Catholic Health Association of the United States

Community Benefit Reporting: *Research*

DEVELOPED BY THE CATHOLIC HEALTH ASSOCIATION OF THE UNITED STATES IN COLLABORATION WITH VIZIENT

COMMUNITY BENEFIT REPORTING: RESEARCH

For many years, the Catholic Health Association of the United States and Vizient (CHA/Vizient) have published guidelines to help hospitals plan and report community benefits. CHA and Vizient are pleased to provide this additional resource which contains information designed to help hospital organizations report Research as community benefit.

For community benefit reporting purposes on IRS Form 990, Schedule H, *Research* is any study or investigation — the goal of which is to generate increased generalizable knowledge made available to the public — *and* that is funded by a tax-exempt or government entity (including the tax-exempt hospital organization itself). Clinical trials and other types of research conducted by hospitals and funded by for-profit entities (e.g., pharmaceutical companies and medical device manufacturers) are **not** reportable as community benefit.

On Schedule H, hospital organizations can report direct and indirect expenses they incur in conducting qualifying research studies as well as contributions they make to qualifying research performed by other entities. "Direct offsetting revenue" also is to be reported including:

- Grant funds provided by tax-exempt or government entities that are earmarked by the grantor (and used during the tax year) for qualifying research studies,
- Contributions or income received from foundations or endowments and restricted by these entities to be used for research,
- Medicare and other third-party patient care reimbursement generated when patients participate in covered research studies, and
- Any license fees or royalties received due to research that has been reported as community benefit.

What you need to know

- Many hospitals support Research that is:
  - Intended to increase public knowledge, and
  - Funded by a tax-exempt or government entity (including the hospital itself), and thus
  - Reportable as community benefit.
- Corporate structure can affect how Research is reported.
- This paper provides a recommended reporting process.

Several issues and questions have arisen over the years regarding how to report this important category of community benefit. This document is designed to help and is organized into the following sections:

- Why Research is reported as community benefit,
- Summary of Schedule H instructions,
- Research: What Counts, and
- Research: Accounting and Reporting Issues and Approaches.

WHY RESEARCH IS REPORTED AS COMMUNITY BENEFIT

The IRS has determined that conducting research is a factor in considering whether a hospital organization operates to benefit the community, is "described in Section 501(c)(3)" of the Internal Revenue Code,[1] and thus qualifies for tax-exempt status.

Section 501(c)(3) provides exempt status "for organizations that are, in general, religious, charitable, **scientific**, literary or educational."[2] IRS Rev. Rul. 69-545 provides examples illustrating whether a hospital organization is described under Section 501(c)(3) and provides community benefit, including "using surplus funds to advance medical training, education, and **research**."[3]

The IRS further states that "by using surplus funds to advance its medical training, education, and **research** programs, a hospital is promoting the health of the community."[4]

Schedule H instructions integrate these and other concepts into the definition of community benefit. The instructions state:

"Community benefit activities or programs also seek to achieve a community benefit objective, including improving access to health services, enhancing public health, **advancing increased general knowledge,** and relief of a government burden to improve health. This includes activities or programs that do the following.

- Are available broadly to the public and serve low-income consumers.
- Reduce geographic, financial or cultural barriers to accessing health services and if they ceased would result in access problems (for example, longer wait times or increased travel distances).
- Address federal, state or local public health priorities such as eliminating disparities in access to health care services or disparities in health status among different populations.
- Leverage or enhance public health department activities such as childhood immunization efforts.
- Strengthen community health resilience by improving the ability of a community to withstand and recover from public health emergencies.
- Otherwise would become the responsibility of government or another tax-exempt organization.
- **Advance increased general knowledge through education or research that benefits the public."**[5]

Many hospital organizations conduct research as an important component of their overall mission. They fund or subsidize research in recognition that new knowledge and discoveries can play a vital role in support of new knowledge and discoveries and in addressing community health needs.

SCHEDULE H INSTRUCTIONS: REPORTABLE RESEARCH

IRS Form 990, Schedule H instructs hospital organizations to report the total expense and direct offsetting revenue for research made available to the public and funded by tax-exempt or government entities including the organization itself. These are characteristics of research that provides community benefit and is not intended to benefit private, commercial interests.

The instructions state:

"Research means any study or investigation the goal of which is to generate increased generalizable knowledge made available to the public (for example, knowledge about underlying

1. https://www.irs.gov/charities-non-profits/charitable-hospitals-general-requirements-for-tax-exemption-under-section-501c3
2. bid, emphasis added.
3. Ibid, emphasis added.
4. Ibid.
5. Instructions for Schedule H (Form 990), emphasis added.

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.)

The organization can include the cost of internally funded research it conducts, as well as the cost of research it conducts funded by a tax-exempt or government entity."[6]

The instructions also enumerate the types of costs that can be reported for research that satisfies the above definition:

> "Examples of costs of research include, but aren't limited to, salaries and benefits of researchers and staff, including stipends for research trainees (Ph.D. candidates or fellows); facilities for collection and storage of research, data and samples; animal facilities; equipment; supplies; tests conducted for research rather than patient care; statistical and computer support; compliance (for example, accreditation for human subjects protection, biosafety, Health Insurance Portability and Accountability Act (HIPAA), etc.); and dissemination of research results."

Worksheet 7 in the Schedule H instructions is designed to support reporting research community benefit expense and offsetting revenue. See below:

Worksheet 7. **Research (Part I, line 7h)** *Keep for Your Records*

Total community benefit expense			
1.	Direct costs	1.	
2.	Indirect costs	2.	
3.	**Total community benefit expense** (add lines 1 and 2; enter on Part I, line 7h, column (c))	3.	
Direct offsetting revenue			
4.	License fees and royalties	4.	
5.	Other revenue	5.	
6.	**Total direct offsetting revenue** (add lines 4 and 5; enter on Part I, line 7h, column (d))	6.	
7.	**Net community benefit expense** (subtract line 6 from line 3; enter on Part I, line 7h, column (e))	7.	
8.	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 25)	8.	
9.	**Percent of total expense** (divide line 7 by line 8; enter on Part I, line 7h, column (f))	9.	%

6. Instructions can be found here: https://www.irs.gov/forms-pubs/about-schedule-h-form-990

The instructions also provide the following clarifications for specific lines in Worksheet 7:

- **Line 1.** Define direct costs under the guidelines and definitions published by the National Institutes of Health (NIH).
- **Line 2.** Define indirect costs under the guidelines and definitions published by the NIH. [7]
- **Line 4.** Enter license fees and royalties the organization received during the tax year that are directly associated with research that the organization has (in any tax year) reported on Schedule H as community benefit.
- **Line 5.** An example of "other revenue" is Medicare reimbursement associated with any research expense reported as community benefit.

The instructions clarify that "direct or indirect costs of research funded by an individual or an organization that isn't a tax-exempt or government entity" are not reportable as community benefit. But a hospital organization can:

"describe in Part VI any research it conducts that isn't funded by tax-exempt or government entities, including the cost of such research, the identity of the funder, how the results of such research are made available to the public, if at all and whether the results are made available to the public at no cost or nominal cost."[8]

Several issues and questions have arisen over the years regarding how to report Research. The following sections are intended to provide helpful clarifications.

RESEARCH: WHAT COUNTS ISSUES

The section that follows discusses several issues regarding "what counts" as Research, including:

- Research provided by the hospital organization versus other entities,
- Research that is fully funded,
- Types of studies that are counted and not counted, and
- Research that is partially funded by for-profit sources.

Research Expense Incurred by the Hospital Organization versus by Other Entities. Sorting out the extent to which the hospital organization (versus other entities) is conducting (and incurring expenses for) Research is one of the first steps in reporting this category of community benefit.

Differences in corporate structure and "who accounts for what" can be significant when it comes to reporting Research on Schedule H. In some academic medical centers, research is conducted primarily by an affiliated medical school, research institute, or other affiliated entity. These affiliates employ the researchers and ultimately bear the "costs of research" described in the Schedule H instructions. If these affiliates file IRS Form 990s that don't include one or more hospitals, then research they conduct would not be reported on Schedule H filings as community benefit. In other academic medical centers, substantial amounts of research are accounted for on the books of teaching hospitals that file Schedule H.

The IRS Form 990 is informative regarding the extent to which a filing organization is incurring research expenses. Part IX of the core Form 990 includes a "Statement of Functional Expenses" for filing organizations. Staff compiling community benefit information for Schedule H need to know how much research-related expense (for the "costs of research" identified in the instructions) is present in Part IX. If these amounts are zero or minimal, then the hospital organization itself is not bearing the "expense" of research studies.

It may be that the hospital organization is supporting research conducted by an affiliated medical school or research institute through cash transfers that are not accounted for as expense. Community benefits are reported as expense on Schedule H; some types

7. See: https://grants.nih.gov/grants/policy/nihgps/html5/section_7/7.3_direct_costs_and_facilities_and_administrative_costs.htm

8. Instructions can be found here: https://www.irs.gov/forms-pubs/about-schedule-h-form-990

of cash transfers are not accounted for or reported as expense in the core Form 990 and thus are not reportable as community benefit on Schedule H.[9] An alternative accounting treatment may be warranted if hospital organizations want to count their research support as community benefit.

The hospital organization may be funding Research provided by an affiliate. If the organization has restricted these amounts, in writing, to be used for that purpose, it could report them as

"Contributions for Community Benefit" on Schedule H. The amount of such contributions reported on Schedule H should be consistent with the amount of expense reported in IRS Form 990, Part IX for the contributions.

Research that is Fully Funded. Questions also arise regarding studies that appear to be fully funded by grants. The Schedule H instructions do not say that studies only are reportable if offsetting revenue is less than the direct and indirect costs incurred in providing the research. All research conducted by the hospital organization that meets the Schedule H definition of Research is to be reported.

Types of Studies Counted and Not Counted. Questions sometimes are raised regarding whether a specific study, evaluation, or investigation is "research." One example is an evaluation of a community health improvement program.

The Schedule H instructions include a broad definition of *Research*, namely: "any study or investigation the goal of which is to generate increased generalizable knowledge made available to the public …" If a hospital (using its own funds) evaluates the impact of a community health intervention or conducts internal quality improvement studies with the intent of publishing the results, then it has conducted qualifying Research.

Final regulations for IRC Section 501(r) require hospital community health needs assessment reports (CHNA) to include an evaluation of "the impact of any actions that were taken since the hospital facility finished conducting its immediately preceding CHNA." CHA/Vizient recommends including any cost associated with this impact evaluation and the CHNA process in Community Benefit Operations expense rather than in Research.

Another example is a study or investigation where the results are negative or unsuccessful. CHA/Vizient also recommends reporting all qualifying research expense on Schedule H whether or not the outcomes are successful. Nothing in the Schedule H instructions states that research studies must yield positive or successful results to be reported as community benefit.

Research that is funded in whole or in part by a for-profit source (e.g., a for-profit pharmaceutical company) is not reportable as community benefit on Schedule H.

CHA/Vizient recommends not reporting research if the findings only are used internally and are not made available to the public.

As always, it's helpful to consider whether a prudent layperson would conclude that a study or investigation is "research" or some other type of program, because the goal is to "generate increased generalizable knowledge made available to the public."

RESEARCH: ACCOUNTING AND REPORTING ISSUES AND APPROACHES

This section summarizes information regarding:

- A suggested reporting process for Research,
- Indirect cost rates,
- Reporting grant revenue, and
- Supporting research conducted by other entities.

9. Any such transfers can be described in Part VI of Schedule H.

The section concludes with a brief discussion regarding impacts of Research on hospital Ratios of Patient Care Cost to Charges.

Reporting Process. Organizations have found it helpful to implement the following process when reporting Research.

1. Develop a database that includes the following information for each study or investigation conducted by the organization:[10]

- Third-party study sponsor (e.g., NIH, National Cancer Institute, pharmaceutical company, foundation, etc.),
- Sponsor tax status (tax-exempt or for-profit),
- Date of institutional review board (IRB) approval,
- Date of intended publication/public release,
- Direct expense (incurred by the hospital organization for the relevant tax year),
- Negotiated indirect cost rate,
- Actual indirect cost rate,
- Actual indirect expense (direct expense x actual indirect cost factor),
- Total expense (sum of direct expense and actual indirect expense),
- Grant funding used for the study/investigation during the tax year (by grantor),
- Medicare and other third-party reimbursement (if any),
- Other direct offsetting revenue (e.g., license fees or royalties),
- Total direct offsetting revenue, and
- Net expense (total expense minus total direct offsetting revenue).

2. Identify the studies and investigations that are reportable as community benefit, because they are funded by a tax-exempt source and are intended for publication.

3. Tally the total expense and direct offsetting revenue for studies and investigations identified as reportable in step two.

4. Add in costs for IRB and for research administration, unless these costs already are included in indirect costs.

If the indirect cost factor applied to direct expenses has accounted for the entire cost of the organization's IRB and of other research administrative costs, then no such costs should be added again to avoid double counting.

5. Add in costs to present or publish the research as well, if these costs are borne by the hospital organization and if they also haven't been included already in indirect costs.

6. Identify whether the organization has received any license fees or royalties during the year due to research it reported as community benefit in any prior tax year.

If in the current year a hospital organization receives royalties on research it reported as community benefit in prior years, then the Schedule H instructions indicate that these amounts are to be included in direct offsetting revenue.

7. Assess whether research that is not reportable as community benefit should be described in Schedule H, Part VI, as allowed by the instructions.

10. Many academic medical centers have an Office of Research with information on research studies and Finance staff who specialize in grant accounting.

Indirect Cost Rates. The NIH provides the following clarification regarding direct and indirect costs:[11]

1. What is the difference between a direct cost and an indirect cost?

A direct cost is any cost that can be easily identified with a specific project (grant/contract): e.g., Salaries and Wages, Materials & Supplies, Subcontracts, Consultants.
An indirect cost is any cost that cannot be easily identified (or it would not be cost effective to identify) to a specific project, but identified with two or more final cost objectives. There are three types of indirect costs: Fringe Benefits: services or benefits provided to employees, e.g., Health Insurance, Payroll Taxes, Pension Contribution, Paid Absences, etc

Overhead: indirect costs associated with the performance of a project, e.g., Facility Costs (rent, heat, electricity, etc.), General Laboratory Supplies, etc.

G&A: indirect costs associated with the overall management of an organization, e.g., President's Office, Human Resources Office, Accounting Office, office supplies, etc.

For NIH-funded research, indirect costs are added to direct costs through negotiated rates that are applied to direct costs. As of 2017, the national average indirect cost rate for NIH grants was 52 percent.[12]

Indirect cost rates for many governmental and some other tax-exempt grantors are negotiated.[13] Indirect cost factors also can be subject to caps. The Schedule H instructions state that indirect costs are to be defined under the guidelines and definitions published by the NIH. The instructions don't say that the amounts must be based on negotiated outcomes.

As a result, when including indirect costs for Research reported as community benefit, it's important to include those amounts based on NIH guidelines and on the organization's actual overhead, G&A expenses and other costs described above.

Grant Revenue. Direct offsetting revenue includes grant funds used during the tax year to fund reportable Research expenses. For research projects that span multiple tax years, hospital organizations should use care not to report the entire amount of grant funds in the year they are awarded or received; instead, direct offsetting revenue should include the amount of funding actually used during each year.

Supporting Research provided by other entities. Many hospital organizations provide Contributions for Community Benefit. Hospital organizations providing cash and/or in-kind contributions for Research conducted by other entities can report these contributions as community benefit. As stated in the Schedule H instructions, to be reported, cash contributions or grants must be restricted by the organization in *writing* to be used by the recipient for a specific community benefit purpose, e.g. Research. These amounts generally would be reported on Schedule H, Part I, Line 7i (Cash and in-kind contribution for community benefit) rather than on Line 7h (Research).

Impact on Ratio of Patient Care Cost to Charges. Most hospital organizations use a Ratio of Patient Care Cost to Charges to estimate costs for Financial Assistance, Medicaid and Subsidized Health Services (the ratio). A worksheet to calculate the ratio is included in Schedule H instructions (Worksheet 2) and in CHA's *Guide to Planning and Reporting Community Benefit*.

Worksheet 2 includes adjustments to the ratio to avoid double counting and to exclude certain expenses that are unrelated to patient care. For example,

- A hospital may have $50 million in total Research expense reported as community benefit. If that $50 million is not subtracted from the numerator of the ratio, then a portion of Research expense will be double counted. $50 million of Research would be reported in full and then some additional Research expense would be included again when the ratio is used for Financial Assistance.

11. See: https://oamp.od.nih.gov/dfas/faq/indirect-costs#difference

12. https://www.sciencemag.org/news/2017/06/nih-plan-reduce-overhead-payments-draws-fire

13.https://www.niaid.nih.gov/grants-contracts/understanding-indirect-costs

- The Schedule H instructions allow hospitals to use Other Operating Revenue as a proxy for the cost of non-patient care activities. Many organizations subtract Other Operating Revenue from the numerator of the Ratio of Patient Care Cost to Charges.

If, however, a hospital organization has included grant revenue in Other Operating Revenue, it runs the risk of over-correcting the ratio.

Say, for example, that the hospital organization has reported $50 million in Research expenses as community benefit. This same hospital has reported $40 million of research grants in Other Operating Revenue — grants that are being used to fund the same $50 million in Research expense.

This hospital should not adjust the ratio by $90 million ($50 million in Research expense and $40 million in Other Operating Revenue). Doing so would reduce the ratio more than intended. The numerator of the ratio should be reduced by $50 million, thereby avoiding double counting.

ABOUT THE CATHOLIC HEALTH ASSOCIATION

The Catholic Health Association of the United States (CHA), founded in 1915, supports the Catholic health ministry's commitment to improve the health of communities and provide quality and compassionate health care.

CHA is recognized nationally as a leader in community benefit planning and reporting. In collaboration with member hospitals, health systems and others, CHA developed the first uniform standards for community benefit reported by not-for-profit health care organizations. These standards were used by the Internal Revenue Service to develop the Form 990, Schedule H for Hospitals.

ABOUT VIZIENT

Vizient is a member-driven, health care performance improvement company committed to optimizing every interaction along the continuum of care. Vizient was founded in 2015 as the combination of VHA Inc., a national health care network of not-for-profit hospitals; University HealthSystem Consortium, an alliance of the nation's leading academic medical centers; and Novation, the care contracting company they jointly owned. In February 2016, Vizient acquired MedAssets' Spend and Clinical Resource Management (SCM) segment, which included Sg2 health care intelligence.

Vizient has a long track-record of working to ensure that community-based, not-for-profit health care is supported. Congress, the White House and federal regulatory agencies, such as the Internal Revenue Service, regularly examine the merits of tax-exemption for not-for-profit hospitals and look to ensure that exemption is justified by activities that provide meaningful benefits to their communities. Vizient continues to work with policymakers to ensure that our members are represented in those policy discussions and are able to fully tell the full story of the essential care that they provide to the communities they serve.

ABOUT THE AUTHOR

Keith Hearle, MBA, is President of Verité Healthcare Consulting. Prior to establishing Verité in 2006, Keith led the Hospitals and Health Systems practice for The Lewin Group, Inc., served as CFO of the San Francisco Department of Public Health (Public Health Division), as a Manager at KPMG Peat Marwick and as a Senior Equity Analyst (Healthcare) for a California-based money manager.

In 1989, he developed for CHA/Vizient the first accounting framework for hospital community benefit and co-authored the CHA/Vizient Social Accountability Budget. He also authored the accounting chapters (and worksheets and other materials) in the May 2006 and December 2008 CHA/Vizient Guide to Planning and Reporting Community Benefit and in all subsequent editions. He developed a framework for determining "What Counts as Community Benefit," adopted by CHA/Vizient in 2007. In 2008, he was asked by IRS officials to draft major sections of the Instructions to IRS Form 990, Schedule H. He worked with IRS staff thereafter on refinements to the Instructions.

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COMMUNITY BENEFIT

A Mission to Care: A Commitment to Community

From the very beginning, civic leaders and congregations of religious women and men courageously responded to the needs of the communities they were called to serve.

Today, that same call to provide health and hope is being answered in unique and creative ways through community benefit programs.

AS COMMUNITY BENEFIT LEADERS:

We are concerned with the dignity of persons.
We are committed to improving health care access for all persons at every stage of life regardless of race, culture or economic status and to eliminating disparities in treatment and outcome.

We are concerned about the common good.
We design community benefit programs to improve health through prevention, health promotion, education and research.

We have special concern for vulnerable persons.
We put a priority on programs that address the most vulnerable in our communities and ensure that all programs reach out to persons most in need.

We are concerned about stewardship of resources.
We use resources where they are most needed and most likely to be effective.

We are called to justice.
We advocate health care for all and work to improve social conditions that lead to improved health and well-being.

We care for the whole person.
We engage partners in our communities so that together we improve health and quality of life through better jobs, housing and the natural environment.

For more information about community benefit and Catholic health care, go to www.chausa.org/communitybenefit

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