

# Hot Topics for Tax-exempt Health Care Providers



Presented by  
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# Agenda

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- ✓ Redesigned Form 990
- ✓ IRS Compliance Initiatives
- ✓ Other New Developments



# Redesigned Form 990

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- ✓ Form 990 last revised in 1979
- ✓ Current Form 990
  - Illogical form design
  - Very complex
  - Nine-page core form, Schedules A & B and 36 possible attachments

# Redesigned Form 990

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- ✓ **IRS Guiding Principles**
  - Improve transparency
  - Improve compliance
  - Reduce burden



# Redesigned Form 990

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- ✓ 11-page Core Form
- ✓ 16 Potential Supplemental Schedules
- ✓ Required for 2008 Returns
- ✓ Per IRS, instructions to be released in Spring 2008



# Redesigned Form 990

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## ✓ IRS Initial Estimates

- Three of 15 schedules completed by > 25% of organizations
- Eight completed by < 10% of organizations

## ✓ Guess What?!

- Most health care organizations will be in minority
- Reduced burden??

# Redesigned Form 990 – Core Form

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- ✓ Part I – Summary
- ✓ Part III – Program Service Accomplishments
- ✓ Part IV – Checklist of Required Schedules
  - Questions are triggers for supplemental schedules
  - Trigger question for Schedule H revised from June 14 draft to read: “Did organization operate one or more hospitals?”
- ✓ Part V – Other IRS Filings



# Redesigned Form 990 – Core Form

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## ✓ Part VI – Governance Issues

- Information on composition of board & business relationships between board members
- Number of independent voting board members
- “Was copy of Form 990 provided to organization’s governing body before it was filed?”
- Written conflict of interest policy
- Whistleblower policy
- Document retention & destruction policy



# Redesigned Form 990 – Core Form

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## ✓ Part VII – Compensation Information

- Current officers, directors & key employees regardless of compensation
- Five highest-paid employees
- Former officers, directors & key employees if compensation exceeds thresholds
- Must use amounts reported on most recently filed Forms W-2 & 1099s
- June 14 draft indicated that organization's address may no longer be used; however, IRS has backed off this position



# Redesigned Form 990 – Core Form

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- ✓ Part VIII-X – Financial Information
- ✓ What should you do now?
  - Review program service accomplishments closely to paint an accurate picture of your organization on Part III
  - Review questions on Part IV to determine which supplemental schedules will be required for your organization



# Redesigned Form 990 – Core Form

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- ✓ What should you do now? (Cont'd)
  - Review questions on Part VI closely to determine if your organization should consider adopting any new policies
  - Review your compensation practices & procedures closely to accurately complete Part VII



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule A

- Required by all 501(c)(3) organizations
- Reason for Public Charity Status, Public Support Test
- Publicly supported organizations that do not meet 33 1/3 % public support test will be required to provide an explanation of how it meets 10 % facts & circumstances test



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule B

- Same as current requirements (\$5,000 or more from any one contributor)

## ✓ Schedule C

- Political campaign and lobbying activities
- Report lobbying portion of association dues



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule D

- All types of organizations
- Information on donor-advised funds
- Contains various financial statement attachments
- FIN 48 Footnote Disclosure
- Recommendations
  - Discuss FIN 48 with your BKD audit contact
  - Identify which sections of Schedule D will apply to your organization



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule H

- According to IRS, schedule's instructions will define hospital by reference to state licensing or certification
- Schedule H will be completed on an entity-by-entity basis
- Transition relief
  - Only Part V, Facility Information, will be required for 2008 returns
  - Remainder of Schedule required for 2009 returns



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule H (Cont'd)

- Billing information table has been removed
- Part I – Charity Care & Other Community Benefits at Cost
- Part II – Community Building Activities
- Part III – Bad Debt, Medicare & Collection Practices



# Redesigned Form 990 – Supplemental Schedules

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- ✓ **Schedule H (Cont'd)**
  - **Part IV – Management Companies & Joint Ventures**
  - **Part V – Facility Information**
  - **Part VI – Supplemental Information**



# Redesigned Form 990 – Supplemental Schedules

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- ✓ Schedule H – What should you do to be prepared?
  - Stay tuned for form instructions & worksheets
  - Review Schedule H closely & assess your current systems
  - Consider whether any new policies need to be adopted or committed to writing

# Redesigned Form 990 – Supplemental Schedules

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- ✓ Schedule H – What should you do to be prepared? (Cont'd)
  - Work with your marketing department to develop strong community benefit report & narrative information on community building activities
  - Review HFMA Statement 15 for guidance with respect to bad debts & charity classification
  - Consider reviewing Catholic Health Association's community benefit model



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule J

- Triggered by questions 3, 4 & 5 of Form 990, Part VII, most commonly if reportable compensation exceeds \$150,000
- Part I – Questions Regarding Compensation
- Part II – Compensation Information, prior three columns expanded to seven columns



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule K

- Supplemental information on tax-exempt bonds
- Transition relief
  - Only Part I, Bond Issues, will be required for 2008
  - Remainder of Schedule required for 2009
- Organizations not required to report information regarding bonds issued before 2003



# Redesigned Form 990 – Supplemental Schedules

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- ✓ Schedule K (Cont'd)
  - Recommendations
    - Closely review Schedule K & begin gathering information to report
    - Contact bond counsel with any significant issues discovered



# Redesigned Form 990 – Supplemental Schedules

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## ✓ Schedule L

- Information on excess benefit transactions, loans to or from interested persons and business transactions involving interested persons
- Required information expanded

## ✓ Schedule M

- Information on non-cash contributions



# Redesigned Form 990 – Supplemental Schedules

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- ✓ **Schedule O**
  - Supplemental Information to Form 990
- ✓ **Schedule R**
  - Information on related organizations, including disregarded entities, related tax-exempt organizations, partnerships & corporations
  - Expanded information on transfers between 501(c)(3) organizations & related noncharitable exempt organizations



# IRS Compliance Initiatives

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- ✓ Executive Compensation Initiative
- ✓ Tax-exempt Hospital Compliance Check
- ✓ Tax-exempt Bond Compliance Check



# Executive Compensation Initiative

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- ✓ IRS Compensation Initiative
- ✓ Over 1,800 exempt organizations contacted
  - 1,225 compliance check letters
  - 600 single-issue examinations
- ✓ 200 additional examinations from compliance check letters
- ✓ Phase III will continue in FY 2008



# Examination Issues

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- ✓ Compensation policies & procedures
- ✓ Duties and responsibilities of officers, trustees & key employees
- ✓ Compensation oversight by Board
- ✓ Reconciliation of Forms 990, W-2 & 1099
- ✓ Individuals' use of organization's assets
- ✓ Redesigned 990 will require reporting much of above information



# Executive Compensation Initiative Findings

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- ✓ Significant Reporting Issues Exist
  - Over 30% of compliance check recipients amended their Forms 990
  - Reporting, not excessive compensation, was major concern
  - Where problems were found, significant dollars were assessed (>\$21 million against 40 disqualified persons or organization managers)



# Automatic Excess Benefits

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## ✓ Taxing scheme

- 25% excess benefit, plus
- 200%, if not corrected
- Also, 10% tax on organization manager

## When Automatic?

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- ✓ Compensation, including taxable fringe benefits, not properly substantiated
  - Reported on W-2, 1099 or 990
- ✓ Regardless of FMV, IRS treats unsubstantiated compensation/benefits as automatic excess benefits, subject to excise taxes
  - Also subject to payroll & income taxes



# Exposure Items

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- ✓ Personal use of automobile
- ✓ Personal use of club memberships
- ✓ Moving expense reimbursements
- ✓ Personal travel, *e.g.*, spouse & family
- ✓ Housing allowances
- ✓ Business travel, entertainment & other expenses not adequately documented
  - Accountable plan rules
  - Business purpose, who entertained, date, amount, etc. . . .

# Example

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- ✓ Assume key executive receives following:
  - Salary of \$375,000
  - Personal use of car & country club membership with a FMV of \$25,000
  - Reimbursement of travel & entertainment expenses of \$20,000
- ✓ Adequate documentation required by IRS to support business purpose is not maintained contemporaneously
- ✓ Only \$375,000 included in W-2
- ✓ Non-accountable plan rules apply



# Example

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- ✓ Excess benefit transaction occurs
  - Penalty assessed of  $\$45,000 \times 25\% = \$11,250$
  - If  $\$45,000$  not repaid, then 2<sup>nd</sup> tier tax of  $\$45,000 \times 200\% = \$90,000$
  - Total excise tax =  $\$101,250$
  - Possible 10% penalty ( $\$4,500$ ) on any organization manager or board member who knowingly participates

# How to Avoid Automatic Excess Benefits

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- ✓ Have written plan in place
- ✓ Educate employees
- ✓ Periodically review policy
- ✓ Have board of directors periodically review
- ✓ Review employment arrangements
- ✓ Obtain contemporaneous documentation of value of goods or services

# Executive Compensation Governance

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- ✓ Consider meeting requirements of rebuttable presumption of reasonableness
  - Compensation set in advance by *disinterested* board members
  - Based on comparability data
  - Decisions must be appropriately & timely documented
- ✓ Shifts burden of proof to IRS



# Executive Compensation Governance

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- ✓ Reasonable Compensation – amount ordinarily paid for:
  - Like services
  - By like enterprises (whether taxable or tax-exempt)
  - Under like circumstances
- ✓ Comparability data can be obtained from Guidestar, ERI Economic Research Institute, SalariesReview, Abbott & more



# Executive Compensation Governance

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- ✓ **Good Compensation Governance**
  - Procedures – set & follow
  - Substance – responsible effort to determine appropriate levels
  - Board of directors/trustees maintains appropriate oversight

# Other New Developments

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## ✓ E-file

- For years ending 12/31/06 or after
  - \$10 million of assets & filing 250 returns
  - Required filing
  - Additional effort required
  - If organization prepares 990, must have IRS-approved software (see Useful Web Links slide for list of approved vendors)



## Other New Developments

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- ✓ **IRS Reminds Charities of Political Activity Ban**
  - IRS issued news release November 19, 2007
  - Direct & indirect candidate support:
    - Contributions
    - Participation in campaigns
    - Public statements for/against particular candidate
  - Absolutely prohibited



## Useful Web Links

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- ✓ Executive Compensation Phone Forum Materials
  - <http://www.irs.gov/charities/article/0,,id=158408,00.html>
- ✓ Hospitals and Community Benefit – Interim Report
  - <http://www.irs.gov/charities/charitable/article/0,,id=172267,00.html>
- ✓ Draft Redesigned Form 990
  - <http://www.irs.gov/charities/article/0,,id=171216,00.html>

## Useful Web Links

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- ✓ IRS List of Approved E-file Software Vendors
  - <http://www.irs.gov/efile/lists/0,,id=119598,00.html>
- ✓ IRS Reminds Charities of Political Activity Ban
  - <http://www.irs.gov/newsroom/article/0,,id=175818,00.html>
- ✓ GuideStar
  - [www.guidestar.org](http://www.guidestar.org)
- ✓ HFMA Statement 15
  - <http://www.hfma.org/NR/rdonlyres/B32E0CB5-9AE5-4127-83A3-02FFDE0054D5/0/400530Statement15.pdf>

## Useful Web Links

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- ✓ Catholic Health Care Community Benefit Information & State Comparison
  - <http://www.chausa.org/Pub/MainNav/ourcommitments/CommunityBenefits/>
  - <http://www.nonprofithealthcare.org/documentView.asp?docid=1064&sid>
- ✓ Federal Tax Manual for Charities Serving the Elderly
  - [http://www.aahsa.org/advocacy/legal\\_issues/documents/irsmanualfinal.pdf](http://www.aahsa.org/advocacy/legal_issues/documents/irsmanualfinal.pdf)

Thank you!

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