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Hospital Loses Property Tax Exemption For Not Being “Charitable” Enough

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Recently, the Illinois State Supreme Court affirmed a previous ruling revoking an Illinois Hospital’s property tax exempt status. Playing into the decisions were the following facts:

- The Hospital provided free or discounted care to 302 patients out of 110,000 admissions for the year in question;
- The charity care amounted to \$831,724, or less than 1% of the Hospital’s \$113 million in revenue;
- The Hospital did not advertise that charity care was available; and
- Unpaid bills were automatically referred to collection agencies.

The relevant property tax exemption statute required that the property be “actually and exclusively used for charitable or beneficent purposes.” In finding that the Hospital failed to meet this standard, the court stated, “both the number of uninsured patients receiving free or discounted care and the dollar value of the care they received were de minimus [sic]. With very limited exceptions, the property was devoted to the care and treatment of patients in exchange for compensation through private insurance, Medicare and Medicaid, or direct payment from the patient or the patient’s family.” In addition, the court turned to case law which provided the following characteristics of a charitable institution:

1. It has no capital, capital stock or shareholders;
2. It earns no profits or dividends but rather derives its funds mainly from private and public charity and holds them in trust for the purposes expressed in the charter;
3. It dispenses charity to all who need it and apply for it;
4. It does not provide gain or profit in a private sense to any person connected with it; and
5. It does not appear to place any obstacles in the way of those who need and would avail themselves of the charitable benefits it dispenses.

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The court found that the Hospital failed factors two, three and five. The Hospital overwhelmingly generated its funds by providing medical services for a fee as opposed to charitable contributions. As discussed above, charity care was not advertised and collection agencies were automatically utilized for unpaid bills. In the end, the court was troubled "that there was little to distinguish the way in which [the Hospital] dispensed its 'charity' from the way in which a for-profit institution would write off bad debt."

Although this ruling deals with a hospital's provision of charity care, all nonprofit organizations that claim property tax exempt status, due to their charitable conduct, should take note. State and local budgets have stretched beyond their breaking points, causing the taxing authorities to pursue every possible revenue source with the utmost vigor. The challenge of an organization's property tax exempt status does not require a prior/current IRS challenge of the organization's federal tax exemption. It should be noted though, that any challenge of an organization's property tax exempt status may cause other taxing authorities to increase their own scrutiny. **Organizations planning on filing for property tax exempt status, or those who have such status, should seek legal advice to ensure that their operations will not cause such request or status to be denied or revoked, respectively.** Manatt, Phelps & Phillips, LLP's tax attorneys stand ready to assist with any questions you may have.

For additional information on this issue, contact:



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