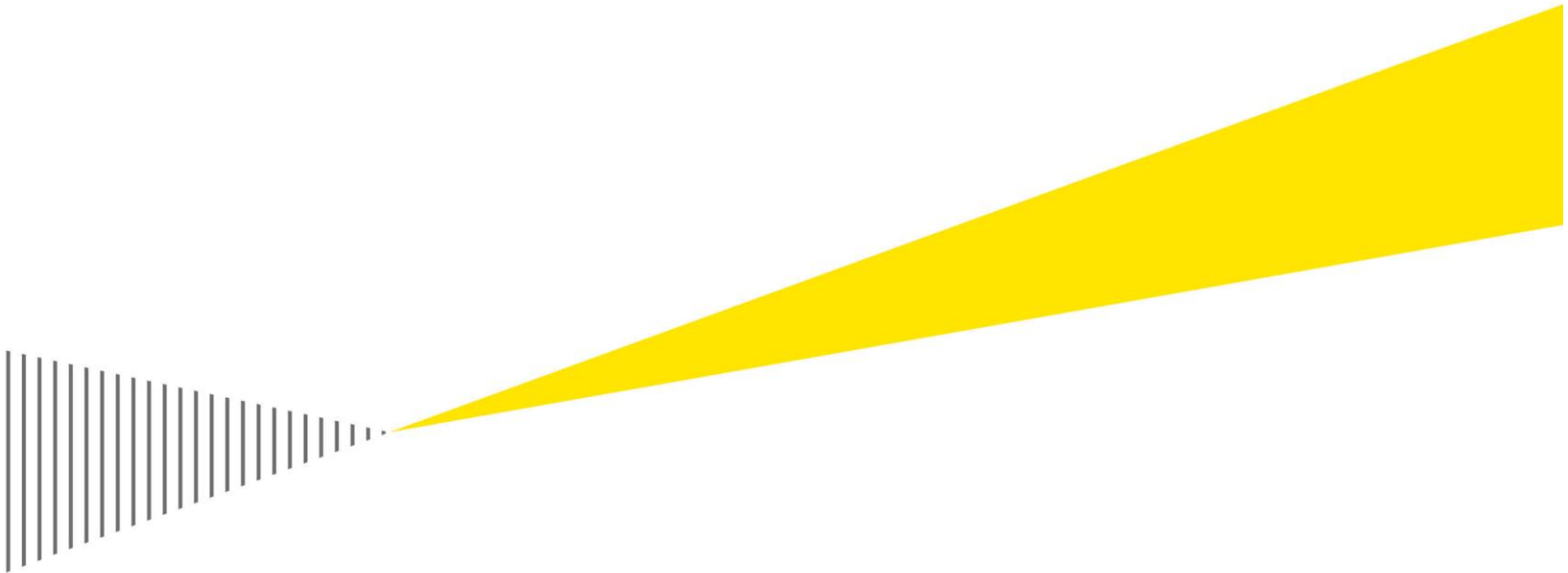


Value of tax exemption of tax-exempt hospitals in Indiana for tax year 2022

Prepared for the Indiana Hospital Association

January 2025



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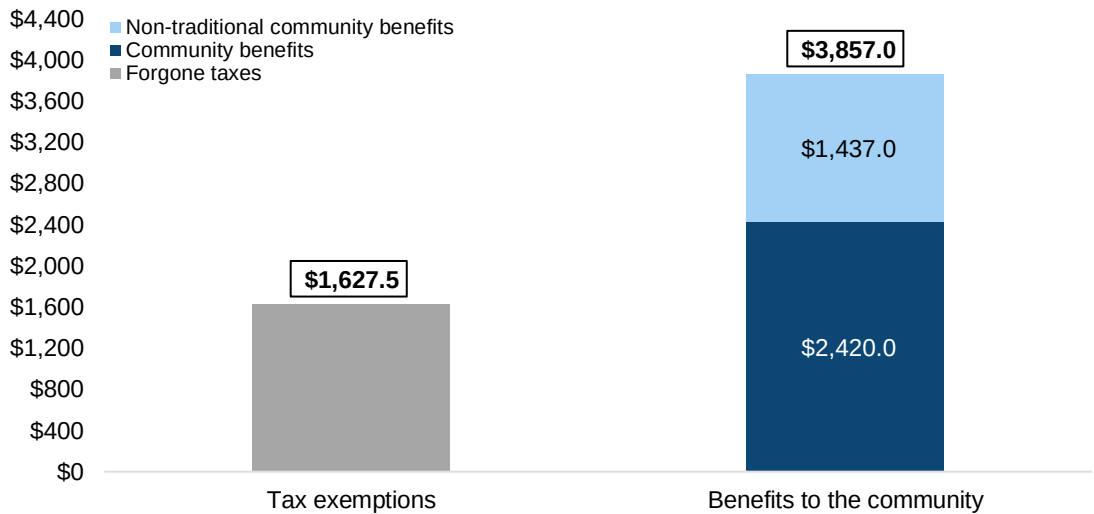
Executive summary

This report provides an estimate of the federal, state, and local revenue foregone due to the tax-exempt status of Indiana not-for-profit, tax-exempt hospitals (“tax-exempt hospitals”) as well as the benefit of their tax exemption compared to the community benefits provided.¹

As part of their charitable missions, tax-exempt hospitals within the Indiana Hospital Association provided community benefits totaling over \$2.4 billion in tax year 2022. When considering non-traditional community benefits, this total reaches \$3.9 billion in benefits to the community. In the same year, these tax-exempt hospitals received tax exemptions totaling \$1.6 billion. However, Indiana’s hospitals generated net operating losses in 2022 which they could likely carryforward to future periods and use to offset future corporate tax liability, if those hospitals were taxable. The estimated tax value of those carryforward losses is approximately \$342 million, which reduces the total benefit of tax exemption to \$1.3 billion. The largest exemptions were \$578 million from real property tax, \$571 million from tangible property tax, and \$283 million from sales tax.

Overall, as shown in figure E1, the traditional community benefits Indiana tax-exempt hospitals provided exceeded the value of their tax exemptions by nearly \$793 million. Additional non-traditional community benefits totaled \$1.4 billion, resulting in total benefits to the community exceeding the value of tax exemptions by \$2.3 billion.

Figure E1. Tax exemptions for Indiana tax-exempt hospitals relative to community benefits provided, 2022 (\$ in millions)



Sources: EY tabulations of IRS Forms 990, Schedule H; EY’s report on “Community benefits of tax-exempt hospitals in Indiana for tax year 2022”; and audited financial statements for tax-exempt hospitals and health systems within Indiana.

¹ The Indiana Hospital Association has 193 acute care hospitals and systems, of which 96 are tax-exempt entities, 63 are for-profit taxable entities, and 34 are governmental entities, representing all Indiana hospitals. Our analysis considers Schedule H’s for 64 distinct EINs affiliated with 82 tax-exempt hospitals across 20 hospital systems. Certain hospitals and types of operations (e.g., rehabilitation) are not required to fill out the IRS Form 990 Schedule H, though they might be considered to benefit the community though their affiliation with their broader hospital system. The tax exemptions extended to hospitals without the IRS Form 990 Schedule H are still included in our estimate of our overall tax exemptions provided to hospital systems. Analyses of both community benefits and tax exemptions exclude any standalone hospital without a Schedule H and the portion of any hospital systems located outside of Indiana.

I. Benefit of tax exemptions for Indiana tax-exempt hospitals, tax year 2022

Overview

This report provides an estimate of the federal, state, and local revenue foregone due to the tax-exempt status of Indiana's tax-exempt hospitals, as well as the benefit of their tax exemptions compared to the community benefits.²

As presented in EY's report on "Community benefits of tax-exempt hospitals in Indiana for tax year 2022," as part of their charitable mission, tax-exempt hospitals in Indiana provided community benefits totaling over \$2.4 billion. When considering non-traditional community benefits, this total reaches \$3.9 billion in benefits to the community.³

The tax-exempt hospitals in Indiana received tax exemptions totaling over \$1.6 billion. These tax exemptions represented 6.3% of the hospitals' total expenses in 2022 (\$25.8 billion).⁴ Overall, the community benefits Indiana's tax-exempt hospitals provided exceeded the value of their tax exemptions by \$793 million. Total benefits to the community exceeded the value of tax exemptions by \$2.3 billion.

Benefit of tax exemptions

In tax 2022, tax-exempt hospitals in Indiana received over \$1.6 billion in tax benefits, comprised of \$196 million in forgone federal taxes and \$1.4 billion in forgone state and local taxes. When accounting for losses these hospitals would be able to claim on federal corporate income taxes and Indiana corporate adjusted gross income taxes due to expenses in excess of revenue, this total would drop to \$1.3 billion.

For comparison, as presented in EY's report on "Community benefits of tax-exempt hospitals in Indiana for tax year 2022," Indiana's tax-exempt hospitals provided community benefits totaling \$2.4 billion in 2022. When considering non-traditional community benefits, this total reaches \$3.9 billion in benefits to the community.⁵

Figure 1 below displays total federal, state, and local tax revenue forgone due to the tax benefits available to tax-exempt hospitals relative to the value of hospital-provided financial assistance and other community benefits. Overall, the community benefits Indiana tax-exempt hospitals provided exceeded the value of their tax exemptions by \$793 million in tax year 2022. Total benefits to the community, inclusive of non-traditional community benefits, exceeded the value of tax exemptions by \$2.3 billion.

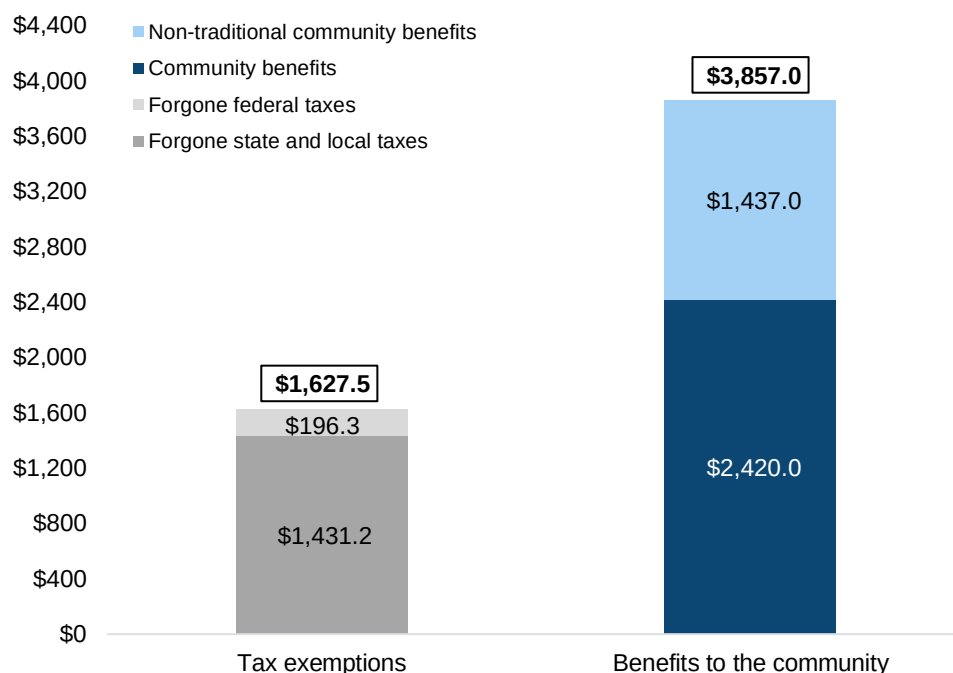
² Please see footnote 1 in the executive summary.

³ See EY's report on "Community benefits of tax-exempt hospitals in Indiana for tax year 2022" for additional details on community benefit calculations and results.

⁴ Source: Total expenses are based on total reported expenses on IRS Forms 990. Separately, based on EY calculations from hospital audited financial statements, total expenses were \$31.1 billion in tax year 2022.

⁵ See EY's report on "Community benefits of tax-exempt hospitals in Indiana for tax year 2022" for additional details on community benefit calculations and results.

Figure 1. Tax exemptions for Indiana tax-exempt hospitals relative to community benefits provided, 2022 (\$ in millions)



Sources: EY tabulations of IRS Forms 990, Schedule H; EY's report on "Community benefits of tax-exempt hospitals in Indiana for tax year 2022"; and audited financial statements for hospitals and health systems within Indiana.

Table 1 compares forgone taxes with total benefits to the community for tax-exempt Indiana hospitals. Total tax exemptions represented 6.3% of total hospital expenses, of which federal taxes were 0.8% of expenses and state and local taxes were 5.5% of expenses. Meanwhile, community benefits represented 9.4% of tax-exempt hospital expenses, and total benefits to the community inclusive of non-traditional community benefits represented 14.9% of total expenses.

Table 1. Tax-exempt hospitals' forgone taxes and total benefits to the community as a percentage of expenses for tax year 2022 (\$ in millions)

	2022	
	Amount	Percent of total expense
Forgone federal taxes	\$196.3	0.8%
Forgone state and local taxes	\$1,431.2	5.5%
Total value of tax exemption	\$1,627.5	6.3%
Traditional community benefits	\$2,420.0	9.4%
Non-traditional community benefits	\$1,437.0	5.5%
Total benefits to the community	\$3,857.0	14.9%

Note: Figures may not sum due to rounding.

Sources: EY tabulations of IRS Forms 990, Schedule H; EY's report on "Community benefits of tax-exempt hospitals in Indiana for tax year 2022"; and audited financial statements for hospitals and health systems within Indiana.

II. Value of tax exemptions for Indiana tax-exempt hospitals, tax year 2022

Total value of tax exemptions

Indiana tax-exempt hospitals benefit from multiple tax exemptions because of their tax-exempt status. The overall benefit to Indiana hospitals, as well as the distribution of exemptions by tax exemption type, are displayed in Table 2 below for tax year 2022. The overall benefit of tax exemptions for tax-exempt hospitals in Indiana totaled nearly \$1.6 billion, including \$1.4 billion in state and local tax exemptions and \$196 million in federal tax exemptions. The total value of tax exemptions as a percentage of hospital expenses was 6.3%.

Current year losses will generally reduce net payments in the current or future years due to refunds or net operating losses carried forward. To reflect this impact, the estimates presented in this report assume that current year losses reduce the aggregate current year exemption of Indiana's tax-exempt hospitals from the federal corporate income tax and the Indiana corporate adjusted gross income tax.⁶ Together, federal corporate income taxes and Indiana corporate adjusted gross income taxes resulted in \$342 million in losses. When accounting for these losses, the total tax benefits to the Indiana's tax-exempt hospitals would be approximately \$1.3 billion. These losses are also shown in Table 2 below. When considering total tax benefits after losses on income, these percentages decline to 5.0%.

Table 2. Value of tax exemptions for Indiana's tax-exempt hospitals, 2022 (\$ in millions)

	2022	
	Amount	Percent of total expense
Real property tax (local)	\$577.2	2.2%
Tangible property tax (local)	\$571.4	2.2%
Sales tax (state)	\$282.6	1.1%
State and local tax total	\$1,431.2	5.5%
Tax exempt financing	\$193.3	0.7%
Federal unemployment tax	\$3.0	0.0%
Federal tax total	\$196.3	0.8%
Total value of tax exemption	\$1,627.5	6.3%
State corporation business tax	-\$67.3	-0.3%
Federal corporate income tax	-\$274.4	-1.1%
Total value of losses on income	-\$341.7	-1.3%
Total tax benefits after losses on income	\$1,285.8	5.0%

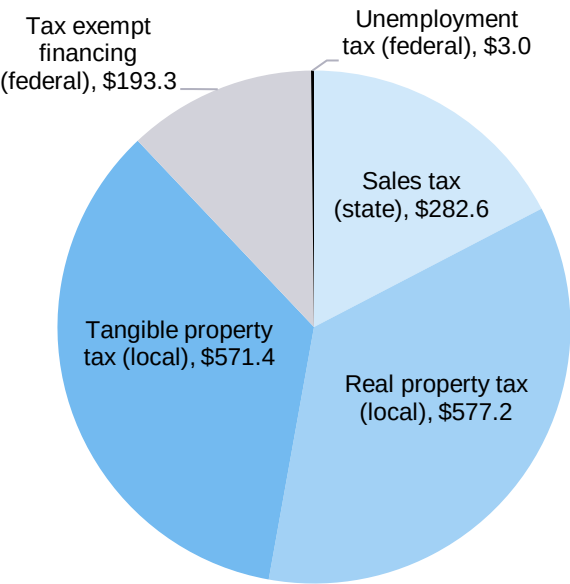
Source: EY tabulations of audited financial statements for hospitals and health systems within Indiana

As shown in Figure 2 below, the largest tax exemptions were \$577 million from real property tax, \$571 million from tangible property tax, and \$283 million from sales tax. The hospitals also

⁶ For Federal corporate income tax purposes, net operating loss deductions can be carried forward indefinitely, but the deductions are limited to 80% of taxable income each tax year.

benefited from lower interest rate on debt issuance worth approximately \$193 million in tax exempt financing and about \$3 million in federal unemployment tax.

Figure 2. Breakdown of federal, state, and local tax revenue forgone from tax-exempt hospitals within Indiana (\$ in millions), 2022



Source: EY tabulations of audited financial statements for hospitals and health systems within Indiana

State and local tax exemptions

Real property tax exemption

In Indiana, all types of real property and improvements to real property are taxed. The tax is levied by localities, such as counties, cities, and townships.

Real property is taxed based on the value of land and the improvements to that land. Our analysis applies Indiana’s assessment ratio of 100% to the total value of real property (land and buildings), leased improvements, and construction in progress as reported on tax-exempt hospital’s audited financial statements. For 2022, applicable Indiana property tax rates ranged from 1.984% for Angola within Steuben County to 8.817% for Gary-Calumet within Lake County. Rates were subsequently applied to total value assessed value.

The total estimated assessed value of real property owned by Indiana tax-exempt hospitals was \$17.7 billion. Had this property been taxed at applicable commercial rates the tax liability would have \$577 million in tax year 2022.

Tangible personal property tax

In Indiana, tangible personal property are also taxed and levied by localities. Tangible personal property is assessed and taxed at the same rates as real property. Tangible personal property includes items such as hospital equipment (e.g., medical equipment, hospital beds).

Similar to real property, our analysis applies Indiana's assessment ratio of 100% to the total depreciated book value of tangible personal property (i.e., equipment, furniture) reported on tax-exempt hospital's audited financial statements. Note that there would be differences between the book depreciation rate and the personal property tax depreciation rates used by Indiana localities. Due to minimum tax depreciation floors in Indiana, this estimate may slightly understate the value of personal property tax. The same tax rates, ranging from 1.984% to 8.817% for each hospital's locality are then applied to the assessed values for those hospitals.

The total estimated value of tangible personal property owned by Indiana tax-exempt hospitals was \$16.3 billion, corresponding to tangible personal property tax exemptions of \$571 million in tax year 2022.

Sales tax exemption

The state of Indiana imposes a sales and use tax at the rate of 7.0%. The sales tax applies to gross retail income received by a merchant.⁷ In addition, the Indiana use tax complements the retail sales tax by taxing purchases for which the sales tax has not been paid (e.g., supplies purchased in another state for use in an Indiana hospital). The sales tax is levied by the state; there is no applicable local sales tax in Indiana.

The value of the sales tax exemption was estimated by applying the state sales tax rate of 7.0% to the estimated amount of taxable purchases by Indiana tax-exempt hospitals. With regard to the sales tax calculation:

- ▶ Purchases of medical equipment, devices, drugs, other supplies, and prescription prosthetic or mobility aids are generally exempt from the state sales tax in Indiana. Items typically included in these categories are blood products, oxygen, artificial limbs and organs, and other items that replace a malfunctioning portion of the body, including extremities.⁸
- ▶ Sales tax collected by tax-exempt hospitals on retail sales by hospitals (i.e., cafeteria sales, breast pump sales, etc.) is treated as paid by the purchasers.

The estimated value of the sales tax exemption on purchases by tax-exempt Indiana hospitals was \$283 million in tax year 2022.

⁷ Wolters Kluwer CCH. Indiana, Rate of Tax. ¶60-110, Rate of Tax -IC 6-2.5-2-2, Indiana, Tax rate; rounding rules & IC 6-2.5-3-3, Indiana, Rates; certain transactions defined. Retrieved from: <https://answerconnect.cch.com/state/jin0109013e2c83b0e2cc/explanations>

⁸ Indiana Department of Revenue. Sales Tax Application to Medical Profession. Retrieved from: <https://www.in.gov/dor/files/sib48.pdf>

Federal tax exemptions

Tax exempt financing

In calculating the revenue forgone from tax-exempt bond financing by tax-exempt hospitals, EY assumed the total amount of long-term debt reported on the audited financial statements of the tax-exempt hospitals was issued as federally tax-exempt bonds. EY also assumed that the average marginal tax rate applicable to investors in tax-exempt bonds is approximately 30%.⁹ The difference in the rates for Aaa and Baa corporate bonds to tax-exempt bonds is applied to the long-term debt reported on the audited financial statements for each tax-exempt hospital or health system.

The estimated revenue forgone from tax-exempt bonds of tax-exempt hospitals was \$193 million in tax year 2022. To the extent that tax-exempt hospitals are using short-term financing with lower yields, the revenue forgone would be lower.

It should be noted that the benefit received by a tax-exempt hospital bond issuer is likely smaller than the federal revenue forgone, as the amount of revenue forgone is dependent on all the marginal tax brackets of the investors, whereas the market-clearing interest rate may be for a lower marginal tax bracket than that of many of the other bondholders. Furthermore, investors may not convert the entire tax benefit they receive into a lower cost of financing for the hospital.

Federal unemployment tax

The value of the revenue forgone from the federal unemployment tax is calculated assuming an effective federal unemployment tax rate of 0.6 percent¹⁰ and a maximum wage base of \$7,000 per employee. Based on the approximately 71,000 full-time equivalent employees working at the tax-exempt hospitals in Indiana, the total value of the exemptions from federal unemployment tax is estimated as \$3 million.¹¹

Federal and state corporate income tax exemptions

Federal corporate income tax and Indiana corporate adjusted gross income tax losses

In aggregate, Indiana hospitals generated net operating losses of \$1.3 billion in 2022, with loss-making hospitals reporting losses of \$1.5 billion and hospitals with net gains reporting net gains of \$202 million. The estimate presented in this analysis is based on the aggregate \$1.3 billion in losses, and assumes that these losses would be available to claim against potential positive prior-year or future-year income to generate a tax benefit. The estimated tax value of those

⁹ Our analysis uses a 30% average marginal rate applicable to investors in tax exempt bonds. This percentage is likely far higher than the actual average (CBO estimates for 2007 ran as low as 21%). This analysis assumes the higher percentage in order to provide a more conservative estimate, as a lower average marginal tax rate would lead to a lower amount of federal revenue forgone for tax-exempt financing. For instance, if the marginal tax rate were assumed to be 21%, then the federal revenue forgone as a result of tax exempt financing would decline to \$3.5 billion.

¹⁰ SurePayroll by Paychex. Payroll Tax Management Services. Retrieved from:

<https://www.surepayroll.com/resources/tax-management>

¹¹ Estimated number of full-time equivalents are from the Indiana Department of health hospital service reports for the tax-exempt hospitals in Indiana. Retrieved from: <https://www.in.gov/health/cshcr/reports-on-health-care-facilities/hospital-reports/>

carryforward losses is approximately \$342 million, including \$274 million of federal tax loss value and \$67 million in state tax benefit.¹² In other words, there is a tax benefit to a taxable hospital of generating a net operating loss and the tax exemption provided to Indiana hospitals in 2022 eliminated that tax benefit, resulting in a negative tax benefit associated with corporate tax exemption.

Estimates of taxable income

Indiana tax-exempt hospitals are exempted from paying federal corporate income taxes and Indiana corporate adjusted gross income taxes. Among the tax-exempt hospitals and systems, 54% had a net book operating gain (income) in 2022. After taking into account differences in the measurement of book net income and federal taxable income, plus the additional deductible expenses from state and local taxes and higher interest expense that would apply if the tax exemption were not available, 37% of the hospitals and systems analyzed would have net operating gains for federal and state tax purposes. In other words, if all tax-exempt hospitals in Indiana were to immediately turn for-profit, 63% of them would be operating at a loss.

Tax-exempt hospitals within Indiana reported \$1.6 billion in net book operating losses. After consideration of book/tax differences including over \$2 billion in unrealized losses, Indiana tax exempt hospitals had a net gain of \$300 million on a tax basis. However, were these hospitals taxable, they would also have deductible indirect tax costs (e.g. sales, property tax) that would reduce the \$300 million of taxable income to \$1.3 billion in losses. Federal corporate income taxes and Indiana corporate adjusted gross income taxes were applied to the net income after taxes were the tax-exempts to be non-tax-exempt. The federal 21% statutory rate was applied to hospitals based on taxable income. The Indiana corporate business tax rate is 4.9%.¹³

With regard to the income tax calculations:

- ▶ For multi-entity hospital systems, there are inter-company allocations that affect income and expense among the consolidated groups. Full eliminations to isolate the consolidated income and expense have not been done in this analysis.
- ▶ For multi-entity hospital systems including both Indiana and foreign (non-Indiana) subsidiaries, only data for tax-exempt hospitals within Indiana was used. Shared activities were apportioned to entities based on revenue (when available) or share of hospitals within system.

¹² Wolters Kluwer CCH. Internal Revenue Code §172 Retrieved from: <https://answerconnect.cch.com/federal/arp1209013e2c83dc44a7SPLIT172b/explanations/arp109d8d62be7c551000bdfad8d385ad169401f/what-are-the-net-operating-loss-nol-carryback-and-carryforward-periods>
For Federal corporate income tax purposes, net operating loss deductions may not be carried back beginning after 2020 (previously NOLs could be carried back two years, though up to five years for 2018-2020) and carried forward 20 years.

Wolters Kluwer CCH. Indiana, Subtractions--Net Operating Loss. ¶16-310, Subtractions--Net Operating Loss. Retrieved from: <https://answerconnect.cch.com/state/jin0109013e2c83f6f752/explanations?searchId=2515539730&disableHighlight=false>

¹³ Indiana Department of Revenue. Corporate Income Tax Overview. Retrieved from: <https://www.in.gov/dor/files/ib12.pdf>

- ▶ Our analysis assumes that each primary entity would file a consolidated tax return and would be able to fully deduct net operating losses in one entity against taxable income from other entities in the group.
- ▶ There are book/tax differences that require adjustment to estimate federal and state taxable income. For instance, “net assets released from restrictions used for operations” may be an equity transfer from other tax-exempt hospitals and would not be included in income for tax purposes. Impairments are one of several major book/tax differences that affect the estimated federal and state income tax liability.
- ▶ Other book/tax differences include depreciation/amortization, realized vs. unrealized gains, the tax basis of assets sold, capital loss limitations, and reserves that may not be deductible for income tax purposes. Adjustments were made where data was available.
- ▶ Some book/tax differences, such as impairments (e.g. unrealized declines in fair market value), may be due to timing differences. While the book treatment recognizes declines in fair market value, the tax loss deduction would not be taken until a later year when the asset has been abandoned or sold.
- ▶ State and local taxes would be deductible against federal income tax liability and have been considered in the estimates. In 2022, this includes the \$578 million real property taxes, \$571 million tangible property taxes, \$283 million state sales taxes, and \$3 million for federal unemployment taxes that would be paid by the hospitals if they were not tax-exempt.
- ▶ Loss of tax-exempt bonds would increase interest costs related to debt by an estimated \$193 million in 2022. To calculate the unconsolidated income tax liability for each hospital in a system, the total amount of long-term debt was distributed among the hospitals based on the proportion of total hospital expense.
- ▶ Federal and state income tax credits may be available, but they are beyond the scope of this review. No state or federal tax credits are assumed.

Adjustments to reported income incorporated in the estimate of revenue forgone from corporate income tax exemptions

In this analysis, we apply the general federal and state tax rules to the levels of tax-exempt activities reported by tax-exempt hospitals. Not all aspects of the detailed federal and state tax rules can be applied to the available financial data in audited financial statements for those hospitals, so estimates of revenue forgone require additional data and/or assumptions, which are described below.

Bonus depreciation not reflected

In 2022, federal tax law allowed bonus depreciation that provided additional first-year tax write-offs of capital investments as part of the fiscal stimulus.¹⁴ Bonus depreciation applied to only

¹⁴ Murray, J. (2020, December 29). Bonus Depreciation and How It Affects Business Taxes. The Balance. Retrieved from: <https://www.thebalancemoney.com/what-is-bonus-depreciation-398144>
US Bank. (2024, January 29). Maximizing your deductions: Section 179 and Bonus Depreciation. Retrieved from:

certain qualifying property, and some state tax systems did not conform to this provision. Due to this complexity and data constraints, bonus depreciation was not considered in this analysis. Had bonus depreciation been reflected in the estimates, it would have reduced the federal corporate income tax forgone for these two years.

Contributions excluded from income

Our analysis reduces hospitals' taxable income by the amount of contributions they received. If contributions constitute gifts for federal income tax purposes, such gifts are not included in taxable income, but may be subject to gift tax. Restricted gifts used for capital improvements may not be included in taxable income if certain conditions are met, in which case they would reduce the taxable basis of the capital improvements. Further, if contributions to hospitals are not eligible for a tax deduction, it is assumed that most donors would choose other qualified organizations. For these reasons, contributions are excluded from the estimate of corporate taxable income.

State and local taxes

Many hospitals would also lose their state and local tax exemptions if they no longer qualified for federal tax exemption. Thus, estimates of the potential sales tax on business inputs and of potential property taxes on tax-exempt hospitals were incorporated in the federal and state tax calculations as deductions from taxable income.¹⁵ Increased state corporate income taxes also would be deductible against federal taxable income, and this factor also is reflected in our analysis.

Items not considered for analysis

The actual federal revenue forgone is likely to be less than the estimate above for the following reasons:

- ▶ Potential federal tax credits, such as enterprise zone and work opportunity tax credits, and special deductions, such as accelerated depreciation, are not included in this analysis due to lack of necessary information;
- ▶ Routine tax planning could result in hospitals retaining less earnings and thus earning less future investment income;
- ▶ Tax net operating losses that remained at the end of 2022 could be used by some hospitals to offset future taxable income; and
- ▶ Some tax-exempt hospitals already pay unrelated business income tax on a portion of their income.¹⁶

<https://www.usbank.com/financialiq/improve-your-operations/industry-insights/maximizing-your-deductions-section-179-and-bonus-depreciation.html#:~:text=The%20rules%20allowed%20Bonus%20Depreciation,reduced%20to%2060%25%20for%202024.>

¹⁵ Council on State Taxation, Total State and Local Business Taxes: Nationally 1980-2019 and by State 2000-2019, October 2020. The methodology used by Ernst & Young in this study was used for the state-by-state hospital estimates of sales tax on business inputs and property taxes.

¹⁶ For example, for tax year 2013, there were 393 Forms 990-T filed that paid a total of \$52 million in unrelated business income tax that was classified as "Healthcare and social assistance". This likely does not account for all unrelated

The estimates do not account for the effects of these issues.

Final summary

Overall, the community benefits of Indiana tax-exempt hospitals provided exceeded the value of their tax exemptions by approximately \$793 million in tax year 2022. Total benefits to the community exceeded the value of tax exemptions by \$2.3 billion.

Together, the Indiana tax-exempt hospitals received tax exemptions totaling approximately \$1.6 billion in tax year 2022. When taking into consideration losses these hospitals would be able to claim to offset federal corporate income taxes and Indiana's corporate adjusted gross income taxes as a result of expenses in excess of revenue, this total would drop to \$1.3 billion.

The largest tax exemptions were approximately \$578 million from real property tax, \$571 million from tangible property tax, and \$283 million from Indiana sales tax. The hospitals also received exemptions of about \$193 million in tax exempt financing and about \$3 million in federal unemployment tax.

business income taxes paid by hospitals, as taxes paid may have been classified under a different category, such as "retail trade" for gift shop sales. Tax year 2013 is the most recent year of reporting for this statistic. Source: Internal Revenue Service Statistics of Income (SOI) Tax Stats – Exempt Organizations' Unrelated Business Income (UBI) Tax Statistics, October 2016

Appendix

Methodology

Aggregate data from audited financial statements was used to analyze reported book income, certain potential book/tax differences, and tax-exempt financing. For entities within systems falling partially outside of Indiana, we distributed tax-exempt bonds based on Indiana entities' portion of total revenue.

EY analyzed three tax provisions that provide a federal exemption for tax-exempt hospitals:

- 1) Federal corporate income tax exemption;
- 2) Tax-exempt bond financing; and
- 3) Federal unemployment tax-exemption

In addition, EY analyzed four tax provisions that provide a state or local exemption for tax-exempt hospitals:

- 1) State corporation business tax exemption;
- 2) State sales tax exemption;
- 3) Local real property tax exemption; and
- 4) Local tangible property tax exemption

Of note, in our analysis, only tax-exempt bond financing and the federal unemployment tax-exemption result in forgone federal revenue. In addition, only exemptions for local real property tax, local tangible property tax, and state sales taxes result in forgone state and local revenue. This is because the tax-exempt hospitals in our analysis generally experience annual income losses due to expenses in excess of revenue. As such, if their income were taxable at the federal and state level, the hospitals would be able to claim losses on future year income tax statements. Consequently, the tax-exempt hospitals' operating losses would not generate federal corporate income taxes or Indiana corporate adjusted gross income taxes.

The estimates in this report reflect the upper bound of the potential values of the federal, state, and local tax exemptions for two reasons:

- 1) Some hospitals may qualify for tax exemption due to their educational or religious nature, in addition to their charitable nature. In the absence of a tax exemption for charitable hospitals, certain institutions could continue to be exempt for other reasons.
- 2) Certain tax exemptions, deductions, and credits provided by federal, state, and local tax codes and regulations are not reflected in this analysis due to a lack of necessary information, such how hospitals would change their structure or behavior to reduce their taxable income, if they were subject to tax.

Limitations of analysis

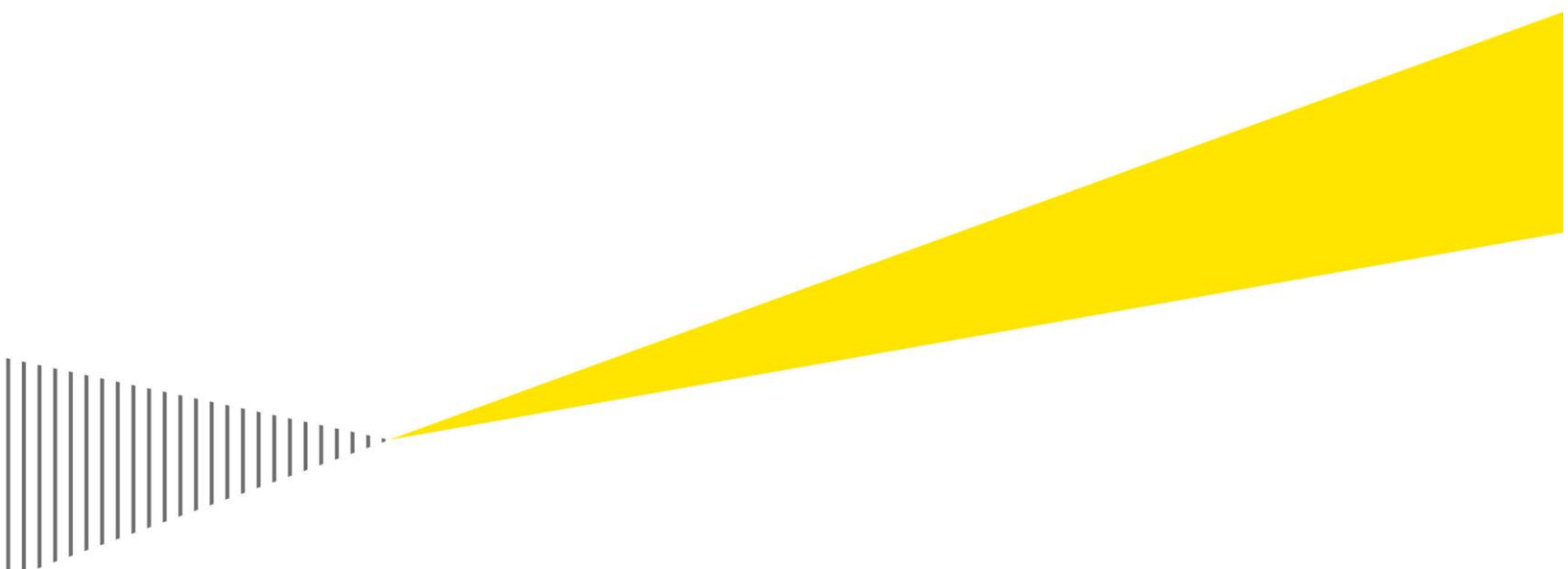
The estimates of the value of Indiana tax-exempt hospitals' tax exemptions are made for tax year 2022, which may not be representative of past or future years. In particular, the COVID-19 pandemic may still have had an impact on this year that caused it to vary systematically from other years. In addition, the estimates are sensitive to the following limitations and estimating conventions:

- ▶ This high-level analysis is intended to provide the general magnitude of the tax exemptions from the current tax-exempt status of tax-exempt hospitals within Indiana. This is a static, non-behavioral calculation of the value of the current tax exemption. The estimates assume no behavioral changes on the part of the hospitals, although some behavioral changes would likely occur if the hospitals were to become taxable. If subject to taxation, organizations might have an incentive to take advantage of existing tax deductions, other exemptions, and tax credits to reduce the cost of their federal, state, and local tax liabilities. For example, a hospital could take advantage of available tax credits to reduce its income tax liability.
- ▶ 501(c)(3) tax-exempt organizations, including tax-exempt hospitals, are eligible to receive tax-deductible charitable contributions. If donations to tax-exempt hospitals were not deductible, many donors would likely donate to other charitable organizations instead. Because the tax-exempt status of hospitals results in a tax benefit to their donors, rather than to the hospitals, the value of this benefit is not included in this calculation. However, if donations to tax-exempt hospitals were no longer deductible to the donors, future endowments may be lower, with reduced taxable investment income and lower income tax liabilities. This potential effect has not been considered in our analysis.
- ▶ Our analysis is based on information supplied to EY by Indiana tax-exempt hospitals and IRS Forms 990, Schedule H data. EY did not perform an independent audit of the data used in this analysis and therefore makes no representations as to the accuracy of those data. Additionally, not all data was available in detail for all respondents. In these cases, EY based its estimates on the total revenue of a tax-exempt hospital as a percentage of the total revenue of its specific hospital system.

Community benefits of tax-exempt hospitals in Indiana for tax year 2022

Prepared for the Indiana Hospital Association

January 2025



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Overview

This report provides an estimate of the community benefit expenses of Indiana's not-for-profit, tax-exempt hospitals ("tax-exempt hospitals"), as well as these benefits as a percentage of the hospitals' total expenses.¹

As part of their charitable missions, in tax year 2022 Indiana tax-exempt hospitals provided community benefits totaling over \$2.4 billion in expenses. On average, the total community benefit provided by Indiana tax-exempt hospitals represented 9.4% of their total expenses in tax year 2022. When considering non-traditional community benefits, the benefit to the community totals almost \$3.9 billion, or 14.9% of total expenses.

This report uses IRS Forms 990, Schedule H data to present the types of community benefits provided by these tax-exempt hospitals, including their total amount of community benefit and that community benefit's percentage of their total expenses. Community benefits provided may include financial assistance, Medicaid, and other means-tested government program expenses, community health improvement services and other community benefit operations, research, health professions education, subsidized health services, and in-kind contributions.

Community benefits of tax-exempt hospitals within Indiana, tax year 2022

This section compares community benefits (i.e., sections 7a – 7k on Schedule H of IRS Forms 990 as presented in the prior sections) and community benefits as a percentage of total expenses for a respective year. In tax year 2022, Indiana tax-exempt hospitals provided over \$2.4 billion in total community benefits, representing 9.4% of total hospital expenses (\$25.8 billion).²

Indiana tax-exempt hospitals provided nearly \$1.8 billion in assistance to means-tested populations, accounting for 6.9% of total hospital expenses. The tax-exempt hospitals also provided \$646 million in other community benefits, including community health improvement services and community benefit operations, health professions educations, research, subsidized health services and cash and in-kind contributions. These other community benefits account for an additional 2.5% of hospital expenses.

¹ The Indiana Hospital Association has 193 acute care hospitals and systems, of which 96 are tax-exempt entities, 63 are for-profit taxable entities, and 34 are governmental entities. Our analysis considers Schedule Hs for 64 distinct EINs affiliated with 82 tax-exempt hospitals across 20 hospital systems. Certain hospitals and types of operations (e.g., rehabilitation) are not required to fill out the IRS Form 990 Schedule H, though they might be considered to benefit the community through their affiliation with their broader hospital system. The analysis of community benefits excludes any standalone hospital without a Schedule H and the portion of any hospital systems located outside of Indiana.

² Source: Total expenses are based on total reported expenses on IRS Forms 990. Separately, based on EY calculations from the hospitals' audited financial statements, total expenses were \$31.1 billion in 2022.

Table 1 shows the net expenses corresponding with financial assistance and certain other community benefits as reported on IRS Forms 990, Schedule H for tax year 2022, as well as each of these community benefit expenses as a percentage of total hospital expenses.

Table 1. Tax-exempt hospitals' community benefits in tax year 2022, by type of benefit (\$ in millions)

	Community benefit expenses	Percentage of total expenses
Part I. Financial assistance and community benefits		
7a. Financial assistance at cost	\$289.5	1.1%
7b. Medicaid shortfall	\$1,441.9	5.6%
7c. Costs of other means-tested government programs	\$42.6	0.2%
7d. Financial assistance and means-tested	\$1,774.0	6.9%
7e. Community health improvement services and benefit ops.	\$182.2	0.7%
7f. Health professions education	\$190.4	0.7%
7g. Subsidized health services	\$223.6	0.9%
7h. Research	\$8.1	0.0%
7i. Cash and in-kind contributions for community benefit	\$41.8	0.2%
7j. Total "other benefits" (categories 7e-7i above)	\$646.0	2.5%
7k. Total community benefit (lines 7d and 7j)	\$2,420.0	9.4%

Note: Figures may not sum due to rounding.

Source: EY tabulations of Indiana tax-exempt hospitals' community benefit expense reported on IRS Forms 990, Schedule H.

Non-traditional community benefits

Indiana tax-exempt hospitals incurred an additional 5.6% of total hospital expenses for non-traditional community benefit activities including 0.1% for community building activities and 5.4% for bad debt attributable to financial assistance and Medicare shortfalls. When considering Parts II and III in addition to those items generally considered to be community benefits in Part I, total benefits to the community were nearly \$3.9 billion, or 14.9% of total expenses.

Table 2. Tax-exempt hospitals' total benefits to the community, including community building, bad debt, and Medicare, in tax year 2022, by type of benefit (\$ in millions)

	Community benefit expenses	Percentage of total expenses
Part I. Financial assistance and community benefits		
Part I, 7k. Total (Lines 7d and 7j)	\$2,420.0	9.4%
Part II. Community building activities		
Line 10. Community building activities	\$34.5	0.1%
Part II Total (Line 10)	\$34.5	0.1%
Part III. Bad debt and Medicare		
Line 3. Bad debt attributable to financial assistance	\$20.7	0.1%
Line 7. Medicare surplus/shortfall	\$1,381.8	5.4%
Part III Total (Lines 3 and 7)	\$1,402.5	5.4%
Total benefits to the community (Parts I, II, & III)	\$3,857.0	14.9%

Note: Figures may not sum due to rounding.

Source: EY tabulations of Indiana tax-exempt hospitals' community benefit expense reported on IRS Forms 990, Schedule H.

Although not typically included in analyses of community benefits, community building activities address community unmet health needs. In addition, the bad debt expense and the losses from

Medicare shortfalls represent the cost of services for which the hospitals are not compensated. As such, they are similar to the list of items in the traditional set of community benefits.

Community-Building Activities

In 2022, hospital systems and individual hospitals spent 0.1% of their total expenses on community-building activities for a total of \$34.5 million. Community-building activities take many forms:

- ▶ Public health initiatives, such as disaster and public health emergency readiness and participation in coalitions to foster collaboration across healthcare entities and to enhance public health infrastructure
- ▶ Community building, such as early childhood initiatives, investing in parks, housing, and public infrastructure, and supporting education
- ▶ Environmental improvements to protect the community from environmental hazards
- ▶ Workforce development programs such as promoting equitable and inclusive job creation

These activities often promote regional health by offering direct and indirect support to communities with unmet health needs. These include patients who are indigent, uninsured, underprovided for, or geographically isolated from health care facilities.

Bad debt expense

In tax year 2022, 22% of hospitals and hospital systems reported bad debt expense attributable to financial assistance, for a total of \$20.7 million.³ The average bad debt expense attributable to financial assistance reported was 0.1% of total expenses in 2022. Some patients unable to pay for their medical care do not complete hospitals' financial assistance processes. Consequently, hospitals classify unreimbursed care for those patients as bad debt expense. Most hospitals and systems report that some portion of their bad debt expense would qualify as a benefit to the community as financial assistance due to the low income of the patients.

Medicare shortfall

In 2022, 68% of tax-exempt hospital and hospital systems in Indiana reported having Medicare shortfalls. Medicare reimbursement shortfalls occur when the Federal government reimburses the hospitals less than their costs for treating Medicare patients. The net shortfall⁴ accounted for an average 5.4% of total hospital expense, with a total net shortfall of \$1.4 billion across all the hospitals studied.

³ Tabulated based on form 990 submissions. Some 990 submissions contain more than one hospital.

⁴ Some hospitals have a surplus. Overall, though, there is a net shortfall for hospitals located in Indiana.

On their Schedule Hs, most hospitals described why their Medicare shortfall should be treated as community benefit:

- ▶ Non-negotiable Medicare rates are sometimes out-of-line with the true costs of treating Medicare patients.
- ▶ By continuing to treat patients eligible for Medicare, hospitals reduce the public-sector burden related to funding medical care. The IRS has acknowledged that lessening the government burden associated with providing Medicare benefits is a charitable purpose.⁵
- ▶ Additionally, hospitals pointed to IRS Rev. Rul. 69-545 in their explanation of Medicare shortfall as a community benefit. IRS Rev. Rul. 69-545 states that if a hospital serves patients with government health benefits, including Medicare, then this is an indication that the hospital operates to promote the health of the community.

Final summary

In tax year 2022, Indiana tax-exempt hospitals provided over \$2.4 billion in total community benefits, representing 9.4% of total hospital expenses. When also considering non-traditional community benefit, total benefits to the community were nearly \$3.9 billion, or 14.9% of total expenses.

⁵ IRS Notice 2011-20.

Appendix

Methodology

Many of the benefits that hospitals provide to their communities are captured by IRS Forms 990 on their Schedule H. Hospitals provide financial assistance and absorb underpayments from means-tested government programs such as Medicaid and incur losses due to costs such as unreimbursed Medicare expenses that qualify as financial assistance. In addition, they offer programs and activities to:

- ▶ Improve community and population health
- ▶ Underwrite medical research and health professions education
- ▶ Subsidize high-cost essential health services

EY reviewed IRS Forms 990 for tax year 2022 for 81 tax-exempt hospitals in Indiana. Data was collected and tabulated for the following sections of the Schedule H form:⁶

- ▶ Part I line 7a-k on financial assistance and certain other community benefits (these are the traditional community benefit items)
- ▶ Part II line 10
- ▶ Part III lines 3 and 7 on bad debt and Medicare

Data reported on the Indiana tax-exempt hospitals' IRS Forms 990, Schedule H are reported at the hospital or hospital system level. For our analysis, the totals for each line item are calculated as a percentage of the respective hospital or hospital systems' total annual expenses in Indiana. Overall, the net expense for community benefit programs is calculated as a percentage of hospitals' or systems' total annual expenses as reported on the Forms 990.

Limitations

Total amounts of community benefits and total community benefit as a percentage of expenses from the IRS Forms 990 provide information on the financial costs and forgone revenue incurred by acute care hospitals and systems in providing benefits. However, they do not measure the overall tangible and intangible benefits of improving their communities' health and economic well-being. Hospitals provide the Internal Revenue Service (IRS) with detailed descriptions of their community benefit programs as part of their filing. These descriptions often provide additional information beyond the financial information presented on the forms.

⁶ The detail of each of these Parts is available on the Form 990 Schedule H 2022 located: <http://www.irs.gov/pub/irs-prior/f990sh--2022.pdf>

Community Benefit Descriptions

On the IRS Form 990, Schedule H, all net benefit expenses are calculated on a cost basis, rather than a charge basis. For details on the calculations, please see the instructions for the Schedule H. Below are short descriptions of each of the community benefit items:

1. **Financial Assistance at cost:** Free or reduced price care provided to individuals who qualify for the financial assistance policy. Expense is net of any offsetting revenue (e.g., payments received from an uncompensated care pool or DSH program in the organization's home state are intended primarily to offset the cost of financial assistance).
2. **Medicaid shortfall:** This is the uncompensated cost of providing care to Medicaid patients. This is on a cost-basis, so if a hospital charges \$1000 for a procedure that costs the hospital \$500 to perform and Medicaid only pays \$300 for the procedure, the shortfall is \$200, meaning the hospital loses \$200 for performing the procedure rather than the loss of revenue.
3. **Other Means Tested shortfall:** This is similar to Medicaid but is for other government-sponsored programs provided at the state and local levels; "means-tested government program" is a government health program for which eligibility depends on the recipient's income or asset level.
4. **Community Health Improvement Services:** Activities or programs, subsidized by the health care organization, carried out or supported for the express purpose of improving community health. Such services don't generate inpatient or outpatient revenue, although there may be a nominal patient fee or sliding scale fee for these services. Marketing activities are not included.
5. **Health Professions Education:** Educational programs that result in a degree, a certificate, or training necessary to be licensed to practice as a health professional, as required by state law, or continuing education necessary to retain state license or certification by a board in the individual's health profession specialty. It doesn't include education or training programs available exclusively to the organization's employees and medical staff or scholarships provided to those individuals. However, it does include education programs if the primary purpose of such programs is to educate health professionals in the broader community.
6. **Subsidized Health Services:** Clinical services provided despite a financial loss to the organization. In order to qualify as a subsidized health service, the organization must provide the service because it meets an identified community need.
7. **Research:** Research means any study or investigation the goal of which is to generate increased generalizable knowledge made available to the public. The organization cannot include direct or indirect costs of research funded by an individual or an organization that isn't a tax-exempt or government entity.
8. **Cash and In-kind Contributions:** Contributions made by the organization to health care organizations and other community groups restricted, in writing, to one or more of the community benefit activities noted above.