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Nonprofit Hospitals' Provision of Charity Care: Is it Commensurate with the Value of their Tax Exemption

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Protecting Health, Saving Lives—*Millions at a Time*

Acknowledgements

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Study Objectives

- We compare the amount of charity care that nonprofit hospitals report to (IRS) and the (CMS).
- We explore the variation of the reporting of charity care across nonprofit hospitals.
- We compute the value of their tax-exemption.
- We compare their provision of charity care to the value of their tax-exemption.

Back to the Future

United States General Accounting Office

GAO

Report to the Chairman, Select Committee on Aging, House of Representatives

May 1990

NONPROFIT HOSPITALS

Better Standards Needed for Tax Exemption

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Background

- Why are nonprofit hospitals exempt from taxes?
- IRS grants them exemption from federal taxes under 501(c)3, hospitals are organized for a charitable purpose.
- What is hospital charity?
- Community benefit standard.

Why is this an issue?

- Health care and hospitals are big business.
- Hospitals are located on prime real estate and do not pay state and local property, income or sales taxes.
- Governments are looking for revenue sources.
- Uninsured and under-insured persons need care.

What is hospital charity?

The IRS defines community benefits

- the charity care;
- unreimbursed costs from Medicaid and other public means-tested programs;
- community health promotion and health education services;
- subsidized medical services,
- research,
- community advocacy, and community building activities;
- health professional education; and
- cash and in-kind contributions to community-based organizations.

Measuring Hospital Charity Care

- Uncompensated care had been the default measure.
- Hospitals had no incentive to distinguish between mission accomplishment and financial failure.
- Primary Data Source AHA Annual Survey of Hospitals, or financial data collected by state governments.

An Incentive for Quality Data

- IRS Hospital Compliant Program in 2009. Hospital report community benefits on Form 990 Schedule H
- CMS revised calculation for subsidies under Medicare DSH and Medicare Electronic Health Record Incentive Programs. Hospitals required to report charity under Medicare Cost Report Form 2552 Worksheet S-10

Affordable Care Act

- The ACA established new requirements for nonprofit hospitals to maintain their tax-exempt status.
- The ACA clarify how nonprofits hospitals should provide charity care.
- Nonprofit hospitals are required to establish a financial assistance policy (FAP). The FAP must 1) identify which patients are eligible for charity care, i.e., free or discounted care, 2) outline the application process for obtain charity care, and 3) state the consequences for nonpayment.

Affordable Care Act

- Nonprofit hospitals must publicize their FAP to the public.
- Nonprofit hospitals were prohibited from charging patients eligible for financial assistance more than their insured patients
- The ACA also specified restrictions on billings and collections. Nonprofit hospitals must make a reasonable effort to determine if patients are eligible for the FAP before initiating extraordinary collection procedures.
- These requirements went into effect in the tax year after the enactment of the ACA on March 23, 2010.

New Data Charity Data

We want to compare charity nonprofits reported to the IRS to the amounts reported to CMS, for the year 2011 and 2012.

- IRS Form 990 Schedule H obtained from Guidestar
- CMS 2552 S-10 data obtain from CMS website

IRS Charity

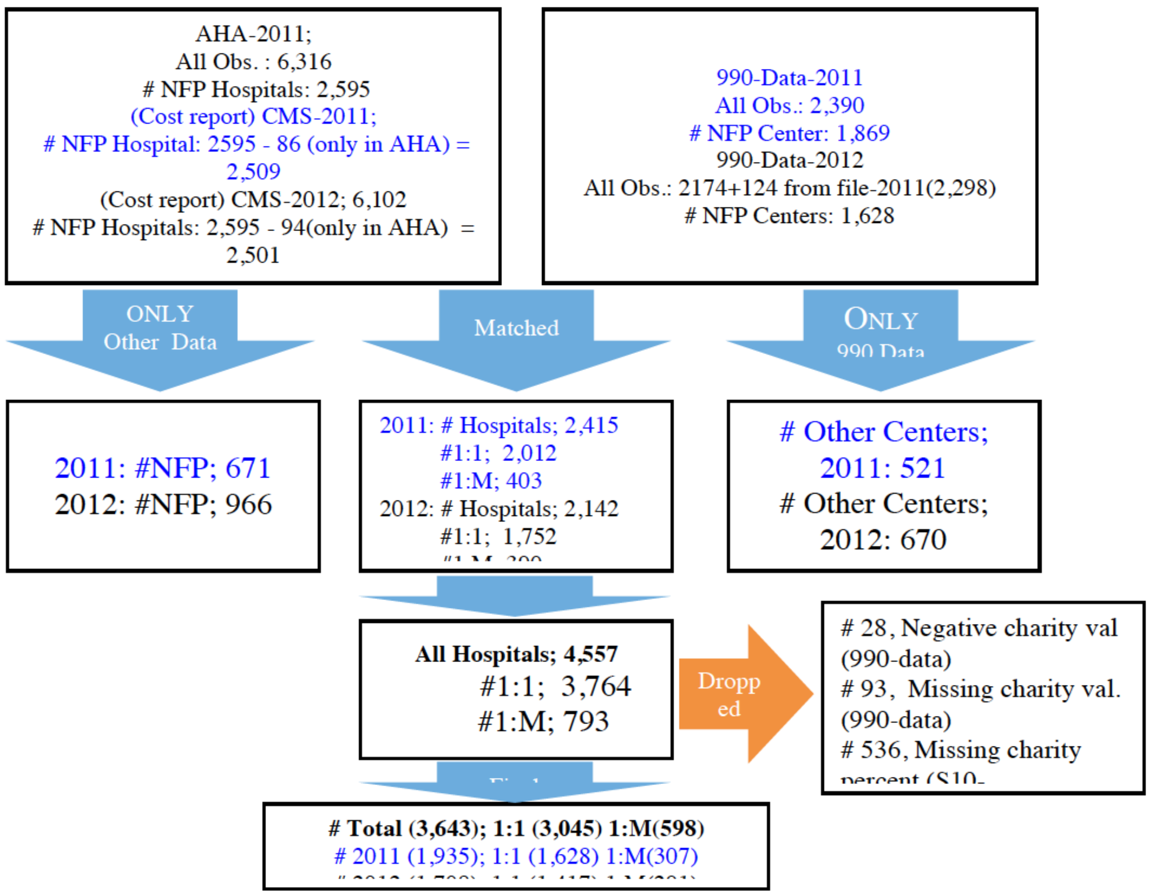
The IRS Form 990 defines charity as - “free or discounted health services provided to persons who meet the organization's criteria for financial assistance and are unable to pay for all or a portion of the services. [Charity care] does not include: bad debt or uncollectible charges that the organization recorded as revenue but wrote off due to a patient's failure to pay, or the cost of providing such care to such patients; the difference between the cost of care provided under Medicaid or other means-tested government programs or under Medicare and the revenue derived there from; or contractual adjustments with any third-party payers”.

CMS Charity

CMS 2552-10 Worksheet S-10 defines charity care is defined as - “health services for which a hospital demonstrates that the patient is unable to pay. Charity care results from a hospital’s policy to provide all or a portion of services free of charge to patients who meet certain financial criteria…” This does not include non-Medicare bad debt and non-allowable Medicare bad debt. Non-Medicare bad debt is for “those health services for which a hospital determines the non-Medicare patient has the financial capacity to pay, but the non-Medicare patient is unwilling to settle the claim.” “Non-allowable Medicare bad debt is the “amount of allowable Medicare coinsurance and deductibles considered to be uncollectible but are not reimbursed by Medicare”.

Creating a crosswalk between 990 and S-10 Data

Figure 1. Outcome from Merging IRS, AHA and CMS Hospital Data



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Findings

- Over the two-year period, nonprofit hospitals reported $20.66 billion in charity care to the IRS and $18.71 billion in charity care to CMS.
- In 2012, the average nonprofit hospital reported $537,000 more in charity care to the IRS than to CMS.
- Paired t-tests show that hospitals reported the different amounts to the IRS (2.54%) and CMS (2.36%). However, there does not seem to be a systematic over or under reporting by any particular hospital subcategory.
- Hospitals reported the same amount of charity care to the IRS and CMS during the two-year study period only about 1.2% of the time (44 observations).
- While there is certainly a strong correlation between the IRS 990 data and the CMS S-10 data, there are many hospitals with very different amounts.

Figure 2: Comparing Diff AMT ($1,000,000) & Diff % of Charity Cost between S10 and 990-Data

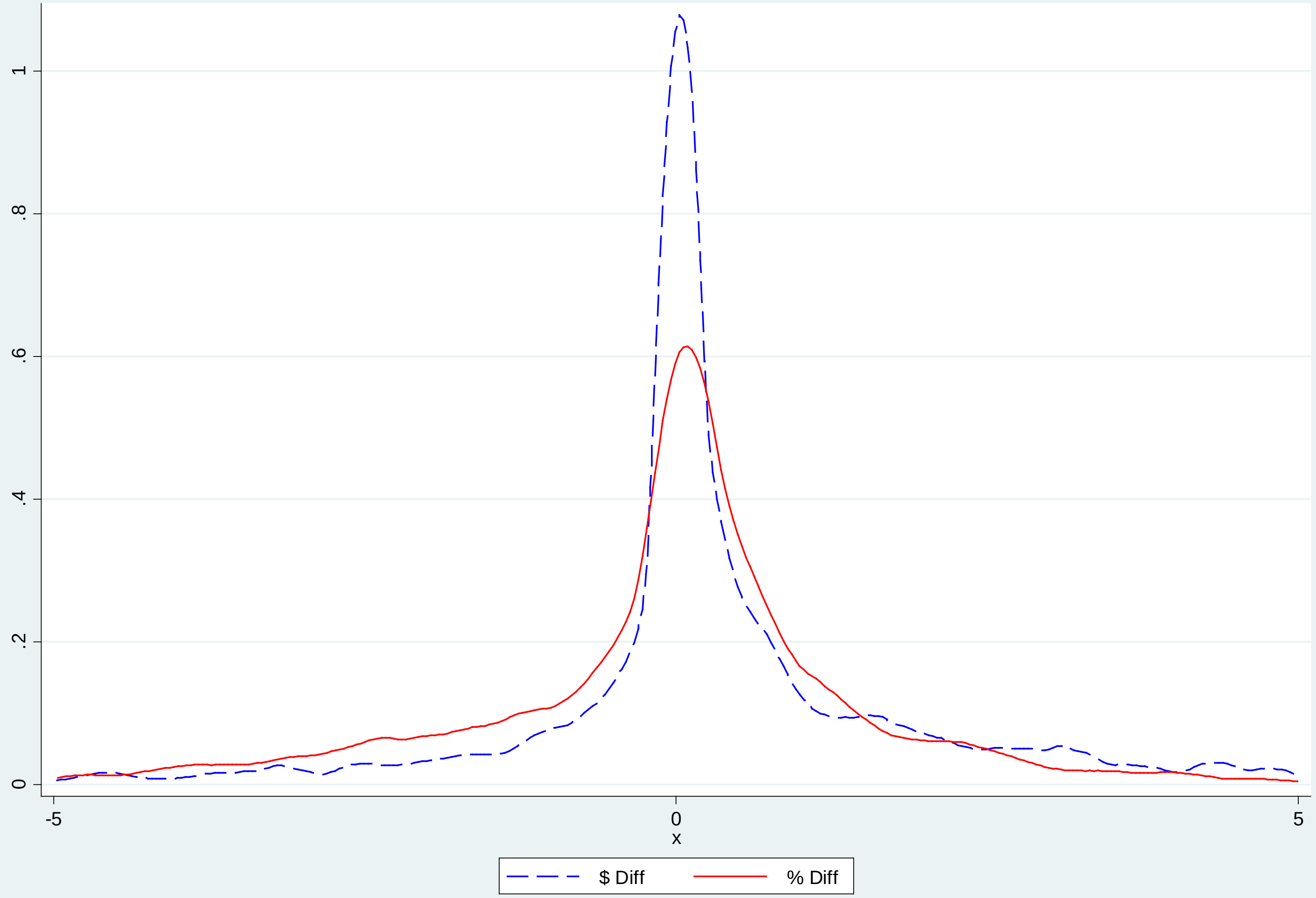
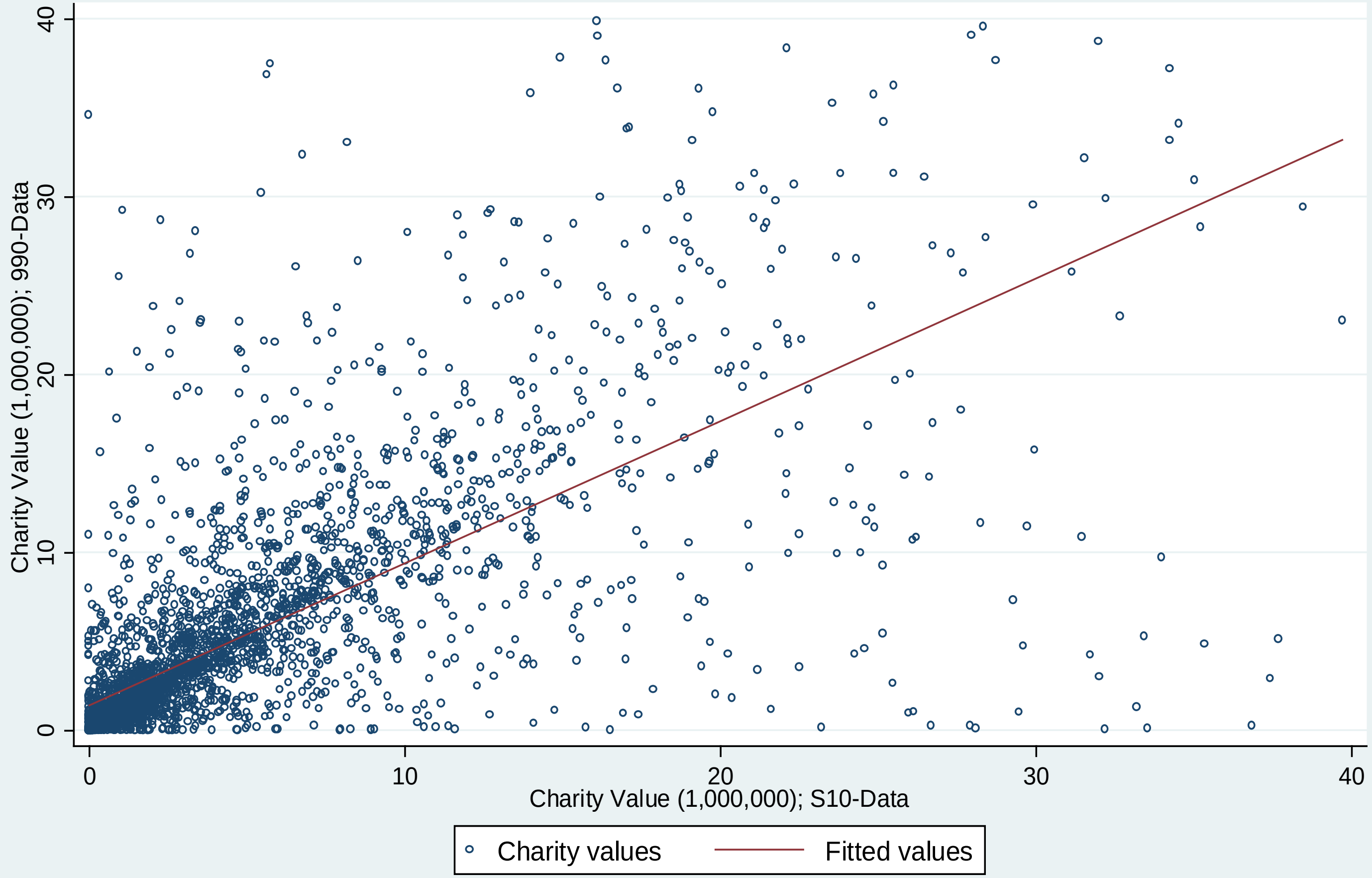
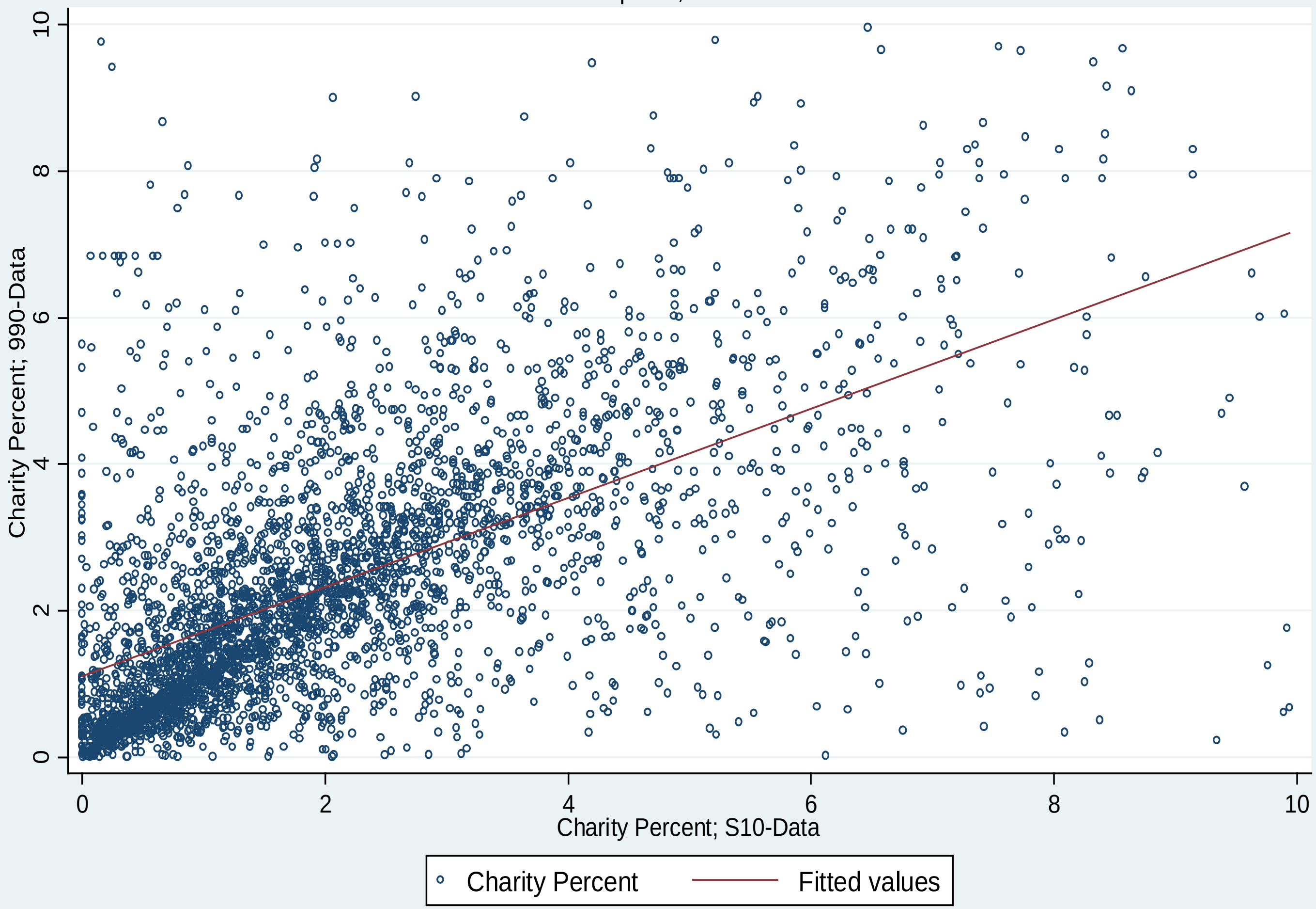


Figure 3: Scatter Plot of the Amounts Reported for Charity Care in the S10 and 990 Data for nonprofit Hospitals, 2011-2012



Sources: 990-Data, S10 Data
Obs>40 dropped for plotting

Figure 4: Scatter plot of the Percent Reported Reported for Charity Care in the S10 and 990 Data for nonprofit Hospitals, 2011-2012



Sources: 990-Data, S10 Data
Obs >10 dropped for plotting

Factors Influencing Differences in Charity Care Reported

- We used a regression analysis to compare the difference in the percent of charity reported to the IRS compared to CMS. We found that hospital and market characteristics were not predictors of the difference in reporting (R^2 = 0.037).

Maybe the differences are errors in reporting

- Are certain categories of hospitals more likely to make report differences?
- We used GLM estimation with a log-link and gamma distribution to control for the skewedness in the dependent variable.
- (See Table 4.)

Differences were related to hospitals and market characteristics

- Larger hospitals, teaching hospitals, members of hospital systems, hospitals that provided safety net services, hospitals in counties with higher percentage of minority residents, counties with a FQHC and those located in highly competitive hospital markets had larger reporting absolute differences.
- Hospitals that served more Medicaid patients, non-church operated, specialty hospitals, contract managed hospitals, rural hospitals, hospitals located in markets with a public hospital, higher percentages of uninsured residents, higher HMO penetration rate, and low and moderate health insurance competition had lower reporting differences.

Estimating the Value of Tax Exempt Status

- We next computed the estimated value of tax exemption for nonprofit hospitals by simulating the amount of taxes hospitals would have paid federal and state governments on their net income, and the hospitals’ lower interest rates paid because their bondholders do not pay taxes on their interest income.

Value of the Tax Exemption

- Over the two-year period, the total value of the tax exemption was $30.95 billion with $18.5 billion from federal income taxes (59.8% of the total), $2.4 billion from state income taxes (7.8%) and $9.98 billion for tax-exempt bonds (32.3%).

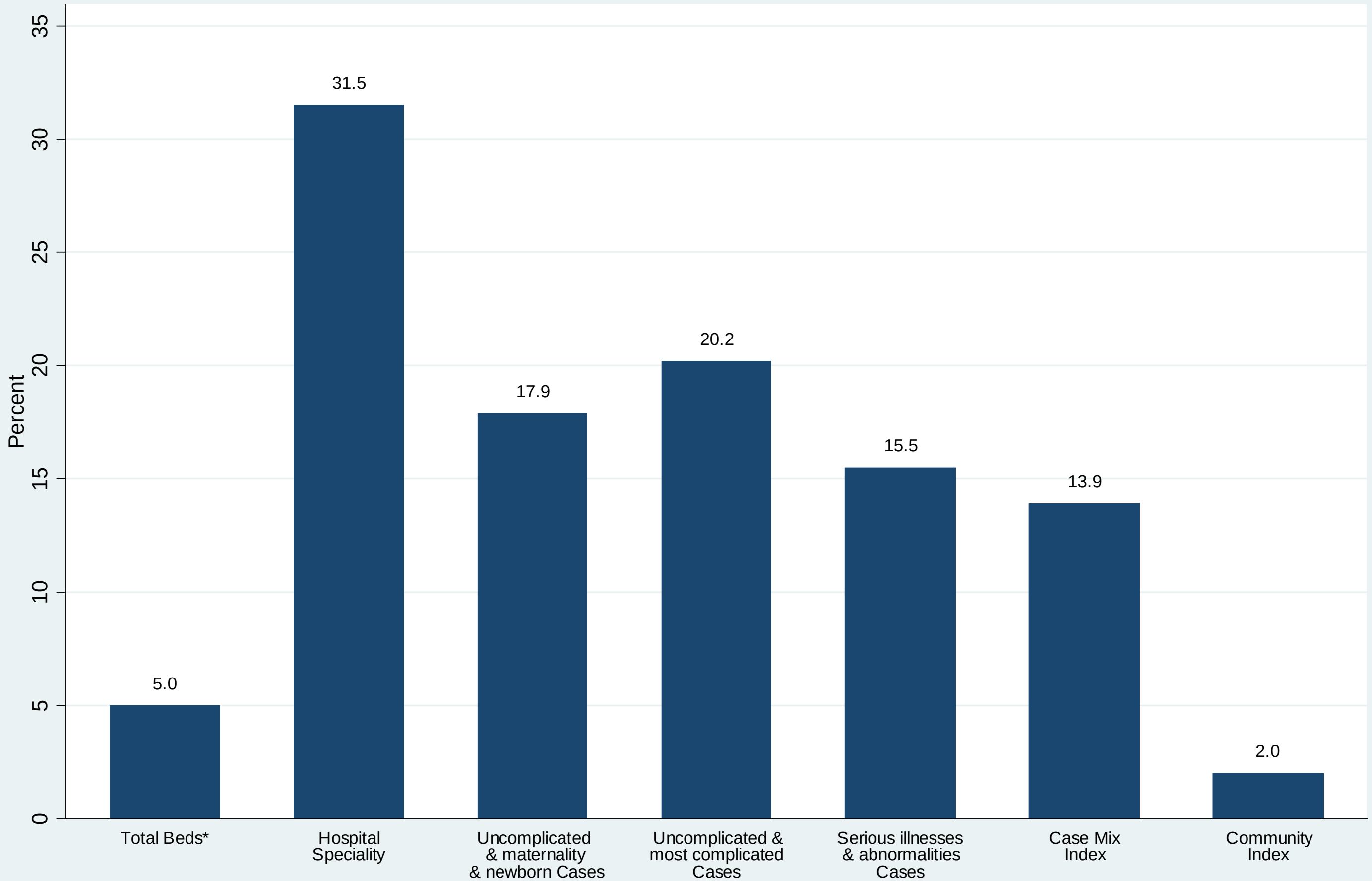
Tax exemption greater that charity care value

- This $30.95 total value of the tax exemption to nonprofit hospitals was 50% greater than the total value of charity care reported to the IRS ($20.66 billion) and 65% greater than the value of charity care reported to CMS ($18.70 billion) during the two-year period.

Distribution of the value of the tax exemption

- 75% of nonprofit hospitals benefited from the federal corporate income tax exemption (as 25% of hospitals reported no positive net income),
- 61% benefited from the state corporate income tax exemption (as some hospitals are in states with no state corporate income taxes),
- 54% benefited from tax-exempt bonds financing.
- Consequently 87% of nonprofit hospitals received a benefit from the tax exemption.

Figure 5. Factors that Predict Positive Value of Tax Exemption in NFP Hospitals, 2011-2012



* This is for 100 units change in bed.
Details for other variables used at the GLM model for Tax-value reported at the Tab 6 (Model without dummy for states)

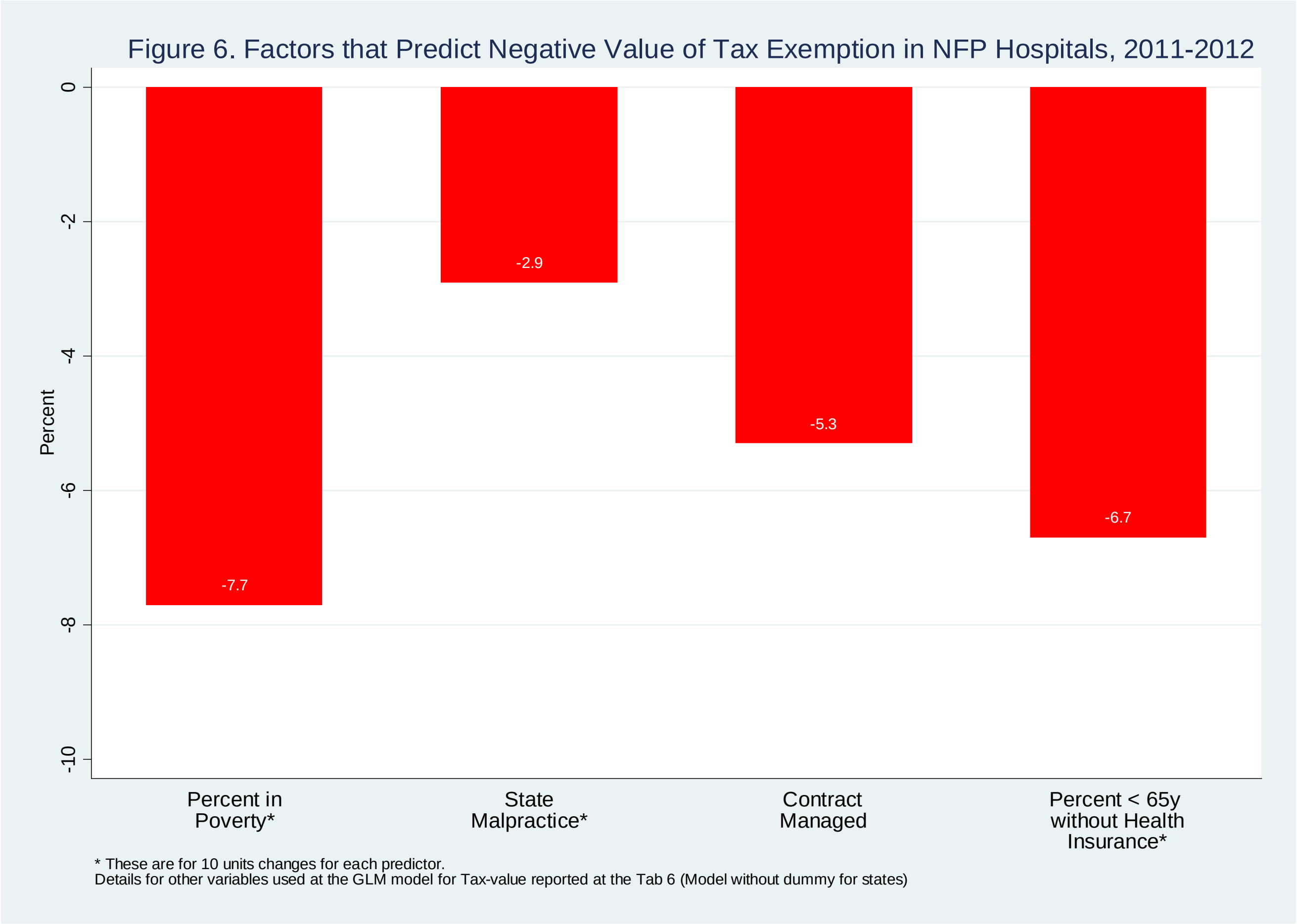


Figure 6. Factors that Predict Negative Value of Tax Exemption in NFP Hospitals, 2011-2012
Percent
0
-2
-4
-6
-8
-10
-7.7
-2.9
-5.3
-6.7
Percent in Poverty*
State Malpractice*
Contract Managed
Percent < 65y without Health Insurance*
* These are for 10 units changes for each predictor.
Details for other variables used at the GLM model for Tax-value reported at the Tab 6 (Model without dummy for states)

Is the value of the tax exemption correlated with charity care? NO

OLS Model	Without State and Market Level		Without State Fixed Effects		With State Fixed Effects	
	A	B	C	D	E	F
	% Charity-990	% Charity-S10	% Charity-990	% Charity-S10	% Charity-990	% Charity-S10
% Total-Estimated-Tax/Tot-Rev	-0.0007	0.0006	-0.0004	0.0008	-0.0006	0.0008
	(0.0004)	(0.0006)	(0.0004)	(0.0006)	(0.0004)	(0.0006)
	G	H	I	J	K	L
GLM Model	Log Charity Value-990	Log Charity Value-S10	Log Charity Value-990	Log Charity Value-990	Log Charity val -990	Log Charity val-S10
Log Total Estimated Tax	-0.0005	-0.001	0.00001	-0.0001	0.0003	0.0002
	(0.0003)	(0.0006)	(0.0003)	(0.0006)	(0.0003)	(0.0006)

Sources: 990, Cost Report: 2011 & 2012, AHA:2011

Note:

1) Models included other hospital characteristics, market level factors and state fixed effects.

Identifying Net Contributors and Net Recipients

- We next computed the net charitable contribution for each hospital as IRS charity care minus the estimated value of the tax-exemption.
- We divided the hospitals into four groups:
  1. Hospitals with net charitable contribution of less than -$12.21 million (i.e., the bottom 10^{th} percentile),
  2. between -$12.21 million and $0 million,
  3. between $0 and $5.15 million
  4. and above $5.15 million (i.e., the top 90^{th} percentile).

Identifying Net Contributors and Net Recipients

- We examined the likelihood of being in either tail of the distribution relative to having a modest positive charitable contribution, i.e., from $0 to $5.15 million by estimating two logistic regression models to identify characteristics of hospitals that were net contributors and net recipients.

Predictors of Net Contributors

- Hospitals that served complicated maternity cases and hospitals designated as regional and major trauma centers and hospitals that provided community oriented services were more likely to be large net contributors.
- Hospitals with higher cost per admission and located in counties with higher percentage of Blacks residents and with an FQHC were more likely to be large net contributors.
- Small hospitals, contract managed hospitals, and rural hospitals were less likely to be large net contributors.
- Hospitals in states with higher malpractice payments and those in counties with a public hospital were less likely to be large net contributors.

Predictors of Net Recipients

- Very large hospitals (>500 beds), specialty hospitals, hospitals that use hospitalists, and hospitals that provide obstetric care for complicated cases were more likely to be net recipients.
- The odds of being a net recipient increased with hospital costs per adjusted admission and case mix.
- Small and medium size hospitals (<200 beds), contract managed hospitals, hospitals serving more Medicaid patients, rural hospitals, hospitals with trauma units, and sole community providers were less likely to be low net contributors.
- Hospitals in county with higher percentages of Black residents and uninsured residents and hospitals in states with higher malpractice payments were less likely to be net recipients.

Limitations

- We don’t give hospital credit for other elements of community benefits.
- We don’t include other tax benefits (property, sales, and charitable gifts).
- Typical problems with hospital based analysis regarding defining the relevant geographic markets.

What does this mean?

- Nonprofit hospitals routinely report different amount of charity to IRS and CMS.
- Nonprofit hospitals probably don't provide charity care commensurate with the value of the tax exemption.
- Congress should value other elements of community benefits
- Tax exemption is a blunt instrument.
- ACA is a good start, but better standards are needed.

Questions?

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