



**hfma**

healthcare financial management association

June 3, 2005

The Honorable Bill Thomas  
Chairman, House Committee on Ways and Means  
United States House of Representatives  
Washington, DC 20515-2216

Dear Mr. Chairman:

The Healthcare Financial Management Association (HFMA) is pleased to submit comments for the record of the May 26, 2005 hearing, "A Review of the Tax-Exempt Hospital Sector."

### **About HFMA**

HFMA is the nation's leading membership organization for more than 34,000 healthcare financial management professionals. Our members are widely diverse, employed by hospitals, integrated delivery systems, managed care organizations, ambulatory and long-term care facilities, physician practices, accounting and consulting firms, and insurance companies. Members' positions include chief executive officer, chief financial officer, controller, patient accounts manager, accountant, and consultant.

HFMA is a nonpartisan professional practice organization. As part of its education, information, and professional development services, HFMA develops and promotes ethical, high-quality healthcare finance practices. HFMA works with a broad cross-section of stakeholders to improve the healthcare industry by identifying and bridging gaps in knowledge, best practices, and standards. For the purposes of this statement, the most relevant examples of these activities are:

- Attributes of tax-exempt status. In 1988, HFMA formed a chairman's task force to identify the specific attributes of healthcare providers that characterize them as tax-exempt institutions. That report was published in 1991. (See [http://www.hfma.org/resource/focus\\_areas/business\\_of\\_hc/articles/02\\_21\\_02.htm](http://www.hfma.org/resource/focus_areas/business_of_hc/articles/02_21_02.htm))

These findings were recently incorporated into HFMA's Principles and Practices Board 2005 monograph: *Issue Analysis 05-01: The Relationship of Community Benefit to Hospital Tax-Exempt Status*, which seeks to clarify ways in which hospitals

can gather and report the information needed to demonstrate their fulfillment of their charitable mission.

- Quantifying bad debt and charity care. In 1993, HFMA published Principles and Practices (P&P) Board Statement 15, which explains how to distinguish between charity care and bad debt. These statements are rigorously peer-reviewed to ensure they reflect the best thinking of the industry. The IRS has recommended adherence to P&P Board Statement No. 15 in all representations regarding charity care. (See [http://www.hfma.org/resource/P\\_and\\_P\\_board/Statement\\_15.htm](http://www.hfma.org/resource/P_and_P_board/Statement_15.htm))

Improving patient financial communications. HFMA leads the *PATIENT FRIENDLY BILLING* Project, a cross-disciplinary, nationwide initiative to make patient financial communications clear, concise, and correct. Five years ago, a Project work group began work on a report aimed at helping hospitals efficiently and effectively review their financial assistance policies to better serve the needs of their communities. The report, *Hospitals Share Insights to Improve Financial Policies for Uninsured and Underinsured Patients*, was published in January 2005. (See [http://www.patientfriendlybilling.org/2005report/2005\\_pfb\\_report.pdf](http://www.patientfriendlybilling.org/2005report/2005_pfb_report.pdf))

### **Summary Points of this Statement**

We would like to make the following points regarding the role of tax-exemption for hospitals, to be discussed in more depth following this summary:

- HFMA strongly urges the Committee to **consider the full range of community services deserving of tax-exemption**, not just charity care. Exempt hospitals are an important part of the healthcare delivery network and provide a wide variety of community services that fall under the IRS definition of “charitable” under Revenue Ruling 69-545.
- Because of this diversity of services, HFMA encourages the Committee to use **great caution when viewing research that compares amounts of charity care provided** by individual hospitals. Some hospitals that provide smaller amounts of charity care may instead devote their exempt resources to other important community services, such as trauma centers, neonatal intensive care units, and a host of other important needs not served by governments or for-profit organizations.
- HFMA asks the Committee to realize that **healthcare needs – including charity care needs – differ greatly by community**, and therefore solutions, whether legislated or voluntary, must be flexible to best serve the needs of the patients and communities they serve.
- In most aspects of daily operations—such as provision of optimal clinical care, effective operations, and business efficiency—a **hospital’s ownership type should be transparent to the patient**. Indeed, not-for-profit entities have an obligation to

operate as efficiently and effectively as possible to ensure the best possible cash flow, which, in turn allows them to fulfill their missions. Instead, the meaningful distinctions among ownership types are found in specific characteristics such as use of financial surpluses, accountability, and the provision of services.

- **Comparable, scaleable reporting standards** will greatly help tax-exempt hospitals accurately document and report the entire range of the community benefits provided. HFMA believes that these comprehensive reports should be communicated regularly and clearly to the public. We applaud the excellent work that the Catholic Health Association and VHA have done in this area.

### **The Role of Charity Care and Community Benefit in Justifying Tax-Exempt Status**

HFMA believes that while the provision of charity care is an important attribute of tax-exemption, it is only one of many attributes that warrant tax-exempt status, as the IRS defines “charitable” under IRC Section 501(c)(3) and Revenue Ruling 69-545. Failure to recognize the broad basis for tax-exemption could lead to a specific trade-off between the amount of charity care provided and the amount of tax-exemption allowed, which would undermine important and cumulative community benefits that tax-exempt healthcare institutions deliver.

Our members know that the problem of care for uninsured patients is far greater than healthcare providers can resolve alone. Even if each provider in the country devoted every exempt dollar to the delivery of charity care, there would still be a shortfall of funds to care for the uninsured, and furthermore, vital community services would have to be eliminated, ranging from trauma centers to boarder baby programs.

### **Attributes of Tax-Exempt Healthcare Providers**

Tax-exempt healthcare organizations are formed to address the specific needs of their communities; therefore, the attributes that merit tax-exemption are not standard across all institutions. In 1991, an HFMA Chairman's Task Force released a report identifying the major attributes of tax-exempt organizations. The P&P Board built on these attributes in light of the current environment.

For the purposes of the issues before this Committee, these attributes can be divided into organizational characteristics and types of services.

Organizational characteristics:

Mission to Provide Community Benefit. Mission is a cornerstone of granting tax-exemption. According to federal law, the tax-exempt provider must have a clearly defined mission statement committing the institution to charitable endeavors. Both the institution's historical background and the community's needs are important in determining the mission statement.

Use of Financial Surpluses. No individual may receive any portion of a tax-exempt institution's financial surpluses as a result of ownership. Both federal and state laws require that all financial surpluses must go toward furthering the organization's charitable purpose. Compensation arrangements must be carefully constructed to reflect fair market value for services rendered.

Accountability. The organization's board of trustees must hold itself answerable to its community for maximizing the entity's contribution to the community.

Goodwill. Goodwill is an intangible attribute characteristic of successful tax-exempt hospitals continuing their mission of providing care and meeting their community responsibility over a long period of time. Such organizations usually have stable ownership and governance structures and regularly receive significant philanthropic and volunteer support.

Types of charitable services:

Provision of Charity Care. Free or discounted care is an important component of many hospitals' tax-exempt missions, but is not the only function that hospitals perform to merit tax-exempt status. Organizations that provide charity care must establish and communicate a clear charity care policy based on community needs and input. The policy should include easy-to-understand, written eligibility criteria.

Reduction of Government Burden. Many tax-exempt hospitals provide services that government otherwise would have to provide. Services especially demanded from tax-exempt healthcare providers include high-tech, high-intensity services, emergency care, chronic care, long-term care, and unprofitable services.

Provision of Essential Healthcare Services. Tax-exempt healthcare providers are often the sole providers of healthcare services that are so essential to community health that tax-exempt status is warranted. Examples of essential services include emergency rooms and outpatient clinics serving low-income patients.

Provision of Unprofitable Services. The provision of unprofitable services is commonly a provider's charitable response to a community need. Unprofitable services in this sense lose money because of high costs combined with low volume or inadequate payment rather than inefficient operations. Common examples of unprofitable services include burn, neonatal, and trauma centers and community mental health centers.

Public Education. Teaching institutions, of course, are exempt because of their role in the advancement of education and science. Most tax-exempt healthcare providers, however, also provide a range of educational programs to enhance public health. Examples of such programs include public health education, wellness programs, and the sponsorship of educational activities.

Serving Other Unmet Human Needs. Some tax-exempt hospitals provide important services that are tangential to health care but that are unmet by any other entity in the service area. Examples of these activities include senior citizen education and outreach programs, care for "boarder" babies, or the operation of a "meals on wheels" program.

### **Documenting Community Benefit**

HFMA believes healthcare providers should identify, measure, and prominently disclose all the attributes of their organizations that warrant tax-exempt status. It is important that all stakeholders, from government officials to members of the provider's community, understand all the reasons why an organization qualifies for tax-exemption and the progress that is being made toward achieving its mission.

This can be accomplished effectively only with appropriate community benefit reporting standards that promote comparability and are still scaleable enough to accommodate the wide variation in provider size and resources that characterize the nation's exempt healthcare providers. HFMA applauds VHA Inc., the Catholic Health Association of the United States, and Lyon Software for their contribution in this area through the development of *Community Benefit Reporting: Guidelines and Standard Definitions for the Community Benefit Inventory for Social Accountability*.

### **Conclusion**

HFMA takes pride in its history of providing balanced, objective healthcare finance technical expertise to Congress, HHS, and advisory groups. We hope that these comments and recommendations are useful as the Ways and Means Committee pursues the best interests of patients, tax-payers, and the nation's healthcare system.

We are at your service to help your Committee gain a balanced perspective on this complex issue. If you have additional questions, you may reach me, or Richard Gundling, Vice President of HFMA's Washington, DC, office, at (202) 296-2920. The Association and I look forward to working with you.

Sincerely,



Richard L. Clarke, DHA, FHFMA  
President and Chief Executive Officer  
Healthcare Financial Management Association