appropriate sources of financial assistance. Hospitals that use a sliding scale distribution based on Federal Poverty Level (FPL) guidelines should examine whether their charity care policies are working based on their actual patient population.

   For example, one facility initially set its charity care write-off at 100% FPL; but after a review of their actual patient mix and payment history, administrators increased eligibility to 200% FPL, which allowed more patients to receive the financial assistance they deserved.

4. Track and measure results.

5. Consider an automated revenue cycle solution.
4. **Track and measure results.**

Hospitals should establish measureable goals to ensure that their charity care reporting processes are meeting compliance with IRS Form 990 as well as the hospital’s patient population mix. Setting a specific number of goals will help keep the focus on the high-priority tasks, helping to ensure that a hospital’s processes can be measured more effectively.

5. **Consider an automated revenue cycle solution.**

To meet legal compliance efficiently, as well as improve accounts receivables management, many hospitals are turning to a revenue cycle solution. This solution automates the process of determining whether a patient is eligible for charity care or other financial assistance, which can help hospitals better prepare for IRS Form 990 Schedule H and free up staff time for compliance issues.

It can also help hospitals:

- Reduce bad debt through improved collections at the time of service and on the back-end of the revenue cycle and reduce the cost of collecting overall.
- Improve cash flow from both self-pay patients and self-pay after insurance patients with deductible and co-pay balances.
- Review charity write-offs to determine whether those given charity care meet the provider’s charity criteria/policy.
- Improve processes and associated cost savings in both the charity interview and public assistance interview such as Medicaid or SCHIPs.
- Validate patient identity information to decrease technical denials, returned mail and to comply with FACTA Red Flag Regulations.

**Case Study 2**

In a recent analysis using an automated revenue cycle solution on a sample file, one hospital was able to identify that:

- **31% of the hospital’s total population did not have the correct name, address or Social Security information on file**

  The hospital learned that by simply asking the patient a few additional questions, the registrar could greatly improve the quality of patient information within the system. The benefits of the improved patient information will flow down to other areas of the revenue cycle, i.e., reduction in returned mail processing and more efficient post-discharge collection efforts.

- **75% of its population could have qualified for Medicaid or charity assistance**

  By alerting a financial counselor to this information, the counselor can fast-track eligible patients for interviews and have them enrolled in these programs, enhancing the hospital’s community commitment and greatly improving Medicaid reimbursement.
Allocating bad debt and charity care with greater confidence to better meet IRS Form 990 Schedule H compliance

While there are five parts to IRS Form 990 Schedule H, many non-profit hospitals may face the most difficulty with two key parts: preparing an accurate accounting for both the community benefit report section and the billing and collections section.

To meet compliance with these two sections in particular, non-profit hospitals must be able to distinguish bad debt and charity care quickly and efficiently. They must also be able to provide comprehensive and timely reports on the charity care that they provide. Hospitals that cannot perform these two functions could lose their tax-exempt status and support from the community it serves.

To overcome any challenges associated with meeting compliance, hospitals should: prepare reporting year-round; report charity care in terms of costs versus charges; periodically assess charity care policies; track and measure results; and consider implementation of an automated revenue cycle solution.

With these measures in place, hospitals can be better prepared for managing compliance with IRS Form 990 Schedule H. This will help provide the necessary documentation to support their tax-exempt status, offer greater transparency and unprecedented information about their charity care activities to the community and help ensure that the information they report is based on objective, validated information that is more up-to-date and accurate.
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