

## **Not Being Understood Well: Some Difficulties with Non-Profit Sector Utilization in Czech Republic**

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**Abstract:** This study seeks to map the links between the various ostensibly discrete concepts that make up the mosaic of determinants of quality and accessibility of social and health services and non-profit principle utilization barriers and advantages. Its aim is to analyze the sense and rationality of non-profit organizations in social and health services in the context of their character and relationships. It shows the difficulties with non-profit sector understanding, implementation and utilization from the perspective of transition economy. Especially it focuses on the relevant theoretical issues of non-profit sector as well as an empirical example of Czech hospitals where this principle is tried to being run without successful results and long-time sustainability of such organizational forms. It is deeply rooted in the theory of public finance, social policy and non-profit sector economics. To the reader, it can give an insight into the rationality of non-profit principles and its perception in reality as well as hints for the non-profit sector key useful characteristics for the socio-economic structures in market economies.

**Key words:** Social services, health services, non-profit sector, health care system, hospitals

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### **INTRODUCTION**

The key element of the article's attention, i.e., the social and health services and ways of their financing and implementation with focus on the non-profit principle will be scrutinised from the perspective of the Czech national economy. This perspective encompasses the economic approach, i.e., the question of the costs of the social and health services and their effectiveness. Economic calculation and the properties of the social and health services upon exchange are key components of this approach. However, in the context of the national economy the social contexts of the question of the accessibility of social and health services in the population and the broader results of consumption of social and health services in the form of increased welfare, wellness and well-being are also important.

The analysis is founded on the idea that the accessibility and quality of the social and health services is important from the point of view of humanity and the dignity of life in modern society. Consumption of social and health services is not just a superior option, it is a general ethical imperative. At a time when there is pressure to reduce a number of areas of life to mere economics, this ethical and humane aspect of the provision and consumption of social and health services needs to be strengthened substantially. Selective calculations of costs and returns must therefore be

complemented by monitoring of the actual social situation of those who are dependent on those services. That can be done in the form of proven subjective satisfaction with the state and standard of the provision of social services, combined with an objective assessment of these people's medical and social situation. Of these facts comes a hypothesis that non-profit sector is highly suitable for this branch of economy.

In the 60's and 70's of 20th century in European countries began the process of objectification of the legislative status (activities and content) of various institutions and organizations controlled by government. The acquisition of legal personality tried to extend the possibilities of these entities and increase their autonomy. Activities for which they were registered were often of public or generally availability nature which were previously in the direct jurisdiction of the government or municipality (e.g., education, health care, social services). Budgetary and contributory (in Czech language "rozpoetova a prispevkova") organizations are one of the forms of not-market-based organization which were established under the centrally-planned economy. In most other European countries those organizations do not exist in this form. They were conceived as largely dependent on state funding and could perform under the budget rules own economic activity. They could not manipulate with their assets because it was not their property but the property of their founders. During the economic

transformation and in particular in the context of the reform of local governments, the task is to change the perception of these organizations active in the field of social and health care.

The aim of this study is to analyze the sense and rationality of non-profit organizations in social and health services in the context of their character and relationships. In the Czech Republic, we still have not generally understood and productively utilized the benefits and positive aspects of non-profit organizations in various institutional forms. It is therefore highly useful to analyze and emphasize their significance, economic and social logic behind them that is what this article strives for to help on the scientific level.

**MATERIALS AND METHODS**

The research methods used includes theoretical analysis of non-profit financing and relationships schemes, public policy options considerations, comparative analysis of different methods of financing, synthetical and deductive analytical approach and socio-economic analysis of principles applied in the Czech social and healthsystem.

During the research, the theoretical heuristics of these findings were filtered primarily in terms of their significance for analysis of the specifics of the social and health services financing and position within economy. The results of the theoretical analysis could also help understand the causes for a number of more general problems in the Czech social and health services sector. This is also consistent with the nature of chosen research area that has been rooted in theoretical concepts and analysis of problems with their implementation and utilization in this sense the study can be seen as a novelty contribution to the current knowledge.

The theoretical background behind utilized concepts include the approaches of public and social policy and the civil society (Potucek, 1997) and the economic analysis of the non-profit principle and things behind it (Arrow, 1963; Akerlof, 1970). The position of the

non-profit sector in society was clearly recognized by Pestoff (1995). At the same time, this concept falls into the branch of social economy (Dohnalova and Prusa, 2011; Zimmer and Priller, 2004). Significant international research has been conducted in this area and the definitions of non-profit sector emerged from the cross-national comparison (Salamon and Anheier, 1997). These results are maintained and expanded up to now (Center for Civil Society, 2012).

Institutionally, the concepts of government and non-government owned for-profit and non-profit based publicly and privately financed organizations (Goulli and Frie, 2001) are useful for the topic. It is worth recognizing that the classic economic classification approach of public and private goods is not enough for this approach because it says nothing about how they are provided and financed in social reality. In this sense also the approach of institutional goods classification is highly relevant (Benard, 1985).

Rather than giving unambiguous solutions and manuals for policy makers, the study seeks for making a picture of situation that leads to suboptimal usage of non-profit sector, identifying the obstacles and considering hints and causes of the current state of art in the Czech Republic in the light of theoretical principles included.

**RESULTS AND DISCUSSION**

**Ways of financing and providing social and health services:** From the economic point of view, social and health services providers can be classified into four categories and can also draw on various sources of financing. That is shown in Table 1.

Table 1 reveals a number of links to the analysis of the economic nature of the social and health services as such. Let us now focus on those links that are the most relevant from the point of view of economic analysis.

First, there is the interaction between public providers and public funds which functions on the principle of hierarchic structures. That paves the way for

Table 1: Relationships between the financing and provision of social and health services

Financing method/Provider	Public	Volunteer	Private	Informal
Tax-public funds	Hierarchic structures, internal quasi-market (the largest part in the Czech Rep.)	Services bought by the government-external quasi-market		Subsidies/support to carers
Voluntary solidarity		Charitable support to volunteers	Payment of care for clients	
Employers		Support for volunteer organisations		Support for people caring for relatives
Private	Payments for public services	Payments for the services of volunteers	Market exchange	
Individual non-cash help	Voluntary work in the public sector	Volunteers taking part in care		Help from the family, friends, neighbours

Wistow (2005); adapted by author for Czech conditions

motivational and monitoring strategies based on an organisational/command mechanism but these have one fundamental drawback, especially as regards individuals' decision-making: they do not function autonomously, particularly with regard to economic rationality. It therefore cannot be assumed that people will follow these strategies of their own volition or that they will behave according to these strategies if some existential pressure is placed on them. These strategies presuppose two basic links to a knowledge of the logic and mechanisms of the system's working and to the participating entities' value systems and motivational preferences. In the Czech Republic, this is the far most largest part of the social and health services financing; moreover in the past when the budgetary and contributory organizations dominated it was the only way to finance and organize possible.

In the case of the organisational/command mechanism, effectiveness is thus achieved by defining and subsequently monitoring goals and rules. An external entity is necessary to define these rules and subsequently monitor whether the practical exercise of a particular activity genuinely corresponds to them. It is also a good idea to define certain indicators that can be used to monitor, perhaps indirectly, the quality and costliness of the performed activities. As the character of services is not primarily determined by an individual's demand, accessibility and quality standards have to be defined.

However, economic theory and experiences with centrally planned economies reveal these approaches' general limitations. For that reason, principles of cooperation, plurality, competition and quasi-competition in the public sector are being increasingly asserted in contemporary public economics in certain cases, these principles can provide effectiveness better than directive allocation and central planning. The distribution of funds to non-profit entities is also the subject of analysis. Optimisation thus becomes a question primarily of the effective use of a defined quantity of public funds. Preserving public funding for certain goods and services and simultaneously improving the effectiveness of allocations in the public sector with the help of the latest findings of public economics is part of the sub-text of these allocation schemes. One outcome is that the allocation of public funds in the first row of the table is shifted towards other providers that will be able to use them more effectively than the state and its organisations.

Second, there is market exchange, i.e., the interaction of private funds between the supply and demand sides. In the market mechanism, it is competition that controls whether a certain entity is behaving rationally in economic terms. In other words, the activity of one entity acts as a control as to whether another entity is ineffective in its activity. In this context, microeconomic theory provides a detailed apparatus for analysing benefit, price fixing and

rational use of production factors and also describes various deformations in the competition environment cause this mechanism of the indirect control of the rationality of allocation to fail (e.g., monopolies, various oligopolies, etc.). The price system works as an information system for participating entities.

Analysis of goods in the field of social and health services has already led to the deduction that each of the said types of interaction has its disadvantages. For that reason, we find in practice a broad range of combinations of social services financing and providers, especially if legislation has put in place an level playing-field for their providers. These can be classified into the boxes of the Table 1.

We have already shown that the economic and social specifics of the social and health services mean that providing them on a market basis, i.e. as the outcome of the intersection of market supply and demand is only one of the alternatives. The typology of social services financing and providers therefore implies the plural nature of this sector.

It is clear, though that both private for-profit providers and public "hierarchical" providers of social services may suffer from "typical disadvantages", meaning that they do not cover all needs in the field of social and health services and do not do so because of the economic characteristics of the way they function. That is one of the reasons for the establishment and existence of the so-called third (civic, non-profit) sector (Zimmer and Prillner, 2004) which seeks to fulfil the goals of "social economics". Its aim is to address social problems and achieve social goals by ensuring that a wider range of actors including non-profit organisations, pay an active role. Definitions of social economics in the relevant literature vary, mainly as regards which organisations are included in it and which are not. The provision of social and health services indubitably ranks among the goals of social economics, however.

**Principles of non-profit organizations and drawbacks of their implementation in the Czech context:**

The basic economic principle behind the non-profit organizations can be explained in a relatively simple way. At the same time, it is strange that this principle is often misunderstood by general public but also by some researchers. Thus, it is worth to emphasize that the non-profit principle does not exclude the possibilities of actually gaining a profit: the important rule is that if this profit is created, it has to be returned into the organization, either in the form of re-investment resulting in the expansion of the services or by lowering the price of existing services.

Non-profit organizations thus strive for rational economic allocation the same way as other economic

subjects do, however, they are not pushed by their owners to maximize profits and allocate them to shareholders or trade their stocks on the exchange. Also the non-profit principle guarantees that the money is kept in the enterprise of its origin; this is especially important for the social and health services as empirically here a pressure for allocating money elsewhere is seen. Also, it brings an important element of autonomous budgeting.

As for the financing sources of non-profit organizations, it highly depends on the branch they operate in and the degree of public service they fulfill. The most general statistics (average from 7 OECD countries) shows that Public sector payment is 41%, Private fees 49% and Private giving (fundraised) is 10% (Salamon and Anheier, 1996), however, the situation varies and for example in health care, the share received from health insurance funds will be always the dominant share of the income.

From the general typology of non-profit organizations (Salamon and Anheier, 1997), the three main types are the most important in the social and health services: non-profit organizations organizing and providing social and health care and services, the charities and foundations doing primarily fundraising and social work and health insurance companies that will deal with social health insurance contributions. The latest example is highly controversial in the Czech public debate: after 2006, the suggestions of privatization of health insurance companies was discussed heavily, even in the form of regulated profit amount in exchange for gaining the right to collect and allocate social health insurance contributions. Currently, the public health insurance companies behave generally like non-profit, however, their status does not explicitly state it and the government influence together with the situation on the market (one big general health insurance company and 7 smaller others) decreases the level of their autonomy very much. This does not imply that the theoretical transformation to the “ideal nonprofit” in the case of health insurance companies is at all cost desirable; the models of those institutions in the health care system vary and it is out of the scope of this study to analyze it.

There are several reasons why particularly in social and health services, similarly to some other branches of economy like education, etc., the non-profit principle is suitable for general use. These include:

- The problem of trust and confidence
- Low demand elasticity and problem of time-based decisions
- Market failure
- Information asymmetry
- Public interest on provision and availability of those services

Many of these aspects were already analyzed in literature, we can quote Arrow (1972) that “the very word, ‘profit’, is a signal that denies the trust relationship” and also “as a signal to the buyer of his intention to act as thoroughly in the buyer’s behalf as possible, the physician avoids the obvious stigmata of profit maximizing” (Arrow, 1963). This means that those services require for their successful application a high level of relationships which could be possibly harmed by the pressure for making profits.

A simplified economic approach could also suggest that when having adequate competition on the market, we do not need the concept of non-profit organizations at all. The suggested mechanism is relying on the competitive market as the factor of decreasing the market prices theoretically up to the point where the profit will be zero thus realizing a “true non-profit” environment. However, in reality, this rarely happens as the degree of competition is almost never like that. Also if it eventually happens, it would prevent the mechanisms of reinvesting the gained profits into the enterprise because the industry would not be able to generate them at all. The last argument in this area is that the nature of competition on the market could be especially without adequate regulation, very rough and ethically unsuitable for areas like social and health services (see also previous arguments of arrow that also can be transposed to the nature of competition on those markets). Thus, even if the questions of effectiveness of the nonprofit organizations in terms of wages, transparency, etc. could be raised, we cannot simply abandon this concept saying that the for-profit principle with adequate market competition will replace the non-profit one.

Moreover, we can see that in the times of globalization and pressure of the financial markets on the economy as well as with increased demand on health and social care services general availability on the other hand, some of those arguments were even strengthened. The result is that we currently can say that the non-profit principle is very important for the effectiveness and availability in this sector and has to be considered as a crucial component of the institutional structure here. And this has its own empirical evidence: social and health services sector was in the 1990s dominant source of growth of the non-profit institutions in the economy (Salamon and Anheier, 1997).

Institutionally, the concept of non-profit social and health services is rooted in many documents at the European level such as the Amsterdam Treaty and the Green (EU, 2003) and White Book on the services of general interest (EU, 2004). In the Czech Republic, there is general legislation in this area which can be utilized, e.g. for social services, however in health care, the situation is different and not using these possibilities.

The ambulatory care is nearly 100% private and the legal form is for-profit independent businesses (economically operating on the principle of high degree of competition and strong regulation by health insurance companies). The hospital sector remained primarily government-owned, even the corporatization was taking place and in 2006 the big discussion of the non-profit hospital laws happened. The new Act No. 245/2006 Coll. on non-profit hospitals was enacted in April and it brought some steps in modernization in terms of applying corporate governance and management to hospitals which absence was the main shortcoming of the previous, contribution from the government health budget based mode of operation. However, the political changes and inadequate institutional environment stopped the successful implementation of this law which resulted in the fact that no hospitals really were transformed by the rules that this law predicted.

This situation as an empirical example has clear consequences when doing statistical comparison as shown in Fig. 1 and 2.

Figure 1 and 2, we can see the situation in hospitals typology being one of the largest institutions in health care industry. Comparison between USA and Czech Republic shows that American structure of hospitals is heavily based on non-profit ones; the Czech structure nearly has not utilized them at all. As an interesting example, Mayo clinic, one of the largest hospitals in the United States is a non-profit one. Other countries come between those extremes; it is also worth noting that in Western Europe the actual number of non-profit hospitals (as an institutional form) is even larger relatively than it would seem from the Fig. 2 because they generally have smaller number of beds per hospital than big public hospitals (which results in the situation shown in Fig. 1).

Currently (at the end of 2014) there have been new initiatives to reform hospital sector. The proposed organization form should be close to non-profit hospitals should not pay taxes and be independent from the direct government auspices. The implementation is however still unclear; the conflict between taking a hospital as a business or as a non profit service remains hot. Where one part of stakeholders believes that the economic responsibility and risk of losses and profits is the key factor of economic performance, second part believes that the absence of for-profit and business optimization motives will lead to better results for the staff and clients. In public and social policy and government decision process, the advantages of non-profit principles have not been clearly recognized and the question of “economic effectiveness and manageability” remains the mantra of policy options.

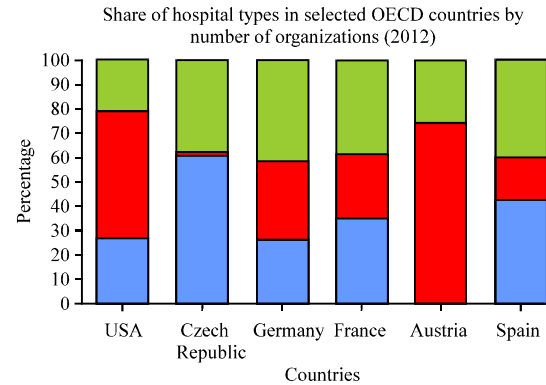


Fig. 1: Share of hospital types by number of organizations, OECD. Blue: Public (government), Red: Non-profit, Green: For-profit or private owner without special status (OECD, 2014)

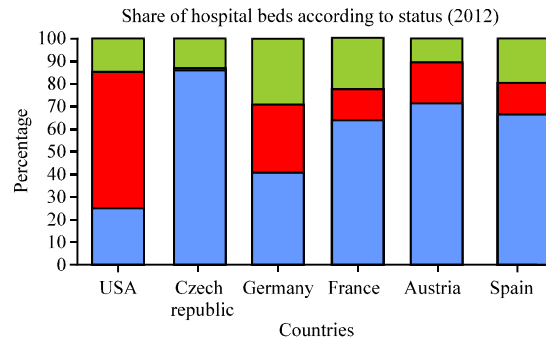


Fig. 2: Share of total hospital beds by type (status) of organization, OECD. Blue: Public (government), Red: Non-profit, Green: For-profit or private owner without special status (OECD, 2014)

We can conclude that although there is a number of economic and institutional reasons and rational approaches that support the usage of the non-profit organizations in social and health services, they have not been utilized in the Czech Republic much. This does not mean that they are a “one size fits all solution”, just suggests that they should have stronger position in the mix. Their effectiveness and/or efficiency are debatable similarly to the for-profit institutions and depends on the market structure, regulation and institutional framework; the absence of the for-profit motive does not mean that they do not provide rational economic allocation of resources just like other economic subjects on the market.

## CONCLUSION

The research results outcoming from the theoretical and empirical analysis done show that the situation in

non-profit sector implementation in Czech Republic heavily suffers from the unfinished transformation processes and poor belief in the structures that do not belong either to government or pure market (for-profit) basis. While in countries with longer tradition of market economy the non-profit principle is heavily analyzed and applied in the Czech context the dependency on government grants, short duration of existence of non-profit organizations and low utilization at the bigger institutional forms prevail.

Non-profit organizations are generally perceived especially in Czech public discourse as belonging to charity and non-market allocation of resources. This surely is one of the branches they can work at but there are further possibilities of the usage of this concept on standard market relationships and transaction together with high corporate culture and governance level.

This is closely connected with the principle of concentration on actual services provision and trustful operation on the market. An imperative to allocate the profits for the development and availability of the services provided together with the long-term stability and economic rationality is something that is highly needed and can be also said missing in economy today where the conflict between inflexible government and global markets exist.

The nature of social and health services is heavily suited for the non-profit principle application. High level of trust required, the inadequacy of profit motives in the relationships between the actors of transaction, importance of actual quality and concentration on the real operation of an enterprise all contribute to this. This does not mean that another ways are not possible theoretically; it just justifies that the non-profit principle should have strong role in the mix, giving those organizations autonomy from the direct auspices of the government and freedom from the market pressure for profits maximization at all costs. Empirically this results in non-profit organizations having strong position in social and health care sector worldwide.

In the Czech Republic especially after the year 2000, strong demand for the transformation of the organizations financing and providing health services arose as the original forms of budgetary and contributory organizations has not been suitable in many cases for the new environment. Especially in health services, however, this process was not successful and the conflict described above resulted in either keeping things under the direct control of the government or the attempts of

“full” privatization. As seen from the international comparison, this radical approach is not usually employed in health care systems of the world and a mixture of institutional forms in providing health care exists where the non-profit organization usually take significant portion of the “market”.

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