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Comments on IRS Draft Form 990

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Introduction

The Association for Healthcare Philanthropy (AHP) is an association of professional development executives who are responsible for the management of foundations and development departments of nonprofit health care providers throughout the United States. A critical part of their mission is supporting local health care programs through philanthropic fundraising that directly benefits the institution in which they work. These nonprofit medical facilities approach and have come to rely on the generosity of grateful patients who they have served to help underwrite wellness programs, mobile health vans, mammography screenings, hearing and eye exams, hospital facility improvements, essential equipment upgrades and health care services for the uninsured.

Established in 1967, AHP is a not-for-profit organization whose 4,500+ members manage philanthropic programs of foundations and development departments in 2,200 of the nation's not-for-profit, charitable health care providers. In 2006, this philanthropic support reached \$7.9 billion according to AHP's most recent giving survey report. As a practical matter, most, if not all, of health care providers routinely factor into their budgets an expected level of philanthropic support.

AHP represents highly skilled fundraisers in health care philanthropy. Many hold the Certified Fund Raising Executive (CFRE) or the Fellow Association for Healthcare Philanthropy (FAHP) designation, which recognize professionalism in the field by documenting experience and testing knowledge in health care resource development. More than 60% of AHP members have been in the field of fundraising for 11 or more years, with 39% having been in the field for 16+ years. Our members believe in transparency and accountability in their work and follow the AHP Statement of Professional Standards and Conduct and its companion Donor Bill of Rights. In addition, in 2006 AHP launched the AHP Performance Benchmarking Service. One of the goals of

this program is to provide consistent reporting of fundraising dollars that AHP member organizations generate.

AHP members are an integral part of their health care institutions and are a critical component in attracting needed dollars to support community benefit programs. With that in mind, AHP is a supporting organization of the *Catholic Health Association's Guide for Planning and Reporting Community Benefit*.

The Association for Healthcare Philanthropy (AHP) supports the Internal Revenue Service in its efforts to revise the Form 990 to facilitate accurate, complete, and consistent reporting by exempt organizations.

The Draft Form 990 generally will be easier for exempt organizations to complete and for the public to understand. There are, however, areas in the draft Core Form and Schedules that are unclear and need revision. AHP offers the comments below to address some areas of concern that affect not-for-profit health care organizations and their institutionally related foundations. AHP is a supporting member of Independent Sector and, where appropriate, Independent Sector's suggestions are incorporated into AHP's comments below.

Implementation and Transition Periods

AHP wants its members to have an improved form as soon as possible. However, health care organizations will need adequate time to understand and implement the changes that will be required to provide complete and accurate reports. AHP does not think it is realistic to require organizations to use a new Form to report financial information and other activities for Fiscal Year 2008. We strongly encourage the Service to delay implementation of the Core Form.

The time required by hospital and hospital foundation auditors to prepare these highly complex audit statements is such that they seldom finish in time to complete IRS Form 990 within the allotted filing schedule "by the 15th day of the 5th month after the organization's accounting period ends." This sequence results in a repeat request for Extension of Time to File (IRS Form 8868) for nearly all hospitals and hospital foundations every year. With this in mind, AHP recommends an additional year or more for implementation of a number of the new Schedules.

Use of the AICPA Audit Guideline

Unlike prior IRS instructions, there is no directive to follow any specific AICPA audit guideline in reporting financial details. In the past, health care organizations had to adapt their AICPA audit guide to match the general-purpose audit requirements. However, there are multiple references to the FASB SFAS 116 on how to account for revenue. AHP requests clarification on the use of the AICPA guide.

Comments on Core Form

Part I: Summary Page

AHP likes the approach taken by the Service of providing essential summary information on the first page of the Form 990. However, we have a number of concerns outlined below.

1. **Part I, Activities and Governance:** Line 6 asks for the number of individuals receiving compensation in excess of \$100,000 as reported in Part II. Line 7 asks for the highest compensation amount paid to Officers, Directors, Trustees, Key Employees, Highly Compensated Employees and Independent Contractors, as reported in Part II. Line 8 asks for officer, director, trustee, and other key employee compensation from Part V, Line 5, column B, which then is divided by program and service expenses and reported as a percentage. In combination, these are sensitive details, are subject to a variety of interpretation, and may lead to an incorrect or misleading picture of an organization's operations when compared only to total program and service expenses (but not administration and general or fundraising expenses).

We find that those who are interested in examining compensation levels are better served by the comprehensive information provided in Part II of the Core Form. A close look at the details in Part II, Section A is necessary, as it requires more compensation data on more individuals than previously. This may present a problem for hospitals with separate and/or subsidiary foundations where compensation paid to officers and directors of the hospital corporation may be paid by funds from the foundation as well as the hospital and vice versa. This same issue also will arise if the hospital "owns" other incorporated entities, either for-profit or nonprofit, where officers and directors of the hospital may receive compensation from another entity related to the parent hospital corporation. This may be a particular issue for hospitals and health care systems.

2. **Revenues, Expenses, Net Assets or Fund Balance, Granting & Fundraising:** The instructions for Line 19a and Line 19b will do nothing to eliminate the "creative accounting" associated with how expenses are reported. Further, it will increase public confusion on its interpretation. AHP's overriding concern is that the public does not understand the costs to raise philanthropic dollars. Whatever the cost, real or contrived, it is likely to be presumed as too much.

Therefore, AHP objects to the use of percentages of revenues and expenditures as appropriate indicators of an organization's effectiveness or efficiency. Whatever fundraising expense is reported and how it is reported (i.e. percentage of funds raised) is too often misunderstood and misinterpreted. Further, this figure is misused frequently by the media and by self-appointed "watchdogs" with their ratings and scores of nonprofit financial performance. These interpretations will add to the public's confusion and raise doubts about whatever amount nonprofits report as fundraising expenses. In addition, inclusion of these percentages gives the impression that the IRS believes there is a "right" percentage for each calculation. We do not believe this is a fair perception.

AHP recommends that the IRS drop the column requiring organizations to calculate revenues and expenses on lines 11-15 and lines 17-19 as percentages of the total amounts.

We further recommend (in concurrence with the Independent Sector) that the IRS drop the following percentage calculations on the Summary Page:

The computation of officer, director, and other key employee compensation as a percentage of total program service expense (line 8b). Those who are interested in the allocation of this compensation will find a more accurate presentation on Part V, Statement of Functional Expense, line 5. There is no reason to highlight the program percentage on the Summary Page.

The computation of fundraising expenses as a percentage of contributions and grants (line 19b). This percentage can vary greatly depending on the organization's size, structure, and current priorities. A single large gift or bequest can be the result of extensive work in prior years, thus skewing the organization's reported percentages in both the current year and the prior years. Such gifts can also be the result of no direct fundraising expense by the organization in any year.

The computation of total expenses as a percentage of net assets (line 24b): This percentage is not an appropriate indication of whether an organization is spending money on current programs commensurate with its resources. An organization may be setting aside funds to purchase or build new facilities, expand its program services, or purchase equipment necessary for its programs. A more complete, useful picture of the allocation of an organization's net assets or fund balances is provided on Part VI, Balance Sheet, lines 28-35. If the IRS believes this information is important to include on the Summary Page, it would be more helpful to readers to ask organizations to indicate their unrestricted, temporarily restricted, and permanently restricted net assets than to include this misleading indicator.

3. **Gaming and Fundraising Information (lines 15, 25, and 26):** AHP believes these two activities should have separate categories and not be combined on the Core Form. Plus, there is confusion on Schedule G and what is to be reported in Part I. What is to be reported on Line 15? The answer is to be taken from Part IV, Line 3, Line 7, Line 9d, Line 11c, Line 13e, and Line 13e. However, membership dues and assessments were already reported as revenue in Part I, Line 13. And, net income from fundraising events is to be reported again on Line 26. This duplication is a concern. More comments are presented in our review of Schedule G.

Part II: Compensation

As we stated above, Part II, Section A may present a problem for hospitals with separate and/or subsidiary foundations where compensation paid to officers and directors of the hospital corporation may be paid by funds from the foundation as well as the hospital and

vice versa. This same issue also will arise if the hospital “owns” other incorporated entities, either for-profit or nonprofit, where officers and directors of the hospital may receive compensation from another entity related to the parent hospital corporation. This may be a particular issue for hospitals and health care systems.

We approve of the new format as it will require full disclosure of every officer or highly paid employee with details on their compensation packages.

Part III: Governance

AHP has no comments on this section at this time.

Part IV: Revenue

An important problem continues to exist in Section IV as it does in the current IRS Form 990. Because Line 11a requires contributions reported on Line 1c to be excluded, most auditors consider fundraising event sponsorships and underwriting gifts to be “contributions” and thus to be reported in Line 1c rather than Line 11a. Only admission and/or ticket sales are reported on Line 11a. This practice reduces the amount of total event revenue and negatively impacts the net income figure. As a consequence, nonprofits frequently report net income loss for their events, which is an incorrect assessment. This net loss also causes confusion and concern with donors and volunteers who supported the event and were told the event made a profit to benefit the organization’s mission.

Another area of concern is Line 1g. It is always difficult to establish the value of Noncash Gifts. Therefore the amount of revenue to be reported must be able to be documented with reliability if the hospital elects to accept such a gift and to assign a value to it that is included as an asset on its audit statement. IRS guidelines offer examples of valuation as “cost or selling price of the donated property, sale of comparable properties, replacement cost, opinions of experts, etc.” These guidelines also cite IRS Publication 561. Determining the Value of Donated Property for use in valuation.

Part V: Statement of Functional Expenses

The general instructions to the draft Form 990 indicate that all organizations will be required to follow SOP 98-2 regarding joint allocation of fundraising costs. The continuing challenge to all nonprofits remains - how to report joint cost allocations between these expense groups that are to be reported in Section V. The IRS instructions refer to SOP 98-2, the current AICPA guideline for joint cost allocation, but some audit firms apply a simple 80%-20% allocation between Fundraising Expenses and Management and General Expenses rather than attempt to assess the actual allocations.

Part VI: Balance Sheet

AHP has no comments on this section at this time.

Part VII: Statements Regarding General Activities

AHP has no comments on this section at this time.

Part VIII: Statements Regarding Other IRS Filings

AHP has no comments on this section at this time.

Part IX: Statement of Program Service Accomplishments

AHP has no comments on this section at this time.

Comments on Schedules

Schedule A: Supplemental Information for Organizations Exempt Under Section 501(c)(3)

AHP has no comments on this section at this time.

Schedule B: Schedule of Contributions

AHP has no comments on this section at this time.

Schedule C: Political Campaign and Lobbying Activity

AHP has no comments on this section at this time.

Schedule D: Supplemental Financial Statements

AHP has concerns with Part XII, Endowment Funds, with the IRS required disclosure of the organization's spending of endowment fund assets over a five-year period. The intent is "to improve transparency of an organization's accumulation of endowment assets including through related organizations, and the rationale for such accumulation." The implication is that funds held as endowments have to be "spent" and that their accumulation is viewed as either inappropriate or unnecessary. The question needs to be answered as to whether there is any Federal law that limits a nonprofit organization's right to develop endowment funds or sets limits on either the value it may achieve or any requirements for use or retention of its investment earnings.

Schedule E: Schools

AHP has no comments on this section at this time.

Schedule F: Activities Outside of the U.S.

AHP has no comments on this section at this time.

Schedule G: Fundraising Activities

Part I, Line 3 "List all jurisdictions in which the organization is authorized to solicit funds." There are two issues here. First, this will not be an easy task for any nonprofit that solicits outside its state of residence where formal registration to solicit is not required by any State regulations. Second, there are multiple local regulations also in place for event registration and reporting, be it a county, city, town, municipality or Indian Reservation. These regulations frequently require a minimal excise tax (3% to 5%) to support the cost of necessary police and fire support of any form of public event.

Part II asks for seven sets of figures for each qualifying event (\$10,000 or more in revenue): Gross receipts, Charitable contributions, Gross revenue, Cash prizes, Non-cash prizes, Rent/Facility costs, and Other direct expenses. Instructions on how to calculate

and report the value for Cash prizes and Non-cash prizes were not provided. This will pose problems.

Schedule H: Hospitals

There are two areas in Schedule H where IRS requirements may be in conflict with State regulations on both charity care and community benefit reporting. Some States already require these details and assess either a fee or tax assessment based on property value. Further, among several states where these reports are required, some prohibit public solicitation to be used to benefit charity care and/or community benefit programs. A lot of confusion already exists here and the new Schedule H will not help resolve this. AHP requests clarification and guidance on this.

The Catholic Health Association's (CHA) *A Guide for Planning and Reporting Community Benefit* is cited as a reference document in support of the new Schedule H. However, it appears this text will apply only to Part I, Community Benefit Report and not the balance of Schedule H, a detail that needs to be resolved.

Schedule I: Grants

AHP has no comments on this section at this time.

Schedule J: Supplemental Compensation Information

AHP has no comments on this section at this time.

Schedule K: Supplemental Information on Tax Exempt Bonds

AHP has no comments on this section at this time.

Schedule L Supplemental Information on Loans:

AHP has no comments on this section at this time.

Schedule M, Noncash Donations

It is always difficult to document the value of non-cash gifts. The IRS states that the method of valuation must be cited but it is still not going to be consistent across the board for nonprofits. For instance, some nonprofit organizations do not record non-cash contributions in their accounting records at their "fair market value," given the time and cost involved in establishing such values.