



CHAPTER HIGHLIGHTS

THE STATE OF NONPROFIT AMERICA

LESTER M. SALAMON *editor*

Chapter 2 Highlights HEALTH

Bradford H. Gray and Mark Schlesinger

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HEALTH *

By Bradford H. Gray and Mark Schlesinger

Nonprofit organizations have always played a critical role in the delivery of health care services in the United States, but financial, regulatory, and technological changes in recent decades pose unprecedented challenges to the nonprofit health sector. Authors Bradford H. Gray of the New York Academy of Medicine and Mark Schlesinger of Yale University argue that to sustain their place in the health care system, nonprofits must increase their efforts to demonstrate their distinctiveness in responding to community needs, while also finding ways to survive in an increasingly tough competitive marketplace.

This analysis is part of the broader assessment of *The State of Nonprofit America* coordinated by Dr. Lester M. Salamon of the Johns Hopkins University and published by the Brookings Institution Press in collaboration with the Aspen Institute.

Nonprofit health organizations face financial challenges resulting from growing competition from for-profit organizations, shifting government policies that formerly favored nonprofits, and changing policies by cost-conscious third-party purchasers such as Medicare, Medicaid, and private health insurers. Charitable contributions account for only a few percentage points of most nonprofit institutions' revenues, and the ability of these organizations to subsidize charity care and public goods from revenues generated from the sale of services has been constrained by the efforts of private and public purchasers to reduce the flow of dollars.

Gray and Schlesinger show that the nonprofit share of different fields within health care varies widely. Some fields, including acute care hospitals and hospices, are primarily nonprofit, while many others, including nursing homes and HMOs, are predominantly for-profit. A rapid shift toward for-profit ownership has taken place over the past two decades, with several fields (dialysis centers, rehabilitation hospitals, home health agencies, HMOs) shifting from nonprofit to for-profit dominance. But the growth in the for-profit share does not seem immutable. Gray and Schlesinger note that the nonprofit share of acute care hospitals has been stable at 60% since the mid-1960s, and that the nonprofit share increased among nursing homes since the mid-1980s and among psychiatric hospitals in the 1990s.

To explain these differences among fields, Gray and Schlesinger suggest that a life cycle of ownership exists in health care. Fledgling organizations that offer new services in response to changing needs or technological developments are mostly nonprofits, started with support from philanthropy, government grants, or existing nonprofit organizations. As the service gains legitimacy, more substantial government funding becomes available to pay for it. This attracts investor capital, and a for-profit sector develops, responding, thanks to its access to equity capital, more quickly than do the nonprofits to the increased demand. However, the for-profit sector eventually encounters natural limits resulting from maturation of the market, inability to sustain unrealistic stock valuations, and a troubling tendency on the part of investor-owned health care companies to take advantage of the opportunities for fraud and abuse that abound in the health care arena. The resulting boom and bust cycles underline the importance of

retaining a nonprofit presence in sensitive fields where on-going care-giving relationships are important. To maintain their position in the health care sector in the face of escalating commercial pressures, nonprofits have found it necessary to move closer to the commercial model. Many have made organizational and operating decisions that blur the lines separating them from for-profits, investing in for-profit ventures and forming partnerships with physician groups and for-profit companies. This has led to growing skepticism in both academic and public policy circles about the justification of the tax exemptions nonprofit health care organizations enjoy. More than 20 states have adopted programs in the last decade requiring hospitals and, in some cases, other health care organizations to report on their community benefit activities. Gray and Schlesinger raise serious concerns about how narrowly some of these provisions define "community benefit."

Gray and Schlesinger believe that there is an essential role for nonprofit organizations in the United States because of the nation's large uninsured and under-insured population, the presence of needs that cannot be met profitably, and the importance of trustworthiness and reliability in this field. But health care will remain a highly competitive arena and nonprofits will only maintain their place if they maintain the right balance between survival and distinctiveness. To do this, they must demonstrate to the public, to employers who provide health benefits, and to policymakers that they are different from for-profits in ways that are important to communities and the country.

The onus to maintain a vital nonprofit health sector is also on policymakers, the authors say. They call for government programs to subsidize the capital investments of nonprofit health care organizations and urge regulatory bodies to avoid decisions that prompt boom-and-bust cycles in specific fields. They also recommend the creation and integration into third-party reimbursement systems of new "report cards" on organizational performance that include measures of community service and trustworthiness.

In the end, the authors say, the future of the nonprofit health sector depends upon the ability of nonprofit organizations ability to reconcile their roles as fee-collecting, service-providing organizations with their roles as tax-exempt charitable organizations. This reconciliation must be done in a manner that is open to the public and policymakers, so that it helps to reinforce the standing of the nonprofit sector and directly answer the challenges that have been posed to its legitimacy.

* Adapted from "Health" by Bradford H. Gray and Mark Schlesinger in Lester M. Salamon, editor. *The State of Nonprofit America*. Washington: The Brookings Institutions Press, 2002. Published in cooperation with the Aspen Institute.

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“Tells a readable story of how a multitude of intertwined public and private trends – shifts in demography, public policy and attitudes, technology, the marketplace – have combined to shape today’s diverse nonprofit sector. Beyond reporting on how the sector has responded to past challenges, it provides provocative suggestions for changes necessary to promote nonprofits’ health over the long term. It is a welcome addition to the literature, and I commend this book to anyone interested in the special role nonprofits play in American life.”

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“Provides a revealing insight into the important role that nonprofit organizations have come to play in the effective operation of our publicly funded services. It makes clear why we must make this partnership work.”

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– Peter B. Goldberg, President and CEO, Alliance for Children and Families

Chapter highlights are from “Health” by Braford H. Gray and Mark Schlesinger, a chapter in *The State of Nonprofit America*, edited by Lester M. Salamon and published by the Brookings Institution Press in collaboration with the Aspen Institute.

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