

## Health Affairs Press Release

### **Four Views on Nonprofit Healthcare Performance, Public Accountability and Tax Exemption**

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#### **Researchers Find That Impact Of Nonprofits, And Grounds For Tax Exemption, Range Far Beyond Care For Indigent**

*Health Affairs Authors Argue That States Should Help Each Community Decide  
On Local Accountability Requirements For Nonprofits*

**Bethesda, MD** -- By itself, the amount of indigent care provided by nonprofit hospitals and other nonprofit health care entities does not justify their tax exemptions, but these institutions often provide other, less easily measured benefits that vary from service to service and from community to community.

That's the conclusion reached by Mark Schlesinger and Bradford Gray in the lead article of a four-paper package published today on the *Health Affairs* Web site. "There are many ways that providers can influence the health of communities. Thus, restricting the rationale for tax exemption to indigent care, as done in some states and favored by some policy analysts, is a misguided approach to improving community health," say Schlesinger, a professor of health policy at Yale University, and Gray, a principal research associate at the Urban Institute.

At a time when tax exemption for nonprofits is at the center of controversy in state legislatures, Congress, and the courts, Schlesinger and Gray provide a comprehensive look at whether and how nonprofits behave differently from their for-profit, taxpaying counterparts. **The two researchers find that "the major institutional transformations of American medicine over the past few decades seem not to have vitiated the distinctiveness of nonprofit ownership."** They report: "Our literature review found some differences between nonprofits and for-profits regarding cost, quality, or accessibility for every service studied.

"However, the effects of ownership manifest in different ways for different services," Schlesinger and Gray note. For example, "there is overwhelming evidence that for-profit nursing homes have lower costs and greater efficiency [than nonprofit nursing homes]. ... Among hospitals, however, costs and efficiency results are more mixed but predominantly favor nonprofits." Schlesinger and Gray assert that earlier studies have provided conflicting findings regarding the effects of ownership form on health care entities because scholars have "carelessly combine[d] findings based on different health services or performance measures."

Some ownership effects appear to apply more consistently across services, say Schlesinger and Gray. As a rule, nonprofits “appear more trustworthy in delivering services”: They are “less likely to make misleading claims, to have complaints lodged against them by patients, and to treat vulnerable patients differently from other clientele.” Nonprofit entities are also less aggressive about marking up prices and otherwise maximizing revenues, and they are “typically the incubators of innovation.”

### **A Mix Of For-Profit And Nonprofit Ownership Is Needed In Local Markets, Say *Health Affairs* Authors**

Not all ownership-related effects constitute clear advantages for nonprofits. For example, “nonprofit health care providers are slower to react to change, expanding capacity less quickly when demand rises and dropping services or withdrawing from markets less frequently when profitability declines,” report Schlesinger and Gray, who say that this can help or hurt consumers, depending on the circumstances. The researchers conclude that a mix of both for-profits and nonprofits is appropriate.

The evidence available, while sketchy, suggests that “even a small for-profit presence (a share of 10 percent or less in the local market) induces greater efficiency among nonprofit competitors. The nonprofit presence required to induce greater trustworthiness in for-profit competitors appears to be larger -- market shares of at least 20–30 percent,” Schlesinger and Gray report. **“Because the spillover benefits of mixed ownership occur at the local level, it is there that an appropriate balance should be maintained. This contrasts dramatically with the current distribution of ownership for many services, in which many local markets are exclusively nonprofit or for-profit in character.”**

Schlesinger and Gray reject what they say are the “two competing approaches to achieving accountability for nonprofit health care.” First, the two researchers argue that neither states nor the federal government should “establish standard criteria against which nonprofits’ performance would be evaluated.” This approach, which “seems to be the thrust of current congressional inquiries into nonprofit medical care,” is “excessively inflexible, substituting decisions by state and federal policymakers or regulators for choices better made in local communities.”

Schlesinger and Gray also criticize as inadequate “policies adopted by some states that require nonprofits to assess community needs and report publicly on their efforts to meet them.” They point out that “reporting requirements are not in themselves sufficient, since reports are famous for sitting unread on shelves” and “communities might lack the capacity to imagine forms of community benefit . . . or to influence nonprofits’ practices.”

In place of these two approaches, Schlesinger and Gray argue for an “approach to accountability that fosters community involvement, supported by a state-financed infrastructure.” First, “states should adopt guidelines that identify the full range of plausible community-benefit activities associated with different health services.” Second, states should “provide communities with resources to organize and deliberate about these community-benefit activities. Smaller communities might pool their capacity to gain greater influence over health care organizations that serve larger market areas.”

## **Horwitz Defends Freedom Of Nonprofit Actors; Hyman and Sage, And Bloche, Push For Subsidizing Performance, Not Ownership**

In a Perspective on Schlesinger and Gray's article, Jill Horwitz argues that "mandating the use of private, charitable property for narrowly defined community purposes, even in exchange for [tax] exemption, violates the goals of charities law. Nonprofit institutions are meant to allow private actors, within broad constraints, to create and implement their own ideas of what counts as the public good."

The University of Michigan law professor adds that Schlesinger and Gray's "invocation of deliberation and community consultation is nice, but what legally enforceable duties do the authors envision? Without more detail, it is hard to imagine how a list of community-generated benefits would have enough bite to matter, yet not rise to the level of government control [that Schlesinger and Gray] legitimately fear." Horwitz adds, "Much of what we want our health care organizations to do is hard to define and hard to measure. There is no reason to assume that progressively passing authority down along levels of government -- from federal to state to local, or even all the way down to community groups -- will make it easier to decide which interests should prevail."

David Hyman, a professor of law and medicine at the University of Illinois-Champaign, and William Sage, a professor of law at Columbia University, emphasize that nonprofit status and tax exemption are two different things. "Schlesinger and Gray's analysis makes it clear that entity status matters," they say, but "the more difficult policy questions are whether it matters enough to justify a sizable subsidy and whether it makes more sense to use an undifferentiated subsidy tied to status (current practice) or a graduated subsidy tied to quantifiable, objective measures of performance." They conclude that public policy should move from an "all-or-nothing" subsidy tied to nonprofit status to "an approach that ties the amount of the subsidy to the satisfaction of specific quantifiable and objective measures of performance."

Hyman and Sage are also "quite skeptical" of Schlesinger and Gray's suggestion that policymakers in each market should attempt to specify the optimal balance of nonprofit and for-profit entities." They declare that "it will be nigh on impossible to develop a command-and-control infrastructure that can make the subtle regulatory judgments that Schlesinger and Gray propose. Decades of experience with certificate-of-need proceedings demonstrate that processes of this sort are prone to interest-group manipulation and often will be used to anticompetitive ends."

**Gregg Bloche calls tax exemption for nonprofit hospitals "a historical relic without a plausible, current rationale." He argues that the case for tax exemption lost its logical underpinnings during the first half of the last century, as hospitals evolved from refuges for the sick poor into commercial institutions that treat mainly paying patients.** Nonprofit hospitals have campaigned to preserve their exemption by arguing that they deliver greater "community benefit," but, Bloche asserts, "there is no evidence that the purported difference in community benefit between the nonprofit and for-profit sectors approaches the exemption's cost." Even if the difference in community benefit exceeds the exemption's cost, this argument is unpersuasive, he contends, absent a showing that exemption "buys" this difference in performance. The claim that nonprofit status, in itself, explains this difference weighs against the exemption. "Unless a tax expenditure procures a package of

public benefits worth more than the tax revenues forgone, it squanders our shared resources,” writes Bloche, a Georgetown University law professor and visiting fellow at the Brookings Institution.

Instead of granting tax exemption to nonprofits per se, Bloche argues, government should adopt a pay-for-performance approach to both charity care and community benefit: “Public spending, including tax subsidies, should support development of electronic medical records, evidence-based practice protocols, better ways to assess and compare hospitals’ and health plans’ clinical outcomes, and other quality-enhancing tools.”

You can read Schlesinger and Gray’s article and the three Perspectives at [http://www.healthaffairs.org/alert\\_link.php?url=http://content.healthaffairs.org/cgi/content/full/hlthaff.25.w287/DC3&t=h&id=369](http://www.healthaffairs.org/alert_link.php?url=http://content.healthaffairs.org/cgi/content/full/hlthaff.25.w287/DC3&t=h&id=369)