

# 2013 New Jersey not-for-profit hospitals' community benefits and economic impact analyses

Prepared for New Jersey Hospital Association

December 2015

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## Executive Summary

The New Jersey not-for-profit hospital sector is organized as 63 acute care hospitals and systems. These not-for-profit entities conduct research, educate current and future medical professionals, improve their communities' health and well-being, and provide healthcare services regardless of patients' ability to pay. In 2013, these hospitals reported total revenue in excess of \$20.3 billion<sup>1</sup> and employed approximately 140,000 full and part-time employees.

These hospitals operated mostly as federal not-for-profit organizations. As part of this not-for-profit mission, in 2013 the hospitals provided \$2.4 billion in community benefits, absorbing a \$1 billion cost in financial assistance and other care to means-tested populations.

These hospitals were also prime drivers of economic activity for their communities. In 2013, the 140,000 hospital employees received \$8.3 billion in salaries and paid \$673.8 million in state and local taxes.<sup>2</sup> In addition to direct employment, New Jersey not-for-profit hospital activity supported an additional 113,589 jobs throughout the state. This activity generated nearly \$776.5 million in taxes related to suppliers and businesses that sell to hospital employees and suppliers.

In 2013, hospitals in New Jersey also supported the state government by paying two assessments. Each hospital pays an assessment equal to 0.53 percent of total operating revenue, which results in \$114 million of state revenue. Hospitals also pay \$10 per adjustment admission, which generates approximately \$17 million. At the local level, hospitals paid \$25.9 million in real property tax on leased, retail or other specified space owned by the hospital or in the form of a pre-established PILOT (payment in lieu of taxes) program.

The following sections provide details on EY's analyses of New Jersey not-for-profit hospitals for 2013:

- ▶ The community benefit as reported on the 2013 Form 990 Schedule H
- ▶ The total economic contributions

## 1. Community benefits of New Jersey not-for-profit hospitals and systems, 2013

Many of the benefits that hospitals provide to their communities are captured by IRS Form 990 Schedule H. Hospitals provide financial assistance and absorb underpayments from means-tested government programs such as Medicaid and incur losses due to unreimbursed Medicare expenses and bad debt expenses that are attributable to financial assistance. In addition, they offer programs and activities to:

- ▶ Improve community and population health
- ▶ Underwrite medical research and health professions education
- ▶ Subsidize high cost essential health services

Ernst & Young LLP (EY) assisted the New Jersey Hospital Association (NJHA) in reviewing their member hospitals' Form 990 Schedule Hs for tax year 2013. Schedule Hs were provided for all member not-for-profit hospitals. On average, the New Jersey hospitals studied provided benefits totaling \$2.4 billion in 2013, which accounts for 13.4 percent of their total hospital expense. This is higher than the national average of 12.3 percent, as reported by EY and the American Hospital Association in their study of 2012 Form 990 Schedule Hs.<sup>3</sup> 2012 is the most recent year analyzed by EY at the national level.

This summary of 2013 Schedule Hs reports the financial costs and forgone revenue incurred by acute care hospitals and systems in providing these community benefits, but does not measure the overall tangible and intangible benefits of improving their communities' health and economic well-being. Hospitals provided the Internal Revenue Service (IRS) with detailed descriptions of their community benefit programs as part of their filing. These descriptions often provide additional information beyond the financial information presented on the form.

## Methodology

Data was collected and tabulated for the following sections of the Schedule H form:<sup>4</sup>

- ▶ Part I on financial assistance and certain other community benefits
- ▶ Part II on community building activities
- ▶ Part III on bad debt and Medicare

Data reported on New Jersey not-for-profit hospital Schedule Hs are reported at the hospital or hospital system level. Part I, II, and III responses are reported to the IRS as a percentage of hospitals' or systems' total annual expenses. Overall net expense for community benefit programs was calculated and compared to aggregate total hospital expense.

## Hospitals' benefits to the community

In 2013, hospitals and systems reported an average of 13.4 percent of their total annual expense as providing benefits to the community. Benefits to the community include financial assistance, Medicaid and other means-tested government program underpayments, community health improvement services, research, health professions education, subsidized services, bad debt expense attributable to financial assistance, Medicare shortfall, and other community benefits and building activities. These are the financial costs or foregone revenue incurred by hospitals in providing these community benefits, but do not necessarily reflect the value of these services to communities.

Table 1 shows the average percentage of total expense disaggregated to correspond to Parts I, II, and III of the Schedule H form:

- ▶ Part I on financial assistance and certain other community benefits
- ▶ Part II on community building activities
- ▶ Part III on bad debt and Medicare

**Table 1. Hospitals' benefit to the community, by type of benefit**  
Millions of dollars

	Net Expense	Percent of total expense
7a Financial assistance	\$ 612.8	3.5
7b Medicaid	\$ 376.6	2.1
7c Other government means tested	\$ 36.5	0.2
7d Financial assistance and means tested	\$ 1,025.9	5.8
7e Community health improvement	\$ 61.6	0.3
7f Health professionals education	\$ 229.5	1.3
7g Subsidized health services	\$ 154.4	0.9
7h Research	\$ 21.0	0.1
7i Cash and in-kind contributions	\$ 8.2	0.0
7j Total other benefits	\$ 474.5	2.7
7k Total Financial assistance, means tested, and other benefits	\$ 1,500.4	8.5
Part II Community building total	\$ 8.0	0.0
Part III 3 Bad debt attributable to financial assistance	\$ 234.7	1.3
Part III 7 Medicare shortfall	\$ 620.9	3.5
<b>Total benefit to the community</b>	<b>\$ 2,364.0</b>	<b>13.4</b>

Note: Figures may not appear to sum due to rounding.

Source: EY tabulations of New Jersey hospital Form 990, Schedule Hs, 2013.

New Jersey not-for-profit hospitals provided over \$1 billion in assistance to means-tested populations, accounting for 5.8 percent of total hospital expense. They provided an additional \$475 million in other community benefits, including health professional education, subsidized health services, and community health improvement, which together accounted for an additional 2.7 percent of total hospital expense.

### Bad debt expense

In 2013, 64 percent of the hospitals reported bad debt expense attributable to financial assistance, for a total of \$235 million.<sup>5</sup> The average bad debt expense attributable to financial assistance reported was 1.3 percent of total expenses in 2013. Some patients unable to pay for their medical care do not complete hospitals' financial assistance processes. Consequently, hospitals classify unreimbursed care for those patients as bad debt expense. Most hospitals and systems report that some portion of their bad debt expense would qualify as a benefit to the community as financial assistance due to the low income of the patients.

### **Medicare surplus and shortfall**

In 2013, 73 percent of participating hospitals and systems reported having Medicare shortfalls. Medicare reimbursement shortfalls occur when the Federal government reimburses the hospitals less than their costs for treating Medicare patients.

On their Schedule Hs, most hospitals described why their Medicare shortfall should be treated as community benefit:

- ▶ Non-negotiable Medicare rates are sometimes out-of-line with the true costs of treating Medicare patients.
- ▶ By continuing to treat patients eligible for Medicare, hospitals reduce the public-sector burden related to funding medical care. The IRS has acknowledged that lessening the government burden associated with providing Medicare benefits is a charitable purpose.<sup>6</sup>
- ▶ Additionally, hospitals pointed to IRS Rev. Rul. 69-545 in their explanation of Medicare shortfall as a community benefit. IRS Rev. Rul. 69-545 states that if a hospital serves patients with government health benefits, including Medicare, then this is an indication that the hospital operates to promote the health of the community.

### **Community-Building Activities**

In 2013, hospital systems and individual hospitals spent on average 0.05 percent of their total expenses on community-building activities. Community-building activities take many forms:

- ▶ Hospital employees report participating on the state Board of Health, in regional health departments and neighborhood community relations committees, and with university and other school partnerships;
- ▶ Environmental improvements such as alleviation of water or air pollution, safe removal or treatment of garbage or other waste products, and other activities to protect the community from environmental hazards;
- ▶ Workforce development programs such as recruitment of health professionals.

These activities often promote regional health by offering direct and indirect support to communities with unmet health needs. These include patients who are indigent, uninsured, underprovided for, or geographically isolated from health care facilities.

## 2. Quantifying the total economic contributions of New Jersey's not-for-profit hospitals during 2013

This section presents estimates of the total economic and tax contribution of New Jersey's not-for-profit hospitals in 2013. This report summarizes the data provided by hospitals, the analysis methodology, and the results of the analysis.

### Key findings:

- ▶ Hospitals are a significant sector for the New Jersey economy, with a higher concentration of employees in hospitals than the national average.<sup>7</sup> In 2013, an estimated 139,864 people were employed at New Jersey not-for-profit hospitals, accounting for nearly 4% of statewide employment.<sup>8</sup>
- ▶ Nearly one-in-three employees in the health care and social assistance sector are employed by hospitals.<sup>9</sup> Employment in the New Jersey hospital industry has been fairly stable over the past decade – increasing by approximately 4% since 2003.
- ▶ Not-for-profit hospitals are an important segment of the health care and social services industry. Of the four main industry sub-sectors within health care (ambulatory health care services, hospitals, nursing and residential care facilities, and social assistance), hospitals have, by far, the largest share of employees working for not-for-profit establishments.
- ▶ In addition to direct employees at hospitals, not-for-profit hospital operations supported an additional 113,589 jobs, including jobs related to hospital suppliers (50,388 indirect jobs) and jobs related to employee consumption activities (63,201 induced jobs).
- ▶ Although not directly subject to tax, New Jersey's not-for-profit hospitals supported state and local tax revenues of \$1.5 billion in 2013. Of this amount, \$700.3 million were direct taxes – primarily paid by hospital employees (\$673.8 million). The direct tax impact includes \$25.9 million of property taxes paid by hospitals. Additional economic activity supported \$776.5 million of taxes, including \$369.3 of indirect taxes and \$407.3 of induced taxes.



## Study methodology

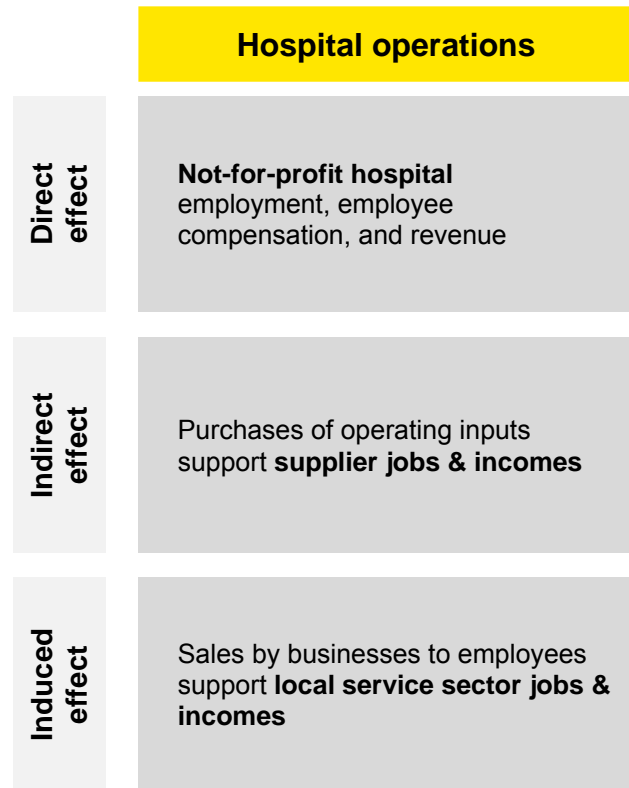
New Jersey's not-for-profit hospitals support economic activity in the state as a result of operations. This study estimates the direct, indirect, and induced economic and tax impacts of the industry's operations using data obtained from a survey of 73 members and items reported in system financial statements for FY2013.

Estimates of the indirect and induced economic contributions are based on data provided by New Jersey hospital administrators, supplemented with independent research by EY and the IMPLAN model.<sup>10</sup> Data provided by New Jersey hospital administrators has not been independently verified by EY.

## Economic impact methodology

The economic impacts related to not-for-profit hospital operations in New Jersey were estimated using detailed economic models that incorporate industry-specific employee compensation, productivity, and operating expense data for the state. The model estimates direct, indirect, and induced economic activity by tracing flows of purchases of local goods by companies and employees. The economic model's database, constructed by the IMPLAN Group, is widely used throughout the US for impact analyses by state and local economic development agencies, private-sector companies, and trade associations. The components of the estimated economic impact are described below.

1. **Direct contribution (operations and investments by New Jersey not-for-profit hospitals).** Employment, income, and output due to hospital expenditures on wages and salaries and business input purchases are the direct economic impacts of not-for-profit hospital operations in New Jersey.
2. **Indirect impact (supplier-related).** Indirect impact results from purchases from New Jersey suppliers, as well as purchases from other in-state businesses providing medical services, utilities, telecommunications, information services, and other operating inputs support employment in these industries. Further, this category reflects additional jobs and income supported in the state as these suppliers purchase inputs to fulfill demand by hospitals. Indirect impacts are



estimated based on the inter-industry demand matrix in the IMPLAN economic model of New Jersey, which incorporates industry-specific production functions. The indirect economic impact estimates incorporate economic information in the IMPLAN model that identifies the location of suppliers based on average industry relationships and other economic data.

- 3. Induced impact (consumption-related).** The induced economic impact reflects economic activity related to employee spending. Hospital employees and employees at other businesses indirectly affected by hospital operations use a portion of their incomes to purchase goods and services from New Jersey businesses. These transactions support employment at businesses such as retailers, restaurants, and service companies. Induced impacts are estimated based on household demand in the IMPLAN economic model of New Jersey, which incorporates detailed household purchases, by commodity.

Throughout the report, the direct, indirect, and induced impacts are described in terms of four indicators, described below.

- ▶ **Employment:** number of full- and part-time employees (headcount).
- ▶ **Labor income:** total employee compensation (wages, benefits, and bonuses). Benefits include all cash compensation paid to employees, as well as the value of employer payroll taxes and employer-sponsored retirement and healthcare contributions.
- ▶ **Gross domestic product (GDP):** payments to labor and capital. GDP (or value added) includes employee compensation (wages and benefits), self-employed income, indirect business taxes (sales and excise taxes), consumption of fixed capital (depreciation), and corporate profits.
- ▶ **Economic output.** For most industries, economic output is equivalent to total revenues.
- ▶ **Tax revenues:** State and statewide local tax revenues in New Jersey.

The estimated economic contributions are largely determined by the purchasing relationships between suppliers and purchasing industries. The magnitude of the estimated impact can be expressed in terms of “economic multipliers,” which are metrics equal to the total (direct, indirect, and induced) economic contribution per unit of direct contribution. The multipliers that result from the IMPLAN economic model are based on the Leontief matrix, which estimates the total economic requirements for every unit of direct output in a given industry using detailed inter-industry relationships documented in the input-output model. The input-output framework connects commodity supply from one industry to commodity demand by another. The multipliers estimated using this approach captures all of the upstream economic activity (or backward linkages) related to an industry’s production by attaching technical coefficients to expenditures. These output coefficients (dollars of demand) are then translated into dollars of GDP and labor income and number of employees based on industry averages.

## Tax impact methodology

Not-for-profit hospital operations and related economic activities generate substantial tax revenues for New Jersey governments. These taxes are generally not paid directly by the hospitals, but by hospital employees or hospital suppliers (both businesses and employees).

Because hospitals are tax-exempt entities, taxes paid directly by the hospitals are limited to local property taxes paid on non-exempt real and personal property. Hospitals also pay some employment and payroll taxes (including FICA and unemployment insurance, among others). These payments – totaling \$182.4 million in 2013 – are included in employee compensation, not as taxes.

Taxes paid by hospital employees are also considered a direct tax impact, and include sales and use, excise, gross receipts, local property, and other taxes. Indirect tax impacts occur as other businesses in the region's economy grow to provide goods and services to not-for-profit hospitals or hospital employees. Taxes not paid by hospitals were estimated using ratios of the most recent tax collections to state personal income for each type of tax. Estimates of the taxes resulting from indirect and induced economic activity are based on EY's state and local tax model for New Jersey that relates changes in personal income to changes in tax revenue by type of tax.

Data from the U.S. Bureau of the Census, Governmental Finances and the U.S. Bureau of Economic Analysis (BEA) were used to determine the ratio of state and local taxes to statewide and study area personal income for all major state and local taxes.

Note the following with respect to the tax impact estimates:

- ▶ New Jersey state and local tax contributions related to direct (employee), indirect, and induced economic activity were estimated by multiplying the estimated labor income contribution by the ratio of state and local tax revenue to personal income for each tax in New Jersey.
- ▶ The projected economic impacts and historical ratios of tax collections to personal income were estimated based on US Census Bureau, State and Local Finances tax collection data, and US Bureau of Economic Analysis State Personal Income data.
- ▶ Personal income used to calculate the tax ratios includes wages, salaries, bonuses, employer contributions for insurance, pension funds, and government social insurance. Personal income is a reasonable proxy for labor income used in this report since both measures include income and benefit sources.
- ▶ The estimated tax impact reflects the assumption that not-for-profit hospital employees and suppliers pay taxes at average rates relative to their associated personal income impact. That is, the analysis assumes that the tax impact of hospital employees and suppliers is the same as the New Jersey economy-wide average, measured as a percentage of the personal income impact.

- ▶ Additionally, hospitals pay an annual assessment to the state of 0.53% on their total operating revenues totaling \$114 million, as well as a state assessment of \$10 per adjusted admission totaling an additional \$17 million.

## Estimated economic impacts

The economic impact of not-for-profit hospital operations in New Jersey is presented in Table 2. The direct and indirect impacts are presented in terms of employment, labor income, GDP, and economic output.

**Table 2. Estimated economic impacts related to New Jersey's not-for-profit hospitals**  
Millions of dollars; number of full- and part-time employees

	Direct	Indirect	Induced	Total
Employment	139,864	50,388	63,201	253,453
Labor income	\$10,805	\$3,263	\$3,598	\$17,666
GDP	\$11,355	\$4,974	\$6,172	\$22,502
Economic output	\$18,700	\$7,934	\$9,842	\$36,476

Note: Figures may not appear to sum due to rounding.

Source: EY estimates based on data supplied by hospital management and the IMPLAN economic model of New Jersey.

**Employment.** New Jersey not-for-profit hospitals employed 139,864 full- and part-time employees during 2013, equivalent to approximately 30% of the total employment of the New Jersey health care sector during that year.<sup>11</sup> Indirect economic activity attributable to hospital operations supported an additional 50,388 indirect New Jersey jobs and 63,201 induced jobs, resulting in a total employment impact of 253,453 full- and part-time jobs.

The resulting employment multiplier – a measure of the relative size of the indirect impact – is 1.81, meaning that, for every 100 direct jobs at not-for-profit hospitals, there are an additional 81 indirect and induced jobs supported elsewhere in the New Jersey economy. Expressed another way, not-for-profit hospitals supported 14 total jobs for every million dollars of revenue during 2013.

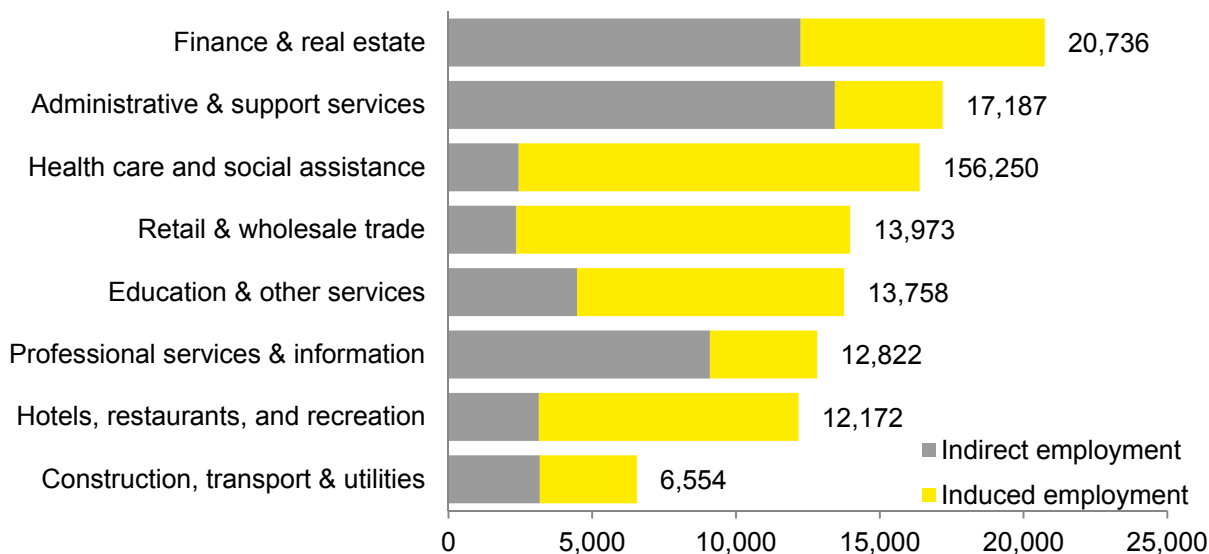
These jobs were supported across a broad range of industries, reflecting suppliers to hospitals and businesses selling to households. Figure 1 presents the distribution of the estimated indirect and induced employment impact, by industry.

Indirect jobs are supported in sectors that sell to hospitals or their suppliers. The largest indirect employment impacts are in the finance and real estate sectors and administrative and support services, which includes industries such as employment, security, and building services.

Induced jobs are supported in sectors that sell to households. The largest induced employment impacts are in the health care, retail trade, and accommodation and food service sectors.

**Figure 1. Distribution of indirect and induced jobs, by industry**

Number of full- and part-time employees; Total indirect & induced jobs = 113,589



Note: Figures may not appear to sum due to rounding.

Source: EY estimates based on data supplied by hospital management and the IMPLAN economic model of New Jersey.

**Labor income.** During 2013, not-for-profit hospital employees earned \$10.8 billion in wages and benefits. When combined with the estimated \$3.3 billion of indirect labor income and \$3.6 billion of induced labor income, the total impact on New Jersey income was \$17.7 billion during 2013.

The estimated labor income multiplier is 1.64. In other words, for each dollar of direct labor income earned by hospital employees, hospital operations generated \$1.64 of total New Jersey income. Expressed another way, not-for-profit hospitals supported approximately \$940,000 of total direct, indirect, and induced New Jersey income for every million dollars of direct revenue (direct economic output) during 2013.

**GDP.** In 2013, not-for-profit hospitals directly contributed nearly \$11.4 billion to New Jersey GDP, which supported an additional estimated nearly \$5.0 billion indirect and \$6.2 billion of induced GDP, resulting in a total GDP contribution of \$22.5 billion.

The estimated GDP multiplier is 1.98. In other words, for each dollar of direct GDP, hospital operations generated nearly two dollars of total New Jersey GDP. Expressed another way, not-for-profit hospitals supported nearly \$2.0 million of total direct, indirect, and induced New Jersey GDP for every million dollars of direct hospital revenue (direct economic output) during 2013.

**Economic output.** In 2013, direct output of not-for-profit hospitals was \$18.7 billion, which supported an additional estimated \$7.9 billion of indirect and \$9.8 billion of induced economic output, resulting in total economic output of nearly \$36.5 billion.

The estimated output multiplier is 1.95. In other words, for each dollar of direct economic output, hospital operations generated nearly two dollars of total New Jersey economic output. Expressed another way, not-for-profit hospitals supported nearly \$2 million of New Jersey economic output for every million dollars of revenue (direct economic output) during 2013.

## Estimated public sector impact

As tax-exempt organizations, New Jersey's not-for-profit hospitals remit relatively small direct tax payments but generate state and local tax revenue through direct payments to labor and indirect and induced economic activity. The tax impact of not-for-profit hospitals is primarily indirect, reflecting taxes paid by employees and by other businesses as a result of ongoing not-for-profit hospital operations.

As shown in Table 3, the estimated total state and local tax impact of New Jersey's not-for-profit hospitals was nearly \$1.5 billion in 2013, split between state and local taxes. State taxes account for 57% of the total impact.

At the local level, property taxes generate the greatest share of total tax revenue, typical of most local tax systems. The property tax accounts for 42% of the hospitals' state and local tax impacts. Local property taxes paid by hospitals are included in the direct local property tax impact, totaling \$25.9 million in 2013. The remaining \$234.7 million (90%) of direct property taxes are paid by hospital employees.

**Table 3. Estimated total tax contribution related to New Jersey's not-for-profit hospitals**  
Millions of dollars

	Direct	Indirect	Induced	Total
<b>State tax impacts</b>				
Sales & excise taxes	\$141.4	\$80.8	\$89.1	\$311.3
Individual income taxes	\$265.4	\$80.2	\$88.4	\$434.0
Corporate income taxes	\$0.0	\$15.1	\$16.7	\$31.8
Other state taxes	\$31.7	\$16.5	\$18.2	\$66.3
<b>Total state tax impact</b>	<b>\$438.5</b>	<b>\$192.5</b>	<b>\$212.3</b>	<b>\$843.3</b>
<b>Statewide local tax impacts</b>				
Property taxes	\$260.6	\$173.4	\$191.2	\$625.2
Other local taxes	\$1.2	\$3.4	\$3.8	\$8.4
<b>Total local tax impact</b>	<b>\$261.8</b>	<b>\$176.8</b>	<b>\$195.0</b>	<b>\$633.6</b>
<b>Total state and local taxes</b>	<b>\$700.3</b>	<b>\$369.3</b>	<b>\$407.3</b>	<b>\$1,476.9</b>

Note: Figures may not appear to sum due to rounding.

Source: EY estimates based on data supplied by hospital management and the IMPLAN economic model of New Jersey.

In addition, hospitals in New Jersey also supported the state government by paying two assessments. A 0.53 percent assessment on each hospital's total operating revenue netted the state \$114 million and a separate \$10 per adjustment admission assessment, also administered by the state netted the state approximately \$17 million. At the local level, hospitals paid \$25.9 million in real property tax on leased, retail or other specified space owned by the hospital or in the form of a pre-established PILOT (payment in lieu of taxes) program.

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<sup>1</sup> Source: EY calculations based on hospital audited financial statements.

<sup>2</sup> New Jersey Hospitals 2014 Economic Impact Report

(<http://www.njha.com/media/316774/2014EconomicImpactReportFINALwtabsupdated.pdf>)

<sup>3</sup> Ernst & Young 2012 Schedule H Benchmark Report for the American Hospital Association:  
<http://www.aha.org/content/15/2012schedhreport.pdf>

<sup>4</sup> The detail of each of these Parts is available on the Form 990 Schedule H 2012 located:  
<http://www.irs.gov/pub/irs-prior/f990sh--2012.pdf>

<sup>5</sup> There are differing opinions regarding the amount of bad debt that should be provided as a community benefit. This report focuses on the bad debt hospitals indicated should be attributed to financial assistance, in the amount of \$235 million in 2013. If all bad debt incurred by New Jersey not-for-profit hospitals were considered a community benefit, the total would be \$909 million in 2013.

<sup>6</sup> IRS Notice 2011-20.

<sup>7</sup> In 2013, the concentration of employment in hospitals was 4% higher than the US overall. Source: US Bureau of Labor Statistics *Quarterly Census of Employment and Wages*.

<sup>8</sup> EY estimate based on data provided by management at New Jersey's not-for-profit hospitals.

<sup>9</sup> US Bureau of Labor Statistics *Quarterly Census of Employment and Wages*.

<sup>10</sup> IMPLAN is an input-output database and model maintained and sold by the Minnesota IMPLAN group. The model was developed originally by the USDA Forest Service to conduct community impact analyses and is used to provide economic impact data and modeling to governments, universities, and public and private sector organizations for assessing the economic impacts of project decisions.

<sup>11</sup> Based on employment data reported by the US Bureau of Labor Statistics *Quarterly Census of Employment and Wages (QCEW)*.