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Nonprofit hospitals' community benefits should square with their tax exemptions. They often don't

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Most U.S. hospitals are nonprofit organizations that receive sizeable subsidies in the form of exemptions from state and federal income taxes, sales tax, and property tax. They can also issue tax-exempt bonds and receive tax-deductible charitable contributions.

In return for these financial perks, nonprofit hospitals must provide community benefits such as charity care, unreimbursed care for people covered by Medicaid, improvements in community health, education for doctors and other health care workers, and research.

We wanted answers to two important questions about these institutions: What do nonprofit hospitals have to do in exchange for these subsidies? Do they provide enough community benefit to earn these exemptions?

The IRS requires every nonprofit hospital to complete a form (Form 990) that quantifies how much community benefit it is providing. The two largest community benefits reported by these hospitals are the unreimbursed costs for treating Medicaid beneficiaries (approximately 44% of total reported community benefit) and charity care provided to the uninsured and under-insured (an additional 17%).

In a study published this week in JAMA Open Network, we used Medicare cost reports from 2019 to examine the unreimbursed Medicaid costs reported by 2,617 nonprofit private hospitals and 829 for-profit private hospitals. In that year, these 3,446 hospitals incurred $20.6 billion in unreimbursed Medicaid costs, averaging 2.52% of total hospital-reported expenses.

At first glance, these aggregate results are reassuring, since they are comparable to a somewhat dated estimate of the total value that tax exemptions provide to nonprofit hospitals. A more telling way to assess the community benefit is to compare the unreimbursed Medicaid costs of these hospitals with those of for-profit hospitals. Viewed from that perspective, our results paint a very different picture.

Overall, nonprofit and for-profit hospitals had similar unreimbursed Medicaid costs as a share of expenses (2.51% vs 2.53%). In 23 of the 45 states in which both nonprofit and for-profit

hospitals operate, nonprofits as a group had lower unreimbursed Medicaid costs as a share of expenses than for-profit hospitals. In the other 22 states, nonprofit hospitals overall had higher unreimbursed Medicaid cost as a share of expenses than for-profit hospitals.

We observed the same patterns in states that did and did not expand Medicaid.

This is not the picture one would expect if as a rule nonprofit hospitals incurred higher unreimbursed cost for caring for Medicaid patients in exchange for receiving various tax exemptions. Nonprofit hospitals should consistently have higher unreimbursed Medicaid costs as a share of expenses than for-profit hospitals, but our research shows that often does not happen.

What about charity care, the free or discounted care provided to low-income patients without expectation for payment that is supposed to be the other major component of community benefit provided by nonprofit hospitals? In earlier work using Medicare cost reports from 2018, we found that for-profit hospitals in aggregate provided 65% *more* charity care than nonprofit ones per every $100 in total expenses without receiving any subsidies from taxpayers for doing so.

In other words, the two largest components of community benefit supposedly provided by nonprofit hospitals — unreimbursed Medicaid costs and charity care — are poorly aligned with the effectively automatic tax subsidies these institutions receive. These subsidies are also poorly targeted: they are worth more to financially successful nonprofit hospitals located in wealthy areas, which have higher property values, face less demand from Medicaid beneficiaries and uninsured or under-insured patients, and receive large charitable contributions.

Automatic tax exemption for nonprofit hospitals is a long-standing but poorly targeted policy that should be reformed. Tax exemption provides no assurance that these hospitals will behave in accordance with their charitable mission, and gives them an unfair competitive advantage against for-profit hospitals. If nonprofit hospitals are unwilling to provide sufficient community benefit to justify the value of their current tax exemptions, local communities should not be deprived of the property tax revenues that allow them to fund local schools, parks, and other public services.

Policymakers should address these issues by creating greater transparency about the magnitude of the subsidies received by nonprofit hospitals and link these subsidies to the provision of community benefits, whether in the form of unreimbursed Medicaid costs, charity care, or some other measure. To truly encourage hospitals to do the right thing, the value of the subsidies they receive should be tied to the community benefits they provide — regardless of their nonprofit or for-profit status.

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