Hospital operating margins – profits – have come under intense scrutiny during recent years. Questions about the need for hospitals to be paid more than they spend providing patient services are raised so often that the subject is now a focus of public policy debates. It seems that everyone – from Congress to state legislatures; from government agencies and state officials to local businesses, the press and even the neighbors across the street – has an opinion, and many think hospitals don’t need to generate a profit, especially those operated as charitable, not-for-profit hospitals.

The issue is complicated, at best, and made more confusing by differing opinions on the value of community benefits provided through local hospitals – the amount of charity care they provide, free community health programs they sponsor, etc. Even their status as tax-paying or tax-exempt organizations enters into the equation as a factor for weighing the need for a profit.

Regardless of individual opinions, one fact is undeniable. Like the corporate balance sheet, there is a bottom line to the issue that ultimately will translate into the long-term success or failure of any hospital: a hospital must be well managed financially to generate more revenue than it spends if it is to continue serving its community with the quality care the residents demand, expect and deserve. Whether the IRS calls a hospital a for-profit venture, where most of the profits are distributed to shareholders, or a non-profit charitable organization that reinvests profits back into the organization, the end result is the same. Without the reserves allowed by surplus revenues over expenses, hospitals will eventually wither away and close.

Like any business, hospitals must be paid enough to cover their operating costs. Payroll, utilities, food, supplies, professional fees, capital costs, pharmaceuticals and other normal costs of doing business must be covered or they won’t stay in business long. Realistically, hospital profits are one of those costs. They literally represent the cost of doing business tomorrow.

Hospital charges not only have to include the direct expense incurred providing care to patients – the medications, tests, labor, room and board for the insured and the uninsured – but they’ve also got to cover costs for repairing or replacing worn-out facilities and equipment next month, next year or five years down the road. A local hospital must be able to make those improvements when needed.

More importantly, profits allow a hospital to keep pace with technological advances. Patients expect their hospital to offer access to the most recent technology that yields better diagnostic information, improves treatment outcomes, and leads to more rapid recovery times. They must also be able to employ people with the expertise to operate these sophisticated, computerized biomedical machines. Profits ensure the capability to do these things.

Profits are also necessary to provide new programs to meet community healthcare needs; to support care provided to patients who can’t afford to pay; to hire and retain highly trained healthcare professionals who are in short supply across the country; and to fund hospital-related research and education projects. And, as government programs and private health plans continue to reduce the amounts they pay for hospital services, profits are needed to ensure those payment shortfalls are covered in the future.

Last year, almost 40 percent of Arkansas’ hospitals were paid less than it cost them to provide patient services. They made no profit. Instead, they had to rely on income from other sources like cafeterias, gift shops, interest income, private donations and locally designated tax revenues to help cover their expenses. Even with the money from those sources, about a quarter of them spent more than they received in overall payments for the year. But, they didn’t have to close. They’re still at work providing care for their communities because of the reserve funds built up in past years from the profits they’ve been able to make.

As hospital reimbursements from governmental and private payer groups continue to erode, hospital profit margins will probably shrink, but hopefully won’t disappear. They’re important for meeting our future healthcare needs. They’re essential for ensuring your hospital’s ability to do business tomorrow.