AMERICAN HOSPITAL ASSOCIATION
UNCOMPENSATED HOSPITAL CARE COST
FACT SHEET

November 2009

Each year, the American Hospital Association (AHA) publishes aggregate information on the level of uncompensated care – care provided for which no payment is received – delivered in U.S. hospitals. The data used to generate these numbers come from the AHA's Annual Survey of Hospitals, which is the nation's most comprehensive source of hospital financial data. This fact sheet provides the definition of uncompensated care and technical information on how this figure is calculated on a cost basis. It also describes how the American Institute of Certified Public Accountants' (AICPA) accounting changes to bad debt and free care are currently handled in the Survey to ensure the consistency of uncompensated care numbers.

Please note, this information includes only two components within the universe of benefits that hospitals provide to their communities. In a separate fact sheet, AHA has calculated the cost of underpayment by Medicare and Medicaid. While these two fact sheets contain important information, they do not account for the many other services and programs that hospitals provide to meet identified community needs.

DEFINING UNCOMPENSATED CARE COSTS

What is Uncompensated Care?

Uncompensated care is an overall measure of hospital care provided for which no payment was received from the patient or insurer. It is the sum of a hospital's "bad debt" and the charity care it provides. Charity care is care for which hospitals never expected to be reimbursed. A hospital incurs bad debt when it cannot obtain reimbursement for care provided; this happens when patients are unable to pay their bills, but do not apply for charity care, or are unwilling to pay their bills. Uncompensated care excludes other unfunded costs of care, such as underpayment from Medicaid and Medicare.

Bad Debt and Charity Care

AHA combines the hospital's bad debt and charity care costs to arrive at the hospital's total costs of unreimbursed care provided to medically indigent and underinsured patients. In terms of accounting, **bad debt** consists of services for which hospitals anticipated but did not receive payment. **Charity care**, in contrast, consists of services for which hospitals neither received, nor expected to receive, payment because they had determined, with the assistance of the patient, the patient's inability to pay. In practice, however, hospitals often have difficulty in distinguishing bad debt from charity care.

Hospitals provide varying levels of charity care, which must be budgeted for and financed by the hospital depending on the hospital's mission, financial condition, geographic location and other factors. Hospitals typically use a process to identify who can and cannot afford to pay, in advance of billing, in order to anticipate whether the patient's care needs to be funded through an alternative source, such as a charity care fund. Hospitals also attempt to identify patients who are unable to pay during the billing and collection process. Depending on a variety of factors, including whether a patient self-identifies as medically indigent or underinsured in a timely manner, care may be classified as either charity care or bad debt. Bad debt is often generated by medically indigent and/or uninsured patients, making the distinctions between the two categories arbitrary at best. Therefore, it is reasonable to consider bad debt as a component of hospitals' total cost of care to medically indigent and underinsured patients.

Uncompensated care data are sometimes expressed in terms of hospital charges, but charge data can be misleading, particularly when comparisons are being made among types of hospitals, or hospitals with very different payer mixes. **For this reason, AHA data on hospitals' uncompensated care are expressed in terms of costs.** It should be noted that the uncompensated care figures do not include Medicaid or Medicare underpayment costs.

CALCULATING UNCOMPENSATED CARE COSTS

Uncompensated care is first calculated on a hospital by hospital basis. Bad debt and charity care are reported as charges in the Annual Survey. These two numbers are added together and then multiplied by the hospital's cost-to-charge ratio, or the ratio of total expenses to gross patient and other operating revenue.

- Uncompensated Care Charges = Bad Debt Charges + Charity Care Charges

- Cost-to-charge Ratio = $\dfrac{\text{Total Expenses Exclusive of Bad Debt}}{\text{Gross Patient Revenue + Other Operating Revenue}}$

- Uncompensated Care Costs = Uncompensated Care Charges x Cost-to-charge Ratio

Combining bad debt and charity care to arrive at the hospital's total uncompensated care cost allows for comparability across hospitals. While the 1990 (AICPA) accounting changes used to classify these costs (described below) result in some shifting between bad debt and charity care, they are not expected to influence the total reported cost of uncompensated care. The total reported national uncompensated care cost value is calculated by adding together the individual uncompensated care cost values across all hospitals.

AICPA CHANGES AND THE ANNUAL SURVEY

In 1990, AICPA made important changes to its *Audit and Accounting Guide*, which impact bad debt and charity care. The Guide is the industry standard for health care financial reporting and audits.

Prior to 1990, hospitals reported both bad debt and charity care as deductions from revenue. The new rules require different reporting of the two items. For purposes of external financial statements, charity care is no longer a reported item. Hospitals must now report only net revenue. It is presumed that hospitals will continue to account internally for charity care as a deduction from gross revenue. Bad debt, in contrast, must be reported as an expense item (it may be either separately reported or reported with administrative services or other adjustments) and is no longer deducted from gross revenue. The AHA uncompensated care data are calculated to assure their comparability to data presented before the 1990 AICPA changes.

Please refer questions regarding this fact sheet to: Caroline Steinberg, AHA Policy Division (202-626-2329) or Molly Collins Offner, AHA Policy Division (202-626-2326).

National Uncompensated Care Based on Cost*: 1980-2008 (in Billions), Registered Community Hospitals

Year	Hospitals	Uncompensated Care Cost	% of Total Expenses
1980	5828	$3.9	5.1%
1981	5812	$4.7	5.2%
1982	5796	$5.3	5.1%
1983	5782	$6.1	5.3%
1984	5757	$7.4	6.0%
1985	5729	$7.6	5.8%
1986	5676	$8.9	6.4%
1987	5597	$9.5	6.2%
1988	5499	$10.4	6.2%
1989	5448	$11.1	6.0%
1990	5370	$12.1	6.0%
1991	5329	$13.4	6.0%
1992	5287	$14.7	5.9%
1993	5252	$16.0	6.0%
1994	5206	$16.8	6.1%
1995	5166	$17.5	6.1%
1996	5134	$18.0	6.1%
1997	5057	$18.5	6.0%
1998	5015	$19.0	6.0%
1999	4956	$20.7	6.2%
2000	4915	$21.6	6.0%
2001	4908	$21.5	5.6%
2002	4927	$22.3	5.4%
2003	4895	$24.9	5.5%
2004	4919	$26.9	5.6%
2005	4936	$28.8	5.6%
2006	4927	$31.2	5.7%
2007	4897	$34.0	5.8%
2008	5010	$36.4	5.8%

Source: Health Forum, AHA Annual Survey Data, 1980-2008

*The above uncompensated care figures represent the estimated ***cost*** of bad debt and charity care to the hospital. This figure is calculated for each hospital by multiplying uncompensated care charge data by the ratio of total expenses to gross patient and other operating revenues. The total uncompensated care cost is arrived at by adding together all individual hospital values. The uncompensated care figure does not include Medicaid or Medicare underpayment costs, or other contractual allowances. Moreover, the figure does not take into account the small number of hospitals that derive the majority of their income from tax appropriations, grants and contributions.

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