STATE OF FLORIDA et al v. UNITED STATES DEPARTMENT OF HEALTH AND HUMAN SERVICES et al Doc. 83 Att. 22

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# Nonprofit Hospitals and the Provision of Community Benefits

December 2006

The Congress of the United States ■ Congressional Budget Office

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## Introduction and Summary

The various tax exemptions provided to nonprofit hospitals have come under scrutiny by policymakers, with the central concern being whether those hospitals provide community benefits that justify forgone government tax revenues. In this paper, the Congressional Budget Office (CBO) measures the provision of certain community benefits and compares nonprofit hospitals with for-profit hospitals. For-profit hospitals do not receive tax exemptions and are not required to meet community-benefit standards; the level of community benefits provided by for-profit hospitals serves, therefore, as a useful benchmark against which to compare nonprofit hospitals. The analysis also examines the provision of community benefits by nonfederal government hospitals.[1]

Although nonprofit hospitals must provide community benefits in order to receive tax exemptions, there is little consensus on what constitutes a community benefit or how to measure such benefits. For the purposes of this analysis, community benefits include the provision of uncompensated care, the provision of services to Medicaid patients, and the provision of certain specialized services that have been identified as generally unprofitable. Those services were selected because they benefit the community but are not typically considered financially rewarding.

In general, the comparisons of nonprofit and for-profit hospitals yielded mixed results. CBO found that, on average, nonprofit hospitals provided higher levels of uncompensated care than did otherwise similar for-profit hospitals. Among individual hospitals, however, the provision of uncompensated care varied widely, and the distributions for nonprofit and for-profit hospitals largely overlapped. Nonprofit hospitals were more likely than otherwise similar for-profit hospitals to provide certain specialized services but were found to provide care to fewer Medicaid-covered patients as a share of their total patient population. On average, nonprofit hospitals were found to operate in areas with higher average incomes, lower poverty rates, and lower rates of uninsurance than for-profit hospitals.

### Provision of Uncompensated Care

The level of uncompensated care provided by community hospitals is examined here for hospitals located in five states—California, Florida, Georgia, Indiana, and Texas—using data from 2003 (the latest year for which

1. Hospitals are identified as nonprofit, for-profit, or governmental on the basis of classifications reported by hospitals in the "control type" variable in the Medicare Hospital Cost Report. According to the control type variable, "nonprofit" refers to voluntary nonprofit (with or without church affiliation); "for-profit" refers to proprietary hospitals owned by individuals, corporations, partnerships, or other entities; and "government" refers to state, county, city-county, city, hospital-district, or other governmental entities (federal hospitals were excluded from the analysis).

such data are available).[2] "Uncompensated care" refers to the sum of charity care (services for which a hospital does not expect payment) and bad debt (services for which a hospital expects but does not collect payment). Although charity care is a better measure of the community benefits provided by a hospital, data limitations precluded CBO's analyzing charity care and bad debt separately.

The five selected states were chosen in part because sufficiently reliable data on uncompensated care were available in those areas. The data were provided to CBO by the Government Accountability Office (GAO) and were developed by GAO for use in its analyses of issues relating to the level of uncompensated care provided by different types of hospitals.[3] CBO's analysis expands on GAO's findings in several ways: first, regression techniques are used to calculate adjusted differences between nonprofit and for-profit hospitals in the provision of uncompensated care, taking into account hospital characteristics and the characteristics of local populations; and, second, the provision of Medicaid services and specialized services, such as emergency room care, are analyzed quantitatively.

CBO's five-state analysis of uncompensated care yielded the following key findings:

- In the five states analyzed, nonprofit hospitals provided a total of about $3 billion in uncompensated care, government hospitals provided more than $3 billion, and for-profit hospitals provided about $1 billion in uncompensated care. The difference in the total amount of uncompensated care provided by nonprofit and for-profit hospitals is largely attributable to the fact that nonprofit hospitals accounted for a much larger share of the hospital market than did for-profits.
- The average "uncompensated-care share"—the cost of uncompensated care as a share of hospitals' operating expenses—was much higher at government hospitals (13.0 percent) than at either nonprofit hospitals (4.7 percent) or for-profit hospitals (4.2 percent).
- Individual hospitals varied widely in their uncompensated-care shares. Although nonprofit hospitals, on average, have slightly higher uncompensated-care shares than for-profits (by 0.5 percentage points), the distributions of uncompensated-care shares among those two types of hospitals overlap to a large extent.
- When regression techniques were used to adjust for the hospitals' size and location and for the characteristics of the local populations, nonprofit hospitals were estimated to have an average uncompensated-care share that was 0.6 percentage points higher than that for otherwise similar for-profit hospitals. That estimated difference corresponds to nonprofit hospitals in the five selected states providing between $100 million and $700 million more in uncompensated care than would have been provided if they had been for-profits.[4]

## Provision of Medicaid-Covered Services

Medicaid's payment rates have, in general, been found to be somewhat below the costs that hospitals incur in providing Medicaid-covered services. Because providing hospital services to Medicaid patients is often unprofitable and serves a needy population, it can be thought of as a type of community benefit. Among all community hospitals nationwide, CBO found that the Medicaid share—Medicaid-covered days as a share of all patient

2. "Community hospitals" include nonfederal short-term general hospitals. This definition includes most hospital facilities but excludes, for example, federal hospitals run by the Veterans Administration, psychiatric hospitals, and long-term-care hospitals. Several of the key data sources used are Medicare administrative files. Therefore, only Medicare-certified community hospitals were included in the analyses in this paper. Throughout the text "all community hospitals" refers to all Medicare-certified community hospitals. The findings are referred to as representing the year 2003, but the data are actually taken from either 2003 or 2002. For the analysis of uncompensated care, which includes hospitals in only five states, the data for 57 percent of hospitals are from federal fiscal year (FFY) 2003, and those for 43 percent of hospitals are from FFY 2002. For convenience, 2003 is used to describe the findings because the majority of hospitals report data for FFY 2003. For consistency, the analysis for all community hospitals used the same data years that were used to analyze uncompensated care costs in the five states. The FFY 2003 data were used for all hospitals not in the five states. For the other analyses, which include hospitals in all of the states, 90 percent of hospitals had FFY 2003 data and 10 percent of hospitals had FFY 2002 data.

3. See Statement of David M. Walker, Comptroller General of the United States, before the House Committee on Ways and Means, published as Government Accountability Office, *Nonprofit, For-Profit, and Government Hospitals: Uncompensated Care and Other Community Benefits*, GAO-05-743T (May 26, 2005), available at www.gao.gov/new.items/d05743t.pdf.

4. The range of $100 million to $700 million represents the 90 percent confidence interval from the underlying statistical analysis.

days—was, on average, 1.5 percentage points lower among nonprofit hospitals than it was among for-profit hospitals (15.6 percent versus 17.2 percent). The Medicaid share was substantially higher among government hospitals (27.0 percent). When regression techniques were used to control for hospital characteristics, nonprofit hospitals were found to have adjusted Medicaid shares that were 1.3 percentage points lower than those of otherwise similar for-profit hospitals.

### Provision of Specialized Services

CBO also examined the share of hospitals of different ownership types that provide four specific types of specialized patient services: intensive care for burn victims, emergency room care, high-level trauma care, and labor and delivery services.[5] Each of those services addresses a community need and has been identified as being generally unprofitable. Among all community hospitals nationwide, emergency room care and labor and delivery services were both quite common, whereas few hospitals provided burn intensive care or high-level trauma care.

CBO found that nonprofit hospitals were more likely than for-profit hospitals to provide each of the four specialized services examined. After adjustment for hospital characteristics, nonprofit hospitals were found to be significantly more likely than for-profit hospitals to provide two of the four specialized patient services (emergency room care and labor and delivery services). Compared with otherwise similar for-profit hospitals, the share of nonprofit hospitals providing emergency room care was 3.8 percentage points higher, and the share providing labor and delivery services was 10.5 percentage points higher. CBO did not attempt to quantify the value to the community of the availability of those specialized services.

5. In CBO's analysis, a hospital provides "high-level trauma care" if it is a level 1 or level 2 adult trauma center (stand-alone pediatric trauma centers are not included). A hospital may be designated as a trauma center if it meets certain criteria developed by the American College of Surgeons. Trauma centers are assigned a level ranging from 1 through 5, with level 1 being the highest. To be designated a level 1 or level 2 trauma center, a hospital must "[provide] comprehensive trauma care" and must "have immediate availability of trauma surgeons, anesthesiologists, physician specialists, nurses, and resuscitation equipment." See Ellen J. MacKenzie and others, "National Inventory of Hospital Trauma Centers," *Journal of the American Medical Association*, vol. 289, no. 12 (March 26, 2003), pp. 1515-1522.

### The Value of Tax Exemptions for Nonprofit Hospitals

The Joint Committee on Taxation (JCT) recently examined the value to nonprofit hospitals and their supporting organizations of the major tax exemptions they receive from federal, state, and local governments. Together, the value of the various tax exemptions in 2002 was estimated to be $12.6 billion, with exemptions from federal taxes accounting for about half of the total and exemptions from state and local taxes accounting for the remaining half.

JCT also estimated the value of some of the tax exemptions for nonprofit hospitals located in the five states for which uncompensated-care data were available. In those five states, the exemptions from federal and state corporate income taxes, state and local sales taxes, and local property taxes were valued at $2.5 billion. (Two important categories of tax exemptions—tax-exempt-bond financing and the deductibility of charitable contributions—were included in the national totals but were not available for the five states and are not included in the five-state total.)

## Background

The hospital industry in the United States includes a mix of ownership forms. Nonprofit hospitals are the most common type, but for-profit and government hospitals also play substantial roles.[6] Of the 630,000 beds in Medicare-certified community hospitals in the United States in 2003, 68 percent were located in nonprofit hospitals, 16 percent were located in for-profit hospitals, and 15 percent were located in government (nonfederal) facilities.

This section of the analysis examines the differences between nonprofit hospitals and for-profit hospitals in their ownership structure, tax treatment, and the provision of collective goods. (Collective goods are defined as goods or services that, when used or consumed, generate well-

6. The terms "nonprofit" and "tax-exempt" (or "untaxed") are sometimes used interchangeably, but they are technically distinct. For the purposes of federal taxation, an organization may be deemed tax-exempt by meeting the requirements of section 501 of the Internal Revenue Code. Nonprofit status, on the other hand, is granted by state governments on the basis of criteria that vary from state to state. In CBO's analysis, hospitals that identify themselves as nonprofit in Medicare Hospital Cost Reports are assumed to be exempt from federal, state, and local taxes.