September 10, 2012

The Honorable Stephanie Rawlings-Blake
Mayor, City of Baltimore
100 N. Holliday Street, Suite 250
Baltimore, MD 21202

Dear Mayor Rawlings-Blake:

We are pleased to enclose the Baltimore Efficiency & Economy Foundation’s (BEEF) recent study, Report on Real Property Taxes and Exempt Organizations in Baltimore. The authors, David Brunori and Michael Bell, are experts in the field of property taxes, affiliated with George Washington University and highly commended by the Cambridge, MA-based Lincoln Institute for Land Policy which publishes on the topic.

The Report looks at municipalities nationwide to examine the relationship between the non-profit sector and local government public finance and economics, with a focus on the property tax as the dominant local revenue source. The relationship has two important dimensions. First, lost property tax revenues from non-profits exempt from property taxes worsens the fiscal stress faced by local government. Second, questions of fairness arise when a community’s taxpayers are forced to pay higher property taxes to compensate for the narrowed tax base.

The Report addresses the relatively small number of major non-profits that are significant property owners. Universities and hospitals are the primary beneficiaries of tax exemptions, even though they have substantial resources, own large pieces of real estate and consume a significant number of municipal services. In addition, these larger tax exempt entities bring benefits to constituencies far outside of Baltimore City. The entire metropolitan region (and indeed the entire state) benefits from a well-educated workforce and a quality array of hospitals, but Baltimore City is forced to absorb the entire loss of property tax revenue. Some commentators believe that the state should shoulder some responsibility for the uneven effects for jurisdictions with large numbers of tax exempt organizations.

In FY2012, Baltimore’s total property tax cash value was $51.2 billion. Tax exempt properties are said to have a cash value of $15.1 billion (29%). This number must be viewed with caution (as an understatement) since few resources are committed to the task of accurately estimating the cash value of non-taxable properties that are generating no revenue.

Nonprofit/charitable properties make up 10% of the number of tax exempt properties in Baltimore City, but more than 25% of their value. The rest of the tax exempt properties are largely owned by government. Within this category, there are 62 non-profit/charitable properties (3.3%) that are valued at more than $10,000,000 each, accounting for 43.7% of the value of non-profit/charitable properties in Baltimore.
Two-thirds of the highly valued properties are owned by universities or hospitals, including Johns Hopkins University and Hospital and are conservatively valued at $1.228 billion.

Baltimore’s challenge is to balance the benefits provided by these non-profits with the local government’s legitimate need for adequate revenue to provide basic city services and its need to provide for an equitable distribution of the tax burden across various groups of property owners. This BEEF project is intended to be a first step in meeting that challenge. It is the study called for in early drafts of the City’s 2010 Bed Tax PILOT Agreement to begin in year two of the existing six-year agreement.

The Report gathers the best practices in the growing national trend among local governments to negotiate long-term arrangements for permanent payments in lieu of taxes (PILOTS) and/or services in lieu of taxes (SILOTS) with the major non-profits in their jurisdictions. Although the PILOT is recognized as only a small percentage of the tax amount that would be owed based on property values, it is nonetheless some compensation for the city services that benefit every citizen, including the non-profits – police, fire, sanitation, street repair, et al.

Deciding upon next steps will be a collaborative process largely between Baltimore City government officials and the nonprofit organizations. BEEF recommends the formation of task force composed of all interested parties with impartial leadership to recommend Baltimore’s plan for implementation. In Boston, that process stretched out over five years – too long in our view.

Briefly, the following is a summary of the “recent” discussions regarding PILOTS in Baltimore City. The 2007 Blue Ribbon Committee recommended the consideration of direct payments with nonprofits in lieu of taxes, and referenced what had occurred in 2004-2005 with regard to telecommunications and energy taxes. In Spring, 2010, the City negotiated Bed Tax Pilot Agreements with all of the major colleges and universities and hospitals who agreed to pay varying amounts each year for six years; no new taxes or payments focused on the non-profit community could become effective sooner than six years from June, 2010. And finally, as the City is about to release its Ten Year Plan, this BEEF report serves as a complement to it.

We sincerely hope that this report can serve as the starting point for a substantive dialogue among representatives of the city, the non-profit community, and the broader community of property owning taxpayers, and that that dialogue can conclude with a consensus agreement in two years. It is a critically important dialogue. BEEF is committed to assisting that effort in whatever way it can.

Sincerely,

[Signature]

Tracy Gosson
President
REPORT ON REAL PROPERTY TAXES AND EXEMPT ORGANIZATIONS IN BALTIMORE

FINAL REPORT

David Brunori

Michael Bell

Prepared for Baltimore Efficiency and Economy Foundation

June 23, 2012
Executive Summary

Non-Profit organizations are generally exempt from property taxes. Such exemptions cost local governments billions of dollars annually in terms of foregone property tax collections. As the largest landowners, universities and hospitals usually enjoy the most benefits from these exemptions.

Local governments have developed methods for addressing the issue of lost revenue due to property tax exemptions. The most common method of getting non profits to contribute to the cost of services provided by local governments is payments in lieu of taxes (PILOTS). PILOTS are invariably negotiated voluntary payments made by exempt organizations in place of property taxes, but recognizing the public services being used by the non profit entity. They are or have been used in at least 117 municipalities in 18 states. While PILOT agreements never impose burdens on non profits equal to what their property tax would be, they remain the most successful method of raising local revenue from non profits.

There are several alternatives to PILOTs used by local governments to raise revenue from non profits. These include Services in Lieu of Taxes (SILOTS), municipal services fees and charges, other direct taxes, and state contributions to replace lost revenue. These other methods are used with varying degrees of success. None however have been used with the frequency or success of PILOTs.

A particular problem arises when non profit organizations engage in commercial activity. Depending on the jurisdiction the exempt-status is potentially sacrificed when a charitable institution permits a commercial activity on its premises. Each state’s tax code
addresses an institution’s charitable status differently and no uniform rule can be broadly attributed to all states.

Generally states address the exempt status of a charitable institution that permits commercial activity on its premises in one of three ways: (1) statutes requiring that property must be used exclusively for the organization’s charitable purpose; (2) statutes requiring the primary or dominant use of the property for the organization’s charitable purposes or (3) statutes that allow partial use of the property for other than charitable purposes. Generally, states which require “exclusive use” do not strictly construe this requirement and those states that adopt a more lenient partial exemption approach require that the nonexempt portion be clearly defined or calculable.

Another issue that arises is whether localities can retain tax revenue from properties being sold by taxpaying owners to entities exempt from taxation. There are no statutory or other legal authorities for a local government to retain tax revenue from properties sold to a non taxable entity. In every state, whether the purchased property is taxable or not depends on its current use.

While localities sometimes struggle to obtain revenue from tax exempt organizations, there is a general recognition that such organizations contribute to economic livelihood of those localities. Numerous studies have found that non profit organizations, particularly universities and hospitals, result in more employment, higher over income, and greater economic activity. The challenge for local government officials (and individual non profits) is to balance the benefits provided to the community by the non profit and the costs imposed on community taxpayers who pay higher property taxes because non profits are removed from the property tax base.
# Table of Contents

1. Introduction 4

2. Section I
   Examine best practices generally in cities and other local jurisdictions that have confronted the issue and developed solutions, particularly collaborative solutions, to the problem. 18

3. Section II
   Determine the circumstances when a PILOT should (and should not) be “required” of a tax exempt organization and how its particulars should fairly be determined. 31

4. Section III
   Identify alternatives to PILOTS for raising appropriate revenues from tax exempt organizations. 34

5. Section IV
   Examine the options for responding to the increasing commercial activity engaged in by tax exempt organizations in some jurisdictions that often escape taxation 41

6. Section V
   Examine the options for retaining tax revenues from properties being sold by taxpaying property owners to entities exempt from taxation. 47

7. Section VI
   Review ways to recognize and fairly value the many in kind contributions of non profit organizations. 49

8. Conclusion 53

9. References 55

10. Appendix A 59

11. Appendix B 62

12. Appendix C 66
Introduction

There are approximately 1.5 million organizations in the United States that are exempt from property taxation (Mikesell 2009). The City of Baltimore is concerned about the nature of its tax base generally and in particular the high percentage of property in the city owned by entities exempt from property taxes. The city previously entered into short term agreements with a number of the larger nonprofits for payments in lieu of taxes (PILOTs), generating a significant annual payment. These agreements expire at the end of a specific term. The city recognizes that the entities signing these PILOT agreements represent the owners of only a small fraction of the non-taxed property in the City.

This research project has been undertaken on behalf of the Baltimore Efficiency and Economy Foundation and focuses on the relationship between the non profit community and municipal fiscal systems. The project is designed to address several issues concerning how local governments throughout the United States deal with the loss of revenue from property exempt from taxation.

There are two fundamental issues associated with the property tax exemption of non profit organizations. First, in a city like Baltimore, they can represent a significant portion of the real property tax base. Because these organizations consume locally provided goods and services many feel they should contribute to the cost of providing those services. Second, beyond this issue of foregone revenues, exemptions also lead to a fairness issue. When the property tax base is narrowed because of these exemptions, taxpayers not receiving such preferential treatment must shoulder a greater burden of
paying for government services because their taxes are higher than they otherwise would be if all property was subject to the real property tax.

The remainder of this introductory section describes property tax exemptions for the non-profit sector in general, and for Baltimore City specifically. Taking a national approach, Section I examines the best practices for dealing with the problem of lost revenue due to property tax exemptions. Reviewing statutes from all fifty states, Section II examines when PILOTS should be required of tax exempt organizations. Identifying alternatives to PILOTS for raising revenue from tax exempt organizations is the subject of Section III. In Section IV, options for responding to the increasing commercial activity engaged in by tax exempt organizations are examined. Section V discusses the options for retaining tax revenue from properties being sold by non exempt owners to entities exempt from real property taxation. Finally, Section VI reviews the literature and discusses the ways to recognize and fairly value the economic impact of non profit organizations at the municipal level.

Property Tax Exemptions in the United States

All 50 states have statutory provisions exempting from taxation property owned by non-profit organizations and used for charitable purposes. Legislatures and courts have traditionally rationalized the tax exemption by emphasizing the significant public interest and communal benefits deriving from these organizations’ conduct. Every state generally exempts from property-taxes non-profit charitable organizations, hospitals, education institutions, government owned property and other categories of land use based on the current use of the property or the characteristics of the owners (e.g.,
blind, disabled, etc.) notwithstanding differences in the language or extent of the exemptions. (Gallaher 2002; Brody 2010). In evaluating a non-profit organization’s eligibility for exemption, states require both a charitable owner and a charitable use of the specific property for which exemption is sought. (Brody 2010).

Accordingly, when an otherwise exempt charitable organization starts to engage in private economic activity, the respective state must evaluate whether the organization and use of the property are still “charitable” for property-tax purposes. Thus, state statutory regimes and the level of judicial scrutiny are of central importance in determining an organization’s exemption status. (See Brody 2010, at 624-26, “An important aspect of the state-level tax regime flows from the existence of property-tax exemptions granted in or authorized by state constitutions, and the degree of vigilance with which the courts guard their authority over constitutional terminology.”).

State constitutions authorize the charity property-tax exemption in one of three ways: (1) the state constitution mandates the exemption; (2) the state constitution grants exemption authority to the legislature; or (3) the state constitution is silent on taxes, in which case the legislature has implied authority. (Brody 2010, 671-733, comparing property-tax exemptions by state). In eighteen (18) states the constitution mandates property tax exemptions. In twenty-four (24) states, the constitution grants the legislature authority to exempt property from taxation. In eight (8) states, the constitution is silent on the matter and all exemptions arise out implied legislative powers. Appendix A sets forth the authorities for property tax exemptions in each of the fifty states.

The widespread use of exemptions results in significant losses of property tax revenue for state and local governments. One nationwide study estimates that the
property tax exemption costs local and state governments between $17 and $32 billion each year (Sherlock and Gravelle 2009; see also Cordes, et al. 2002). In 2005 alone, property exempt from the real property tax cost New York City $605 million and Boston $258 million in foregone revenue (Lipman 2006). Yet another study found that exemptions totaled 1.2 percent of all city budgets (Russell 2009).

Property tax exemptions pose several policy issues beyond lost revenue. Despite their exempt status, these organizations benefit from public services (such as firefighting services, snow removal, and road maintenance) that must be paid for by taxable entities. The narrower tax base results in higher property taxes for private businesses and homeowners, because it forces municipalities to compensate for lost revenue by raising tax rates. The property tax exemption also provides an incentive to nonprofits to seek expensive real estate, because they are not concerned about greater property tax burdens. Such subsidies further narrow tax bases by exempting some of the most valuable property available.

Tax exempt organizations can generally be divided into four categories: hospitals, colleges and universities, social service organizations or charities, and religious groups. Churches are rarely mentioned in non-exemption discussions because taxing them raises constitutional and political issues (Brody 2010). Charities comprise the majority of tax exempt entities, but they are mostly very small organizations that possess limited resources: sixty-two percent of charitable nonprofits claiming exemptions in 2010 had annual incomes under $100,000 and accounted for 1.2 percent of all revenue earned by tax exempt organizations (Kenyon and Langley 2010). Furthermore, smaller charitable nonprofits are more dependent on state grants and have seen their financial
situation decline during the recession due to government budget cuts (National Council of Nonprofits 2010). While methods do exist to generate revenue from small nonprofits, the potential revenue that can be raised is negligible.

Moreover, efforts to raise money from charities with limited resources can be self-defeating. While taxing small charities generates revenue, it also forces such organizations to cut programs, which shifts demand for healthcare and human services onto the government (National Council of Nonprofits 2010, see also Fanburg 2011). One observer argues that

“[s]ocial service organizations are, in effect, an arm of government. Their existence relieves government of some of its burdens, which compensates a government for the loss of revenue. Moreover, governments fund most social service nonprofits by buying the services the agencies provide. If they then tax the nonprofit’s income, they are sending the money back to the government with the added layer of administrative costs.” (Lemov 2010).

The vast majority of wealth, property, and assets within the nonprofit sector are concentrated heavily among a relatively small percentage of organizations (Kenyon and Langley 2010). In 2010, 2.9 percent of all entities claiming tax exemptions had annual revenues over $10 million, comprising 84.7 percent of total nonprofit income. The average annual revenue amongst this group was $134 million. This sphere of wealthy nonprofits consists primarily of universities and hospitals, though not exclusively so.\footnote{Lipman (2006) For example, the Getty Museum in Los Angeles, the Chrysler Building in New York City, and the Kimmel Center for the Performing Arts in Philadelphia are all tax exempt, and annually cost their municipalities $18.4 million, $17.5 million, and $5 million, respectively, in potential revenue.} These organizations reap nearly two-thirds of savings from the property tax exemption, although they represent only 4.3 percent of nationwide real property owned by nonprofits. They are the primary benefactors of tax exemptions, despite the fact that they have more resources and consume a larger portion of municipal services. Furthermore,
many small nonprofits rent property, and thus do not benefit from the property tax exemption in the same way as larger organizations that purchase their real estate. This skews exemptions even more in favor of wealthy organizations such as hospitals and universities.

The lopsided distribution of wealth is an important consideration when trying to generate revenue from exempt organizations. Large nonprofits not only have a higher ability to contribute financially, but they also tend to possess larger pieces of real estate (and thus do more to narrow the tax base), and utilize more taxpayer services. From a practical standpoint, such organizations offer more potential for revenue collection because they are more financially able to contribute. From a political perspective, universities, hospitals, and other large nonprofits are seen as an easy target for policymakers because their wealth is known to the public. As one expert stated, “Even if a college or university is only one of many nonprofits in the municipality, the larger the nonprofit exempt footprint, the greater the pressure will be on the ones which look like they have the financial wherewithal to pay.” (Brody 2010, 665).

For these reasons, local governments are more likely to view large nonprofits such as universities and hospitals when seeking revenue. Such organizations often argue that singling them out is unfair, and some commentators agree: Professor Brody observes that they “have a strong argument about unfairness. While [colleges and hospitals] garner much of the focus of revenue-starved and geographically bounded municipalities, focusing just on a sub sector raises troubling questions.” (Brody 2010, 665).

Yet others point out that tax exemptions disproportionately benefit such organizations. Daphne A. Kenyon and Adam H. Langley of the Lincoln Institute of Land
Policy argue that “the exemption is poorly targeted, since it mainly benefits nonprofits with the most valuable property holdings, rather than those providing the greatest public benefits.” (Kenyon and Langley 2010, 42). They further note that “there are no tax savings for nonprofits that rent and the greatest tax savings go to large nonprofits, especially hospitals, universities, and long-term housing facilities.” (id.) Regardless of one’s opinion on the fairness of targeting such entities, the fact remains that they possess far more wealth than other exempt organizations, disproportionately erode the tax base by owning large pieces of real estate, and consume more municipal services. Thus, they offer more potential for raising revenue, and are arguably more indebted to their host municipalities.

Another issue presented by property tax exemptions is which level of government should bear the costs. Currently, in virtually all states, local governments bear the loss of the property tax revenue as a result of exemptions that are granted at the state level. As such, “states may exempt a broader range of nonprofits from taxation than they would have if they had to bear the full cost of the exemption.” (Kenyon and Langley 2010, 42). Additionally, benefits offered by an exempt entity’s activities often accrue outside of the municipality in which it is located (Brody 2010). For example, a tax exempt university in one city might serve as a recruitment center for industry throughout the entire state. While the benefits of an educated workforce are felt regionally, the municipality hosting the university is forced to absorb the entire loss of revenue. Commentators opine that states should shoulder some of the responsibility for the uneven effects created by exemption laws (Brody, 2010, 663). If state governments were forced to share in the
costs of exemptions, legislatures might be hesitant to strip taxing authority from municipal governments.

Finally, some municipalities are impacted significantly more than others (Brody 2010, 270). Nonprofit organizations tend to locate in central cities, where populations are larger and charitable services are in higher need. Similarly, some municipalities host very large nonprofits—usually universities—that comprise a disproportionate amount of available real estate. In such cases, state exemption laws can take a heavy toll on local government’s ability to generate revenue.

**Property Tax Exemptions in Baltimore**

Baltimore City has a taxable real property tax base of $51.2 billion in 2012. The following table presents the composition of that property tax base by land use type. Total residential properties account for 48.5 percent of the base, with single family homes accounting for 92.4 percent of residential property values. Apartments account for more than one-third of the base, while commercial and industrial properties account for just 15.8 percent of the real property tax base in Baltimore.
<table>
<thead>
<tr>
<th>Land Use Code</th>
<th>Type</th>
<th>Number of Accounts</th>
<th>Total FCV</th>
<th>Share of Taxable Base</th>
</tr>
</thead>
<tbody>
<tr>
<td>R</td>
<td>Residential</td>
<td>192,004</td>
<td>$22,921,817,120</td>
<td>44.8%</td>
</tr>
<tr>
<td>RC</td>
<td>Residential/Commercial</td>
<td>22</td>
<td>$3,189,800</td>
<td>0.0%</td>
</tr>
<tr>
<td>U</td>
<td>Residential/Condos</td>
<td>12,059</td>
<td>$1,938,964,800</td>
<td>3.8%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>RESIDENTIAL</td>
<td></td>
<td>$24,863,971,720</td>
<td>48.5%</td>
</tr>
<tr>
<td>M</td>
<td>Apartments</td>
<td>1,938</td>
<td>$18,277,728,800</td>
<td>35.7%</td>
</tr>
<tr>
<td>C</td>
<td>Commercial</td>
<td>8,861</td>
<td>$5,717,493,400</td>
<td>11.2%</td>
</tr>
<tr>
<td>I</td>
<td>Industrial</td>
<td>2,390</td>
<td>$1,845,577,300</td>
<td>3.6%</td>
</tr>
<tr>
<td>CC</td>
<td>Commercial/Industrial</td>
<td>582</td>
<td>$511,454,700</td>
<td>1.0%</td>
</tr>
<tr>
<td>CR</td>
<td>Commercial/Residential</td>
<td>7</td>
<td>$875,100</td>
<td>0.0%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>COMMERCIAL</td>
<td></td>
<td>$26,353,129,300</td>
<td>51.5%</td>
</tr>
<tr>
<td>TOTAL TAXABLE REAL PROPERTY BASE</td>
<td></td>
<td></td>
<td>$51,217,101,020</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Source: Maryland State Department of Assessments and Taxation and author calculations.

A data set of individual tax exempt properties in Baltimore for 2012 was provided by the Maryland State Department of Taxation and Assessment. For each individual property the data set includes information on the block and lot number, an estimate of full cash value, an exempt code reflecting the land use of exempt property, the exempt type and the owner. The following table provides a breakdown of tax exempt property in Baltimore by land use type.
<table>
<thead>
<tr>
<th>Type of Exempt Property</th>
<th>Number of Parcels</th>
<th>Exempt Value</th>
<th>Pct Total Exempt Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Government</td>
<td>71</td>
<td>$769,224,190</td>
<td>5.08%</td>
</tr>
<tr>
<td>State Government</td>
<td>548</td>
<td>$4,054,768,130</td>
<td>26.80%</td>
</tr>
<tr>
<td>City Government</td>
<td>13,384</td>
<td>$4,594,445,520</td>
<td>30.37%</td>
</tr>
<tr>
<td>Town or Municipal</td>
<td>6</td>
<td>$5,695,200</td>
<td>0.04%</td>
</tr>
<tr>
<td>Individual</td>
<td>741</td>
<td>$53,519,410</td>
<td>0.35%</td>
</tr>
<tr>
<td>Religious</td>
<td>2,084</td>
<td>$1,822,936,249</td>
<td>12.05%</td>
</tr>
<tr>
<td>Non-profit/Charitable</td>
<td>1,904</td>
<td>$3,829,733,318</td>
<td>25.31%</td>
</tr>
<tr>
<td><strong>TOTAL EXEMPT PROPERTY</strong></td>
<td><strong>18,774</strong></td>
<td><strong>$15,130,322,017</strong></td>
<td><strong>100.00%</strong></td>
</tr>
</tbody>
</table>

Source: Maryland Department of Assessments and Taxation and author calculations.

In the aggregate, there are 18,774 properties listed as fully exempt from real property taxation in Baltimore. These properties have an estimated full cash value of $15.1 billion in 2012. Such estimates of full cash value, however, must be viewed with caution. Since no revenues are generated from such properties, limited resources are committed to the task of estimating full cash value.

Standard valuation methodologies are employed to estimate the full cash value of exempt property in Baltimore. For example, if the tax exempt property is a residential property, the state’s computer assisted mass appraisal model is used to estimate full cash value. Sometimes, if the exempt residential property is in a neighborhood with mostly rented properties, the full cash value might be estimated using an income approach relying on average revenue and expense estimates for similar rental housing. If a tax exempt property is similar to a commercial property, full cash value would be estimated using an income approach relying on average revenue and expense estimates for similar properties. Finally, if a property is a unique property, e.g., a historical building on a college campus, the full cash value of such a property would be estimating using a
depreciated cost approach which estimates the cost of replacing the structure and then depreciating that estimate for economic and physical obsolesces.

The data in the table indicate that City owned tax exempt properties account for 71.3 percent of the number of tax exempt parcels, but just 30.4 percent of the estimated value of tax exempt properties in the City. The data indicate that real property owned by the State of Maryland accounts for over one-fourth of the value of all tax exempt property in the City, but just 3.1 percent of the number of tax exempt properties. Similarly, federally owned real property accounts for 5 percent of the value of tax exempt properties, but only 0.4 percent of all tax exempt property in the City.

Tax exempt properties not owned by the federal, state or local government fall into three categories – individual, religious and non-profit/charitable. Tax exempt properties owned by individuals are exempt because the owner is blind, disabled or a veteran. There are 741 such exempt properties in Baltimore, accounting for 0.4 percent of the value of exempt properties. There are 2,084 tax exempt properties owned by religious organizations (11.1 percent of total exempt properties) and they account for 12.5 percent of the value of tax exempt properties. As discussed in the previous section, it is unlikely that significant revenues to support the provision of local services can be generated from these exempt properties.

Non-profit/charitable properties account for just 10 percent of the number of tax exempt properties in the city, but more than one-fourth of the value of tax exempt properties. Within this category there are 62 non-profit/charitable properties (3.3 percent of total properties in this category) that are valued at more than $10,000,000 each, accounting for 43.7 percent of the value of non-profit/charitable properties in Baltimore.
Two thirds of these most value properties are either university owned properties or hospitals. As discussed above, these high valued properties receive most of the benefit from these real property tax exemptions and are in the best position, financially and politically, to contribute to the cost of providing government services they consume.

Properties owned by the City of Baltimore account for the largest number (71.3 percent) of tax exempt properties and largest share (30.4 percent) of the value of tax exempt property in Baltimore. The following table provides a breakdown of tax exempt property in Baltimore owned by the City of Baltimore.\(^2\)

The vast majority of city owned tax exempt property has an exempt code of 56 indicating it is housing and community development property. These properties account for 59.6 percent of city owned tax exempt property, but just 16.4 percent of the value of city owned tax exempt property. Properties with an exempt code of 51 account for 18 percent of all city owned tax exempt property, but only 11.6 percent of the estimated value of city owned tax exempt property. Exempt code 51 indicates the property is in the housing authority. Finally, property with an exempt code of 54 account for 10.5 percent of the number of city owned tax exempt properties, but only 0.2 percent of the value of such properties. Properties with an exempt code 54 are city tax sale properties. Properties in these three categories account for 88.1 percent of city owned tax exempt properties, but only 28.2 percent of the value of city owned tax exempt properties. Public

\(^2\) There are a number of properties in the data set provided with inconsistencies between the exempt code, the exempt type and the owner. For example, one property is coded as being a fire department and says it is exempt because it is city owned, but then the Federal Government is listed in the ownership column. The data reported in this report relies on the information as initially provided which classified property by exemption code and exemption type. Alternatively, if the data were reorganized based on ownership, the number of city owned properties would fall from 13,390 to 13,179 and the value of city owned property would fall from $4.6 billion to $4.4 billion.
schools in Baltimore account for just 1.7 percent of the number of city owned tax exempt properties, but 34.4 percent of the value of city owned tax exempt properties.

<table>
<thead>
<tr>
<th>Exempt Code</th>
<th>Number</th>
<th>Share of Total</th>
<th>Value</th>
<th>Share of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>40</td>
<td>17</td>
<td>0.1%</td>
<td>$178,247,800</td>
<td>3.9%</td>
</tr>
<tr>
<td>41</td>
<td>6</td>
<td>0.0%</td>
<td>$10,241,400</td>
<td>0.2%</td>
</tr>
<tr>
<td>42</td>
<td>455</td>
<td>3.4%</td>
<td>$639,286,210</td>
<td>13.9%</td>
</tr>
<tr>
<td>43</td>
<td>9</td>
<td>0.1%</td>
<td>$59,234,100</td>
<td>1.3%</td>
</tr>
<tr>
<td>44</td>
<td>225</td>
<td>1.7%</td>
<td>$1,581,574,610</td>
<td>34.4%</td>
</tr>
<tr>
<td>46</td>
<td>11</td>
<td>0.1%</td>
<td>$97,480,650</td>
<td>2.1%</td>
</tr>
<tr>
<td>47</td>
<td>1</td>
<td>0.0%</td>
<td>$14,200</td>
<td>0.0%</td>
</tr>
<tr>
<td>48</td>
<td>26</td>
<td>0.2%</td>
<td>$65,451,400</td>
<td>1.4%</td>
</tr>
<tr>
<td>49</td>
<td>44</td>
<td>0.3%</td>
<td>$38,279,100</td>
<td>0.8%</td>
</tr>
<tr>
<td>50</td>
<td>653</td>
<td>4.9%</td>
<td>$247,951,810</td>
<td>5.4%</td>
</tr>
<tr>
<td>51</td>
<td>2,407</td>
<td>18.0%</td>
<td>$533,117,530</td>
<td>11.6%</td>
</tr>
<tr>
<td>52</td>
<td>30</td>
<td>0.2%</td>
<td>$49,113,300</td>
<td>1.1%</td>
</tr>
<tr>
<td>53</td>
<td>3</td>
<td>0.0%</td>
<td>$811,300</td>
<td>0.0%</td>
</tr>
<tr>
<td>54</td>
<td>1,404</td>
<td>10.5%</td>
<td>$8,445,190</td>
<td>0.2%</td>
</tr>
<tr>
<td>55</td>
<td>16</td>
<td>0.1%</td>
<td>$93,626,100</td>
<td>2.0%</td>
</tr>
<tr>
<td>56</td>
<td>7,986</td>
<td>59.6%</td>
<td>$754,164,790</td>
<td>16.4%</td>
</tr>
<tr>
<td>57</td>
<td>45</td>
<td>0.3%</td>
<td>$10,505,500</td>
<td>0.2%</td>
</tr>
<tr>
<td>58</td>
<td>42</td>
<td>0.3%</td>
<td>$209,324,930</td>
<td>4.6%</td>
</tr>
<tr>
<td>59</td>
<td>4</td>
<td>0.0%</td>
<td>$17,575,600</td>
<td>0.4%</td>
</tr>
</tbody>
</table>

13,384    100.0% $4,594,445,520 100.0%

Source: Maryland Department of Assessments and Taxation and author calculations.

Typically, the focus of the discussion of tax exempt properties is on non-profit and charitable organizations, which account for 25.3 percent of the value of tax exempt properties in Baltimore. This category includes a wide variety of non-profit and charitable organizations. There are a large number of housing and economic development organizations and a large number of relatively small single purpose charitable entities. As discussed in the previous sections, it can be problematic trying to generate revenues for the City from these small organizations.
Most often the focus is on a few large organizations. For example, tax exempt properties owned by Johns Hopkins University and the Johns Hopkins Hospital are valued at approximately $1,228.8 million, or nearly one-third of the total value of all non-profit/charitable properties values in the City. The challenge for Baltimore City, however, may be the fact that nearly two-thirds of the value of tax exempt properties in the City is owned by some federal, state or local government entity.

The remaining sections of this paper address the issues concerning property tax exemptions for non-profits.
I. Examine best practices generally in cities and other local jurisdictions that have confronted the issue and developed solutions, particularly collaborative solutions, to the problem.

There is little consensus as to what constitutes a “best practice” when it comes to how local governments have addressed the issue of lost revenue due to property tax exemptions. As discussed throughout this paper, there are numerous approaches local governments have taken to get non-profit organizations to contribute, voluntarily or otherwise, to their fiscal health. These approaches include PILOTs, services in lieu of taxes (SILOTS), user fees and charges, other direct taxes, and state subsidies for lost property tax revenue. The two best, and least controversial, practices have been the use of PILOTs and state subsidies to local governments with substantial exempt property. The latter is used infrequently.

A. PILOTs

Payments in Lieu of Taxes remain the preferred method of getting non-profits to contribute to the fiscal health of local governments.

1. Introduction: PILOTs Generally; How Municipalities Can Establish PILOT Agreements

Payments in lieu of taxes (PILOTs) are voluntary payments made by exempt organizations in place of property taxes. PILOTs have grown in frequency over the past few years, as budgetary pressures on local governments have increased during the recession. Over the past ten years they have appeared in at least 117 municipalities and 18 states (Kenyon and Langley 2010). Several large cities have PILOT agreements, including Boston, Philadelphia, Providence, Baltimore, Detroit, Indianapolis, Minneapolis, and Pittsburgh. Boston’s PILOT program is generally regarded as the most advanced in the nation, and has been referred to by at least two commentators as a “best
practice” (Lustig 2010, and Kenyon and Langley 2010, 45). PILOTs are constitutional in all fifty states because they are voluntary agreements. (However, as discussed below, government efforts to coerce nonprofits into making PILOTs can run afoul of the law.)

PILOTs, however, are more ideal for some municipalities than others. They are best-fitted for areas that rely heavily on the property tax and host large nonprofits that own significant portions of real estate. One Minnesota study found that while PILOTs would significantly increase revenue in some municipalities, there was negligible revenue potential in the majority of Minnesota’s towns and cities (see Kenyon and Langley 2010 and studies cited therein). PILOTs are also not right for every exempt organization. As one observer notes, “PILOTs are most suitable for non-profits that own large amounts of tax-exempt property and provide modest benefits to local residents relative to their tax savings” (Kenyon and Langley 2010, 3). Such organizations may feel an obligation to reimburse local taxpayers for the services they consume, and are wealthy enough to contribute. As such, municipalities usually target hospitals, colleges and universities, and nursing or retirement homes.

PILOTs generally do not raise nearly enough money to compensate for revenue lost to tax exemptions. In 2009, Boston raised $14.9 million in PILOTs from nonprofit universities and hospitals, which is only 4.3 percent of what they would have paid in property taxes (City of Boston 2009). On average, PILOTs comprise less than one percent of municipal budgets (Kenyon and Langley 2010). But, while PILOTs may compose a fraction of what would have been raised through property taxes, they can still be significant. Though the money raised in 2009 by Boston’s PILOT program was far short of what tax revenues would have been, it was still enough to pay for snow removal
for an entire winter (City of Boston 2009). Furthermore, some municipalities—especially small towns that host colleges or universities—will benefit disproportionately from PILOTs. For example, Bristol, Rhode Island’s PILOT agreement with Roger Williams University comprises almost 5 percent of the city’s budget (City of Boston 2009). PILOTs may seem negligible in comparison to lost tax revenue, but they can still be a valuable source for cash-strapped municipalities.

PILOTs are often created through what commentators have called the “carrot-and-stick” approach, in which municipalities will combine friendly negotiations with threatened consequences for not contributing (Gallagher 2002). On the positive side, local governments will appeal to nonprofits’ sense of fairness by pointing out that since they benefit from municipal services, they should help local taxpayers shoulder some of the burden. In 2010 the city of Cambridge, Massachusetts wrote a letter to local nonprofits that stated: “It is only fair to expect exempt property owners to make some contribution towards the cost of municipal services” (Kenyon and Langley 2010, quoting City of Cambridge Pilot Request letter, February 6, 2010). The letter also explained that such payments would ensure the city could provide an adequate level of services, which would in turn benefit exempt organizations. Universities are particularly susceptible to this reasoning, because they want surrounding communities to be safe and well-functioning in order to attract students. Agreeing to make PILOTs can also improve an exempt organization’s public image, which is especially persuasive for nonprofits that have bad relations with the local community.

But appealing to the non profit community’s good will does not always result in the desired results. Then, local governments often threaten to impose legislative or
administrative penalties on exempt organizations that do not agree to PILOT programs.
For example, in 2001 the City of Baltimore dropped a proposed energy tax on all nonprofits after the city’s hospitals, colleges, and nursing homes agreed to make a $20 million PILOT over the course of four years (Anft 2001).

In April 2010, Baltimore faced a $121 million budget shortfall and the mayor introduced a plan to balance the budget that included an "exempt bed property fee" or bed tax of $350 per bed per year on the city's largest colleges, universities and hospitals (Rawlings-Blake 2011). After some negotiations between the mayor's office, the Maryland Hospital Association, and the Maryland Independent College and University Association, the bed tax proposal was dropped in exchange for a new six-year PILOT agreement. Under the agreement, the hospital and college associations agreed that 16 of their members located in Baltimore would make cash payments, termed "special assessments," totaling $20.4 million from fiscal 2011 through fiscal 2016, with the payments purposely front-loaded in recognition of the immediate fiscal crisis (id.). The agreement allowed the member institutions to determine as a group how much each institution would contribute to the total, but together Johns Hopkins University and two Johns Hopkins medical institutions agreed to contribute approximately half. The agreement also stipulated that the nonprofits would not be subject to an increase in the energy tax and telecommunications tax they pay over the six-year period. As part of the agreement, the city agreed not to seek additional revenue from the member organizations or to impose any new targeted taxes.

In 2002, Harvard University agreed to pay $3.8 million per year through 2054, which was prompted in part by municipal efforts to pass a law that would levy property
taxes on large exempt organizations. Governments can also threaten to challenge a nonprofit’s exempt status. For example, a Philadelphia PILOT Advisory Board decreed, “All nonprofit, non-governmental institutions in the City should pay their fair share for the municipal services and benefits they receive” (City of Philadelphia Executive Order No. 1-94 Payments in Lieu of Taxes). However, the city anticipated that some non-profits would be unwilling to contribute. The Philadelphia PILOT Advisory Board explicitly stated that, “In the event the Board is unable to enter into a PILOTs/SILOTs agreement with a nonprofit institution whose status as an institution of purely public charity is legally unclear, the Board shall refer the matter to the Law Department, the BRT, and the School District, with a recommendation to institute a challenge to the institution's tax exemption” (Executive Order No. 1-94 Payments in Lieu of Taxes).

Even if such a challenge is baseless, exempt entities might choose to make PILOTs instead of engaging in costly litigation (Leland 1994). Municipalities also can influence nonprofits through their control of “building permits, zoning decisions, and other factors that influence nonprofits’ decisions” (Kenyon and Langley 2010). As one observer notes, “Municipalities often find their hand to be strongest when a university or other nonprofit is expanding and needs a zoning waiver or other approval . . . .” (Brody 2010, 661).

Cities must use caution, however, as courts will sometimes strike down municipal actions motivated purely by a nonprofit’s refusal to agree to PILOTs.³ Overly coercive efforts can also sour relations between local governments and nonprofits to the detriment

³ Gallagher (2002) (citing Pacer Inc. v. City of Middletown, 635 N.Y.S.2d 704 (App. Div. 1995) ruling that the City of Middletown could not deny a special-use permit solely because the applicant refused to make a PILOT); see also Kenyon and Langley 2010, 37 (citing Northwestern University v. City of Evanston, 2002 U.S. Dist. LEXIS 17104, *25 (N.D. Ill. Sept. 11, 2002) (holding that the City of Evanston could not restrict Northwestern University’s future developments because it would not agree to make PILOTs).
of the entire community (Kenyon and Langley 2010). Furthermore, PILOTs usually target large organizations, which have the resources to challenge real or perceived coercion in court. Ensuing litigation can prove expensive for municipalities, and the nonprofit sector has a very successful track record of defending challenges to tax exemptions. Due to these risks, “threatening to use the stick appears better than actually using it” (Kenyon and Langley 2010, 38).

2. Best Practices: Methods Used By Municipalities To Establish PILOT Agreements

Different types of PILOTs are appropriate for different municipalities. Large cities that host several nonprofits—such as Boston, which is home to dozens of colleges and universities—often pursue systematic PILOT programs that can be applied uniformly to all participating organizations. Smaller municipalities that have few nonprofits, but still lose significant revenues to exemptions—such as New Haven, Connecticut, which is home to Yale University—are better served by reaching out to individual organizations and establishing unique agreements. Nonetheless, all PILOT programs face similar obstacles. This section will identify some common challenges, and provide examples of best practices used to address them.

i. Maintaining Good Relations with the Nonprofit Community

The first impediment to PILOT programs is simply convincing exempt organizations to participate: since PILOTs are voluntary, nonprofits are free to ignore cities’ requests for payments. As discussed above, the “carrot-and-stick” method is widely used. This strategy is most successful when municipalities make a conscious effort to establish good relations with the nonprofit community. Professor Brody

---

4 Brody (2010, 621) (“...the nonprofit sector continues to achieve remarkable success in state supreme courts and statehouses in defending property-tax exemptions”).
observes: “How cities and [nonprofits] negotiate is . . . important, as either party can feel unappreciated and slighted.” (Brody 2010, 621“ . . . the nonprofit sector continues to achieve remarkable success in state supreme courts and statehouses in defending property-tax exemptions”).

Boston has set a leading example in this regard. In 2009 Mayor Thomas Menino established a PILOT Task Force to review and improve the city’s existing PILOT program. He invited representatives from Boston’s largest exempt organizations to participate in the formulation of new policies. The list of invitees included university presidents, hospital executives, and other high-level figures in the nonprofit community. Despite their divergent interests, the inclusion of nonprofit representatives allowed Boston’s PILOT initiatives to be “collaborative and driven by consensus” (Lustig 2010, 609). Boston’s nonprofits also favor this arrangement because it reduces uncertainty: by participating in PILOT policymaking, they know what to expect from the city and can plan their budgets accordingly. Conversely, nonprofits in other cities sometimes express frustration when the government makes unanticipated PILOT demands (Kenyon and Langley 2010).

Boston’s creation of the Task Force also had unforeseen political benefits: by inviting nonprofits to participate, the City created publicity and raised awareness about the negative impact tax exemptions have on the surrounding community (Lustig 2010). This increased public pressure on nonprofits to make PILOTs. The Task Force has also used transparency as a political tool. Nonprofits complain that “PILOTs are often haphazard, secretive, and calculated in an ad hoc manner . . . .” (Kenyon and Langley 2010, 3). Appealing to this sentiment, the Task Force adopted “transparency and
consistency” as one of its core principles. This appeased exempt organizations, but it also left them accountable to both the public and to other nonprofits if they decide not to contribute (Lustig 2011). The Task Force periodically publishes data on PILOT payments, which allows citizens to see which organizations do not make PILOTs. It also creates peer pressure from other members of the exempt community: Eric Buehrens, President and CEO of Boston’s Beth Israel Deaconess Hospital, stated: “I’d hate to feel like I was the only guy paying my taxes” (Lustig 2011, 20).

Boston’s inclusion of representatives from the nonprofit community could be considered a best practice for maintaining healthy relations with PILOT participants. Nonprofits appreciate being able to participate in the Task Force because it allows them to voice their concerns and avoid surprises. At the same time, it creates publicity about PILOTs and exemptions, which ramps up public pressure for nonprofits to make payments. The Task Force’s commitment to transparency eases concerns of unfair or coercive tactics, but it also forces nonprofits to face disapproval from the public and from fellow exempt organizations if they do not contribute. Because it appeases nonprofits while benefiting municipalities, local governments would be wise to invite exempt organizations to participate in PILOT policymaking.

**ii. Calculating the Proper Amount for PILOT Requests**

Another common issue is deciding on the appropriate amount to ask from each nonprofit. One method involves assessing the community benefits offered by each organization, and reducing the requested amount if an organization provides substantial levels of community service (Kenyon and Langley 2010). For example, Philadelphia’s Voluntary Contribution Program in the 1990s sought PILOTs from charities that did not
meet the Pennsylvania Supreme Court’s definition of a “purely public charity” (Glancey 2002, 214). In other words, Philadelphia exempted organizations from PILOTs if they provided a high level of public services. Similarly, Boston’s program allows for deductions for “extraordinary community services” (City of Boston 2009). The criteria for considering such services include: whether they directly benefit Boston residents, whether they support the City’s mission and priorities, whether they are quantifiable, and whether they “emphasize ways in which the City and the institution can collaborate to address shared goals. Examples of such services include academic scholarships, free medical care, volunteer workshops, youth employment, job initiatives, and job training programs (City of Boston 2009). Deducting from PILOTs in exchange for community services allows cities to improve their residents’ quality of life, while simultaneously allowing exempt organizations to reduce the amount of money they are expected to contribute.

PILOTs can also be calculated based on a measure of a nonprofit’s value (Kenyon and Langley 2010). In structuring its PILOT program, Boston’s PILOT Task Force considered three such methods: payments based on square footage of property; payments based on units, such as number of students enrolled or number of hospital beds; and payments based on property value. It decided that the property value method was most appropriate, because PILOTs are meant to compensate for lost property taxes. Alternatively, Cambridge, Massachusetts uses square footage of real estate to determine PILOT requests, whereas Baltimore uses an organization’s annual income (Kenyon and Langley 2010, 39).
Cambridge’s method may be more appropriate in municipalities where exempt real estate is difficult to valuate. Baltimore’s system may be best in cities where nonprofits have incomes that are larger than their property holdings, or where an organization’s ability to pay is a priority. Smaller municipalities, on the other hand, usually use different techniques than large cities. New Haven’s PILOT agreement with Yale University is based on the number of students living on campus and the number of employees. This arrangement, which is unique to Yale and does not apply to other PILOT agreements, is typical of a smaller municipality that hosts only one or two very large exempt organizations. Because Yale is the only local organization of its kind, it is more sensible for New Haven and Yale to agree to a unique agreement instead of establishing a systematic method (Kenyon and Langley 2010, 3).

When adopting a methodology for calculating PILOTs, municipalities should consider nonprofits’ exempt footprint, as reflected by the property value and square footage methods used by Boston and Cambridge. Their ability to pay, which is a primary consideration behind Baltimore’s annual income criterion, is also an important factor. Finally, reducing PILOT amounts for public benefits provided, as seen with Boston’s “extraordinary community services” standard, is a useful tool for improving a city’s quality of life and reducing the burdens of government. Using concrete and quantifiable methods reduces the appearance of unfairness, which increases exempt organizations’ willingness to comply with municipal PILOT requests.

iii. Reducing Uncertainty: Trigger Provisions; Long-term v. One-time PILOT Agreements

As mentioned above, Boston’s nonprofits enjoy their positions on the PILOT Task Force in part because such participation reduces uncertainty. Governments feel the
same: predictability in PILOT payments facilitates the process of designing a budget. (Brody 2010, 45 “municipalities above all seem to be seeking a predictable revenue stream that they can count on for budgeting purposes”). Municipalities have at least two tools available to reduce uncertainty surrounding PILOTs. The first is to establish trigger provisions for inclusion in a PILOT program (Kenyon and Langley 2010). One method currently used by the City of Boston is to approach nonprofits about PILOTs when they purchase new, non-exempt property. This is favorable for nonprofits because they can take such costs into consideration when planning expansions. Municipalities favor this method because it allows them to mitigate sudden drops in their tax base. It also improves municipalities’ bargaining power, because organizations under expansion will likely need zoning or building permits from the government. However, trigger provisions raise the cost of entry for new nonprofits, and might discourage exempt entities from making expansions and investments that would benefit the community.

The second method for reducing uncertainty is to pursue multiyear contracts instead of one-time payments (Kenyon and Langley 2010, 40). This gives both nonprofits and municipalities concrete figures to work with during long-term budget planning. Several such agreements currently exist: the Massachusetts Institute of Technology, for example, has a multi-year agreement with Cambridge that is subject to a 2.5 percent annual increase (Kelderman 2010). Similarly, Harvard University agreed to pay Watertown, Massachusetts $3.8 million per year until 2054, with a three percent annual increase (Flint 2002). While such arrangements reduce uncertainty for both parties, nonprofits still may oppose agreeing to future payments. They may also worry about creating a “slippery slope” that allows municipalities to increase PILOT requests year
after year. For example, in Pittsburgh several nonprofits make an annual PILOT to the city and insist that each year’s payment is a “gift” that establishes no precedent for future contributions (Brody 2010, 45). Nonetheless, long-term contracts are preferable to one-time payments for municipalities, and should be pursued where nonprofits are willing to agree to such arrangements.

The world of PILOTs is vast and research on such programs has been scarce. And despite the general view that PILOTs are an effective method for raising revenue, only a small percentage of non profits actually make such payments. One recent study found that only 9 percent of non profits nationwide were making payments under PILOT agreements (Salamon, et. al. 2010). And Lustig (2010) found that 26 percent of localities with exempt property received PILOTs. While these small numbers reflect the fact that most nonprofits do not have the financial resources to make voluntary payments, two thirds of the largest research universities do not make routine PILOT payments (Lemov 2010).

B. State Financial Assistance

Concerns of unequal burden-sharing between local and state governments, as well as between municipalities, must be considered when formulating exemption policies. When municipalities cannot raise adequate revenue because of exemptions, they are more likely to antagonize local nonprofits, which can lead to unfavorable outcomes (Brody 2010 B, Kenyon and Langley 2010, 34). A handful of states have enacted laws to address this issue. Connecticut passed a statute that requires the state government to reimburse municipalities for up to seventy-seven percent of taxes lost to exempt property

---

5 Kenyon and Langley 2010 was the first study to comprehensively gather information on PILOT activity nationwide.
owned by universities and hospitals.\textsuperscript{6} Rhode Island has an identical requirement, except that payments are limited to twenty-seven percent of lost taxes.\textsuperscript{7} Maine and Wisconsin also have similar provisions, which are narrower in scope and require smaller payments (Brody 2010, 644). In 2002 Virginia passed an amendment to the state constitution that shifted the authority to grant tax exemptions to municipalities. Fairfax County subsequently voted to tax all future property purchased by nonprofits (Kenyon and Langley 2010, 42).

These laws are helpful models for states that wish to help overburdened municipalities. While not appropriate for every state, some states might find value in such programs. Connecticut, for example, derives significant economic benefits from Yale University. Yale’s attractiveness to prospective students is based in part on having a vibrant surrounding community in the town of New Haven. Yet New Haven loses significant revenue due to Yale’s exempt status. Thus, Connecticut benefits from assisting New Haven financially, because doing so helps maintain Yale’s ability to attract students and stimulate the surrounding economy. This helps explain why Connecticut paid New Haven $37 million in 2009 to compensate for lost property taxes. (Brody 2010, 644).

While most states do not reimburse local governments for lost property tax revenue, the instances in which they do are widely considered “best practices.”

\begin{footnotes}
\footnote{\textsuperscript{7} R.I. Gen. Laws § 45-13-5.1 (2008).}
\end{footnotes}
II. Determine the circumstances when a PILOT should (and should not) be “required” of a tax exempt organization and how its particulars should fairly be determined.

With three minor exceptions, as a general matter, no states require payments in lieu taxes to local governments by tax exempt organizations. A review of statutory and administrative law in all fifty states revealed no such requirements. Moreover, a literature review of legal and non profit journals found no circumstances in which PILOTs should or should not be required by law.

Only three states have mandatory PILOT laws specifically addressing tax exempt nonprofit entities, however, these laws generally fall into circumstances when a nonprofit entity derives income from rental activities. For example, Delaware Code Section 8156 provides:

Any church, religious society, charitable corporation or nonprofit organization granted a tax exemption pursuant to this subchapter, shall pay to the county and other political subdivision in which the project is situate, in lieu of taxes, a special assessment in an amount not less than 10% of the gross rentals derived from the project, less the cost of utilities and the cost of providing social services to the elderly persons residing in the project. This sum shall be divided between the county and other political subdivisions having authority to levy ad valorem taxes on land and improvements in which the project is situate in proportion to their respective tax rates.

This statute was applied to the specific circumstance when an organization provided housing to the elderly. Oregon has a similar law which applies only to farm labor camps and childcare facilities. In addition, the law applied to situations when the state housing authority had some level of control in the nonprofit organization.

In lieu of real and personal property taxes, each nonprofit corporation eligible for a tax exemption under ORS 307.485 shall pay to the treasurer of the county on or before November 15 an amount equal to 10 percent of the rentals for the period ending the preceding October 15, submitting with the remittance a form supplied by the Department of
Revenue stating the rental and certifying compliance with the requirements of the State Fire Marshal, local health officer or Child Care Division, as applicable. (ORS 370.490.)

Similarly, Nebraska requires non profit hospitals which provide office building or office space to private enterprises charge tenants “a sufficient amount of rent so that a portion of the rent shall be in lieu of taxes. Such payments in lieu of taxes shall be paid to the county treasurer.” Neb. Stat. Ann. 18-2137.

Two states legislatively authorize local governments to enter into PILOT agreements for housing authorities. But these states only grant the power to negotiate PILOTs. In South Carolina, Code Section 12-37-240 states,

When any nonprofit housing corporation owns property within a county or municipality which is exempted from ad valorem taxes under an act of the General Assembly, the county or municipality or both are authorized to contract with such corporation for payments in lieu of taxes for services rendered by the county or municipality.

Similarly in New Hampshire, the law leaves open the possibility of voluntary PILOTS from various nonprofit organizations providing housing for the elderly.

72:23-n Voluntary Payments in Lieu of Taxes -The governing body of any municipality may enter into negotiations for a voluntary payment in lieu of taxes from otherwise fully or partially tax exempt properties, and may accept from such properties a voluntary payment in lieu of taxes.

Many states have a variety of statutes authorizing payments in lieu of taxes by governmental or quasi governmental entities. For example, Kansas law states that cities may impose payments in lieu of taxes on state industrial revenue bond property, but imposition of such payments are not mandatory. K.S.A. 12-1742. Arizona allows local governments to negotiate PILOTs with regional attraction districts. A.S.A. 48-6254. Kentucky allows local governments to enter into PILOT agreements with government
utilities. Kent. Stat. Ann. 247.968. There are little or no legal authorities indicating how the required PILOT programs for rental property should be implanted. Indeed, there are neither regulations nor judicial decisions interpreting the foregoing statutes.

But no state has a broad based requirement for PILOTs aimed at private non profit organizations. A review of tax exempt literature found no studies or commentary suggesting when a state should or should not require a PILOT program. The absence of both legal authority and literature may result from the fact that a mandatory PILOT is more akin to a tax than a traditional PILOT.
III. Identify alternatives to PILOTS for raising appropriate revenues from tax exempt organizations.

Local governments use several methods, apart from PILOTs, to raise revenue from organizations otherwise exempt from property taxation. However, local governments raise significantly less revenue from these alternate sources than they can and do from PILOTs. The current literature on services in lieu of taxes (SILOTs) and other alternatives to PILOTs is very limited. There are few articles (and none of an academic nature) solely devoted to discussing alternatives to PILOTs. Indeed, practically all information concerning alternatives to PILOTs is contained within literature on PILOTs. The most recent literature on the subject is a 2010 report by the Lincoln Institute of Land Policy which includes a significant discussion of PILOT alternatives as a method of changing the conventional debate about the issue of taxation of non-profits (Kenyon and Langley 2010).

Alternatives to PILOTs generally comprise three distinct categories: Voluntary Contributions; Contingent Contributions; and Compulsory Contributions. Voluntary contributions, which include SILOTs, are arrangements that non-profits make with municipalities to directly provide or subsidize community services (Kenyon and Langley 2010). In the limited literature, there is some confusion as to the definition of a SILOT. In addition to directly providing services, sometimes SILOTs are defined as monetary contributions for specific government services such as fire, police or schools.

There are several examples of monetary payments for specific services in the higher education community. Duke University gives money annually to the city of Durham, NC for fire protection services. These payments are based on a formula (Nelson,
Stanford University has contributed to the Palo Alto community with periodic gifts such as a donation of $10 million to the local school district to help fund a new middle school (Nelson 2010). Other non-profits purchase equipment (usually public safety related) and donate the equipment to the local government. For example, the University of Michigan and Northwestern University both have purchased fire trucks for their respective local municipalities. The University of Pennsylvania has donated land to the city for a public school. Washington University pays for part of the costs of city police patrols on or near campus (Nelson 2010).

A SILOT may also involve a non-profit directly providing a municipal service, although this appears to be a much rarer occurrence than monetary contributions. The most common example of such a service involves police and public safety. In Nashville Tennessee, Vanderbilt University has taken on the responsibility of police protection for the areas and neighborhoods surrounding campus (Nelson 2010). This relieves the city of some of its public safety costs.

Tufts University and Somerville, Massachusetts entered into an agreement in 2004 that involved both PILOTs and SILOTs. Under the terms, Tufts would make payments to the City for a ten year period in the amount of $125,000 annually through the year 2013. Tufts also offers a reduced charge for course audits, waiver of rental fees for the use of facilities, and financial support for local children in Tufts' early childhood programs. Somerville residents also receive additional consideration in the undergraduate admissions process and the University commits to an investment of at least $300,000 in need based grant aid each year for undergraduate students from Somerville.
Emory University has an agreement with DeKalb County to provide certain amounts of health care to county residents in addition to PILOT payments to the school district. Some organizations voluntarily keep otherwise exempt property on the tax rolls. For example, Rice University pays property taxes on the president’s residence.

Contingent Contributions are levied by the local government as a replacement for property tax revenue. There are two distinct types of contingent contributions: municipal service fees and user fees. Municipal service fees directly target non-profits as they are only required to be paid by the owners of tax-exempt properties. Such service fees are rare. But the best example is the city of Minneapolis, which since 1973 has charged street maintenance fees on tax-exempt properties based on the square footage of the property (Hjelle 2009, Kenyon and Langley 2010). Municipal service fees are infrequently used by local governments because they single out organizations that are otherwise exempt from tax.

User fees, which are levied on all properties, are a more popular option for local governments to levy. Municipalities generally impose user fees as a replacement or addition to property tax revenue to fund individual services such as trash collection, park maintenance, and street repairs. They are widely used by local governments throughout the Untied States. Indeed, local governments raised over $220 billion in user fees and charges in 2009 (U.S. Census). A study by Johns Hopkins University in 2010 found that 42 percent of non profits nationwide paid some form of user fee to local governments (Salamon, et. al. 2010)

User fees, however, are not without controversy as it can often be unclear whether a fee is legally a fee or a tax that, in some states, cannot be enforced on non-profits. In
2010, the City of Houston adopted a “drainage fee” designed to raise $125 million a year toward improving storm water systems. The city will charge the fee to all property owners and has indicated that no exemptions will be granted to charities or other non-profit organizations. The non-profit community is Houston is challenging the fee as an illegal tax. Similar fees have been adopted in Richmond, VA., Lafayette, Ind., and Verona, Wisconsin. State laws interpret similar fees differently; for example, requiring non-profits to pay a fire protection fee is legally permissible in West Virginia but is unconstitutional in Massachusetts (Youngman 2002). But more importantly, user fees fall on all organizations within the city, taxable and exempt. Imposing user fees in addition to conventional property taxes creates political and economic issues beyond the exempt community.

Compulsory Contributions are alternative taxes that a municipality is legally allowed to levy on non-profits in lieu of traditional property taxes. Unlike Contingent Contributions, these are legally defined as taxes. This option is only permissible in states that allow local governments to impose any kind of taxes on exempt organizations. The constitutions of 17 states (UT, NM, OK, AK, NE, ND, SD, MS, LA, AL, SC, KY, MI, NJ, NY, VT, and ME) prohibit any taxation of charitable non-profits (Kenyon and Langley 2010). One study found that 17 percent of all non-profits pay some form of direct taxes to state and local governments (Salamon, et. al. 2010). The direct taxes levied are usually admissions taxes, certain excise taxes, and in some states sales taxes. (Salamon, et. al. 2010). But these taxes make up a very small amount of municipal revenue. Direct taxes or compulsory taxes are not levied often because they are disallowed in most states. The exemption from property taxes enjoyed by nonprofits is
usually carried over to other types of direct taxes. That is, a non profit that is exempt from property tax is usually exempt from all compulsory levies.

It should be noted that most attempts to directly impose taxes on non profits have failed. In Massachusetts, for example, the House rejected a plan to tax college endowments in excess of $1 billion at 2.5 percent. The tax would have been imposed on eight private colleges, mostly located in Boston, generating an estimated $830 million in tax revenue. In Pittsburgh, the Mayor unsuccessfully sought to expand the scope of payroll taxes to include nonprofits as a way to compensate for the $15 million city pension fund budget deficit (Lord and Barnes 2009).

Cities with large universities and hospitals have contemplated alternative taxes, including tuition taxes on colleges and universities and hospital bed taxes\(^8\). Pittsburgh Pennsylvania recently proposed tuition taxes. In Pittsburgh, the mayor proposed a one percent Fair Share Tax on the tuition paid by the city’s 100,000 students (Fischer 2010). The mayor was prompted by the fact that one third of the city’s property was exempt from tax and about 20 percent was owned by universities and colleges. If approved the tax would have raised approximately $16 million a year. The tax proposal was withdrawn after protests by students and parents and an agreement by the universities to pay PILOTs to the city. Those taxes would have been levied on a percentage of tuition paid by students enrolled in universities within the cities. But the tax proposals were abandoned the proposals after the cities managed to establish PILOT arrangements with local colleges and universities.

\(^8\) Hospital bed taxes are imposed on both for and non profit medical facilities. While these taxes have been discussed at the local level, they are exclusively imposed by state governments.
Providence, Rhode Island has also considered a tuition tax on universities and colleges in its boundaries. Brown University owns real property worth about $1 billion and saves about $38 million from its tax exempt status. In 2011, Brown had made contributions of about $4 million to the city which included property taxes on land used for commercial purposes. Faced with a large budget deficit, the city requested Brown pay an additional $40 million over ten effectively doubling the universities payments. The city held out the possibility of seeking a tuition tax if a new PILOT was not negotiated. The tax would have been a flat $150 per semester for every student at the four colleges in the city. The city reached agreement with other universities, but is still negotiating the terms with Brown.

In December 2009 Jerry Fried, the mayor of Montclair, New Jersey, asked the state legislature to pass a law that would require universities to charge all students $50 per semester to pay for municipal services. This initiative was backed by almost one hundred mayors, who offered their support at New Jersey’s League of Municipalities’ convention in November 2009. In explaining his request, Fried said he wished to recoup some costs of municipal services that university students and staff members enjoy for free: “Obviously we provide a lot of services and don’t get paid back from that. There’s significant costs involved” (Khavkine 2009)

Beyond tuition taxes, cities have also proposed levying special energy taxes on non-profits. Three Maryland counties levy energy taxes—a tax based on an organization’s utility bills—solely on nonprofits classified under 501(c)(3), including churches, universities, and hospitals (Anft 2001). In 2001 and 2004, the Mayor of

---

9 Energy taxes have been proposed in several states but have never been implemented. Typically, an energy tax proposal would impose a rate as a percentage of a non-profit organization’s utility costs. The rates proposed in Maryland were for example eight percent.
Baltimore proposed a similar energy tax on non-profits. The city later abandoned the efforts after negotiating PILOT agreements with the city’s nonprofit hospitals, colleges, universities, and nursing homes.

Alternatives to PILOTs exist and are used throughout the United States. But their use is limited and sporadic. Indeed, the authors conducted a survey of 10 jurisdictions with populations between 500,000 and 700,000 or metropolitan populations of over 1,000,000. Only one jurisdiction received alternative payments; and only three received PILOTs. See Appendix B for survey results.
IV. Examine the options for responding to the increasing commercial activity engaged in by tax exempt organizations in some jurisdictions that often escape taxation.

The issue of exempt organizations engaging in commercial activity has confronted all levels of government for decades. Non profits organizations have benefited significantly from their exempt status. The engagement of non profit organizations in commercial activity presents several issues for policy makers. First, exempt organizations are by definition providing a public good which justifies their status. Commercial activity calls into question whether the organization is acting according to the legal authority that creates the exempt status. Second, given the large amount of tax expenditures associated with exempt organizations, policy makers must consider the revenue losses associated with allowing non profit organizations to carry on commercial activities. Moreover, non profit organizations engaging in commercial activities benefit from market advantages not available to for profit competitors to the extent they maintain their tax exempt status.

At the federal level, charitable institutions are provided tax-exempt status. Under the Internal Revenue Code 501(c)(3), charitable institutions “operated exclusively for” charitable purposes are exempt from federal income taxes. However, the exclusivity requirement of the statute is not applied strictly. Several years of jurisprudence has resulted in the definition of “exclusive” as merely “primarily” (Colombo 2002). This exemption can be challenged, however, when the charitable institution conducts a commercial activity on its premises. Where an organization engages in “substantial amounts of activities that are unrelated to their charitable purpose,” they lose their federal tax exemption (Pena and Reid 2001). This suggests that the federal government will sustain the exemption unless the unrelated activity is excessive. Moreover, the Treasury
Regulations specially address trade or business activity. Treas. Reg. 1.501(c)(3)-1(e) provides that an organization does not lose its exempt status if it conducts a trade or business but the “operation of such trade or business [must be] in furtherance of the organization’s exempt purpose.” The IRS has generally allowed “liberal amounts of unrelated commercial activity” (Pena and Reid 2001).

At the state level, non profits organizations enjoy exemption from the locally imposed property tax. Depending on the jurisdiction, however, this exempt-status is potentially sacrificed when a charitable institution permits a commercial activity on its premises. Unlike the federal regulations, each state’s tax code addresses an institution’s charitable status differently and no uniform rule can be broadly attributed to all states. Although each state is unique, several common themes can be derived from the statutes and case law.

Generally states address the exempt status of a charitable institution that permits commercial activity on its premises in one of three ways: (1) “statutes requiring that property must be used exclusively for the organization’s charitable purpose; (2) statutes requiring the primary or dominant use of the property for the organization’s charitable purposes and (3) statutes that allow partial use of the property for other than charitable purposes” (Kosaras 2000). Generally, states which require “exclusive use” do not strictly construe this requirement and those adopt a more lenient partial exemption approach require that the nonexempt portion be clearly defined or calculable.¹⁰

This issue has increasingly become problematic for many charitable institutions such as hospitals which have been classified as non-profit entities for decades as more

¹⁰ Some states have adopted a time test which calculates the nonexempt portion based on the percentage of time it is used for nonexempt purposes. Alternatively, some states permit a proportionate use test of the property (Kosaras 2000, 146).
organizations have engaged in commercial activity to raise revenue. However, where the hospitals generate significant profits, many governments assert that they are no longer a purely public charity which should qualify for exemption. Many states have held that the entity sustains its exempt status so long as it does not have a profit motive. However, courts have acknowledged that accruing a revenue or profitability does not necessarily imply that the entity is organized for a profit-motive.

More generally, a statute providing for exemption from property taxes will similarly authorize a partial exemption where property otherwise exempt is used for both exempt and nonexempt purposes. 71 Am. Jur. 2d § 306. The authority for such authorization, however, varies from state to state. Additionally, this position is relatively new among those states where direct statutory authority for partial property tax exemptions does not exist. Due to this novelty, not every state has been presented with an opportunity to directly address this particular issue, although a majority has.

Most states suggest that it is the use of the property that gives rise to its tax exemption, rather than mere ownership. And it is often required by statute that such satisfactory use, whether charitable or otherwise, be “exclusive use,” “predominant use,” or the “sole use” of such exempt property. Failure to satisfy these strict standards has historically resulted in a loss of exempt status for the entire property, unless statutory provisions provide otherwise. As already mentioned, several states have enacted statutory provisions that in effect create “exemptions” from these strict standards.

Where the majority of confusion in this area lies is where state legislatures have not provided for such “exemption” provisions. In these states case law generally finds
that, although tax exemption provisions are to be read strictly against the taxpayer, tax exemption analysis should be guided by reasonableness.

The Supreme Court of Minnesota addressed for the first time in its state, “whether the exempt and nonexempt portions of a building are separable for the purposes of assessment for taxation . . . .” *Christian Business Men’s Committee of Minneapolis v. State*, 38 N.W.2d 803, 810 (Minn. 1949). In that case the court was presented with a situation where the first floor of a three-story building was rented out to third party commercial tenants, while the remaining two floors continued to be used for the charitable purposes of its owner. The court ultimately held that a building did not lose its tax-exempt status where even a substantial portion thereof was rented out and used for commercial purposes. Of particular relevance, however, is the reasoning employed by the court in reaching its conclusion. There the court stated:

“In the light, however, of modern conditions involving the construction of large buildings, often consisting of many stories, there seems little justification for adhering to an assumed arbitrary rule of thumb that a building is necessarily taxable or nontaxable in its entirety. Big buildings have become the rule in the congested business areas of large cities where ground space is at a premium. The passage of time does not of itself amend the constitution, but it does amend the factual problems, human and physical, to which the constitution applies. If the purpose of tax exemption is to be achieved, we cannot ignore significant changes which have taken place in our physical surroundings. A tax-exempt institution obviously should not be denied the opportunity of acquiring an advantageous location in a congested downtown area simply because it may not be able to occupy for its restricted purpose an entire building consisting of several floors. Although it is a general rule that constitutional provisions exempting property from taxation are to be strictly construed, such provisions, though not subject to extension by construction or implication, are to be given a reasonable, natural, and practical interpretation in the light of modern conditions in order to effectuate the purpose for which the exemption is granted. The better rule, which we now adopt and which is followed by many other jurisdictions wherein property is entitled to tax exemption only if it is used *exclusively* for a tax-
exempt purpose, is that when a building is owned by a charitable or other tax-exempt institution and one substantial part thereof is directly, actually, and exclusively occupied by such institution for the purposes for which it was organized and another substantial portion thereof is primarily used for revenue by rental to the general public, such building with the grounds thereof is pro rata exempt from taxation and pro rata taxable according to its separate uses, and it should be assessed and taxed on that portion of its proper assessable value allocated to the taxable use, after deducting from its overall assessable value the portion thereof properly allocated to the proportionate tax-exempt use.”

_Id._ at 811.

The views of the court in Minnesota and those similarly interpreting these tax exemption provisions are not universally followed. The State of Alabama, without any statutory authority to the contrary, has consistently found that where a portion of property otherwise exempt from taxes is used for nonexempt purposes, and such use is not incidental to its exempt uses, the entire building becomes taxable. _See Most Worshipful Grand Lodge of Free & Accepted Masons v. Norred_, 603 So.2d 996 (Ala. 1992). No partial exemption in these situations has been recognized. _See id._ at 1000 (“No partial . . . exemption is available.”). Although Alabama’s position is in the minority, it is not alone.

On the other end of the spectrum it appears that only one state, Arkansas, allows for a tax exempt property to keep its status in entirety, at least when property is held for church or religious purposes. Under ARK. CODE ANN. § 26-3-206(a), church property that is used for commercial or business purposes is to be assessed for ad valorem tax purposes. However, under § 26-3-206(b), “in the event any property is used partially for church purposes and partially for investments or other commercial or business purposes, the property shall be exempt from the ad valorem tax.” Treatment of similar situations when exempt property other than religious property is involved isn’t necessarily clear.
As illustrated in Appendix C, twenty states permit partial exempts by statute. In another twenty five (25) states the courts have determined that a non profit is entitled to a partial exemption. In four (4) states any impermissible use results in complete loss of exemption. And in Arkansas non profits enjoy exempt status despite engaging in commercial activity. Overall, the research provided mixed results. The state of the law is clearer in some states than in others.

While there is an abundance of judicial and statutory authority for dealing with non profits engaged in commercial activity, there is no literature assessing the effectiveness of policies designed to deal with the issue.
V. Examine the options for retaining tax revenues from properties being sold by taxpaying property owners to entities exempt from taxation.

There are no statutory or other legal authorities for a local government to retain tax revenue from properties sold by a taxable entity to a non taxable entity. Moreover, there is no legal or policy literature discussing the issue. In every state, whether the purchased property is taxable or not depends on its use. If the purchased property will be used exclusively for exempt purposes it remains exempt from tax. The only recourse a local government may have is to challenge the use of the property. For example, if a non profit purchases property and uses it for commercial purposes, the local government would be able to revoke or partially revoke the non profit’s exemption.

There are, however, other methods utilized to control the growth of exempt property. For example, in October 2002 the supervisors of Fairfax County, Va., approved a moratorium on any new nonprofit tax exemption, citing the need to preserve resources in the face of likely budget cuts. This was in response to an earlier decision to grant the World Wildlife Federation a $300,000 annual exemption for its new headquarters (Rein 2002). In November 2002, voters in Virginia then approved a referendum to transfer approval of new exemptions from the legislature to local authorities (Salmon 2003). Fairfax County, Virginia has not approved a property tax exemption for any taxable property purchased by an exempt organization since that time.

The idea of local consent before acquired property can be exempt has been discussed in other jurisdictions. A Cleveland research body proposed as "alternatives for balancing the valuable services contributed by tax-exempt organizations and the revenue
needs of local governments" a variety of changes, including: requiring local jurisdiction consent before a tax-exempt entity can buy taxable property; phasing in tax exemption on newly acquired property; phasing out exemption after a specific period; limiting acreage eligible for exemption; adopting a dollar cap on exempt property; and including an allowance in state intergovernmental aid to jurisdictions with a large amount of exempt property (Sheridan, et. al. 2002).

Similarly, Pomp (2002) outlined several options for easing the burden on municipal government faced with expanding exempt properties. The options included: Requiring the permission of the local jurisdiction before any taxable property can be bought by a tax-exempt organization; phasing in the exemption whenever taxable property is bought by an exempt organization; phasing out the exemption after a certain period; limiting the number of acres qualifying for the exemption; setting a dollar limit on the amount of property tax can be exempt; imposing mandatory user fees for all government services; and requiring the state to make payments to jurisdictions containing exempt property.

While the concept of local approval for non-profits to expand their exempt holdings is endorsed by scholars and policy experts, few local governments actually have this authority. But as Fairfax, Virginia illustrates, such authority can be very successful in curbing the expansion of exempt property.¹¹

---

¹¹ A survey of public officials by the authors in ten jurisdictions with populations of 500,000 to 1,000,000 found unanimous support for the concept of local approval of exemptions for property purchased by non-profits.
VI. Review ways to recognize and fairly value the many in kind contributions of non profit organizations.

Non profits in general, and universities and hospitals in particular, contribute to the economic livelihood of local governments. There are several methods of identifying and measuring the economic impact of nonprofits, specifically universities and hospitals, on state and local governments and economies\(^\text{12}\). The studies cover four main areas: studies on the impact of hospitals, hospital complexes, and educational medical complexes; studies on the economic impact of universities; in turn, these are considered as groups of “metroversities” or as what’s referred to as “single-site” studies; studies on the impact of nonprofits at the state or municipal level; and general studies on the economic impact of nonprofits.

The most comprehensive discussion of the topic is set forth in Doekson, et. al. (1997). This study reviewed the most widely accepted methods for ascertaining the economic impact of non profit health organizations. The review resulted in the conclusion that the direct and secondary impacts on community employment and income account for 15 to 20 percent of the total community’s employment and income. In addition, the study concludes that a viable health sector is needed if a community wants to attract industry, business, or retirees.

Doekson, et.al. (1997) reviewed previous work by Erickson, et.al. (1986) of Pittsburgh, Moore (1974) of Syracuse, and a statewide study of Montana by McConner

\(^{12}\) The authors note that there are numerous studies commissioned by universities and non profit hospitals illustrating the economic benefits of such institutions. Invariably, these studies show that the particular university or hospital has a significant impact on economic development.
and Weliever (1989). The first two studies measured earnings, employment, and tax revenue generated for cities. The last study measured salaries, wages, and employment for a state.

Using these studies Doeksen, et.al. (1997) developed three procedures to measure the economic impact of the health sector on a local economy. They measure direct, indirect, and induced economic impacts. Subsequently, they use a Type III multiplier, defined as the ratio between direct employment, or that employment used by the industry initially experiencing a change in final demand and the direct, indirect and induced employment. A Type III employment multiplier of 3.0 indicates that if one job is created by a new industry, 2.0 jobs are created in other sectors due to business (indirect) and household (induced) spending (Doeksen, et. al. 1997 28-30).

For universities, the most widely cited research is Drucker and Goldstein (2007). This work reviews the approaches used to examine the influence of research universities on regional economic development outcomes. The authors assess the methodological advantages and shortcomings of four major research designs evidenced in the literature: single-university impact studies, surveys, knowledge production functions, and cross-sectional and quasi-experimental designs. The authors conclude, based on their review that university activities, particularly knowledge-based activities such as teaching and basic research, have been found to have substantial positive effects on a variety of measures of regional economic progress. For example, the research found that universities had a considerable impact on regional economic development in terms of investment in physical capital, employment, technology development and innovation, and growth of private sector industry (Drucker and Goldstein, 23-24.)
Bartik (2008) studied the effects of both higher education and the health care industry on metropolitan regional economic development. The paper studied various impacts on metro economic development including export-base demand stimulus, human capital development, amenity improvements, R&D spillovers, entrepreneurship increase, reduced intra-metro disparities, model employer effects on labor market norms; and economic development leadership.

Bartik (2008) provides quantitative evidence of the magnitude of economic effects of higher education and medical service industries that occur through the mechanism of providing some export-base demand stimulus to a metropolitan economy. The study estimates that medical service industries pay above average wages, holding worker characteristics constant, whereas the higher education industry pays below average wages; the wage standards of these industries may affect overall metropolitan wages. But, the study discusses other ways these two industries may boost a metropolitan economy, including: increasing local amenities, generating R&D spillovers, increasing the rate of entrepreneurship in local businesses, and helping provide local leadership on development and growth issues.

There are other ways of measuring the contributions of non profits beyond the economic impact on the community. Nicholson, et. al., (2000) identified community benefits by using the economic concept of a public good. That research developed a new method for determining the benchmark amount a nonprofit hospital is expected to provide to retain its tax-exempt status. This standard of valuation is calculated by focusing on the amount of community benefits the hospital should provide equivalent to what a for-profit hospital plus the profits the for-profit hospital earns. Typically this
benchmark is higher than the conventional standard – a nonprofit hospital should provide community benefits that are at least as large as the taxes it would pay if it were a for-profit hospital.

In the medical field, an example of a public good would be flu vaccinations for local school children. The vaccinations would provide benefits to all of the people living in the area by helping to contain the spread of the flu. The use of medical care by either low-income or high-risk individuals can be an important type of public good. Many times public goods are furnished in insufficient quantities because it is difficult to convince many of the people who benefit from it to pay for it. The concept of a public-good provides a verifiable measure of potential community benefits. However, the determination of what is a public good is subjective rather than objective. Nicholson (2000) used the public-good framework to determine a set of hospital activities that could constitute community benefits. The activities included in the study are 1) uncompensated care, 2) the cost of other unbilled public-good services, 3) losses on medical research, 4) taxes, 5) Medicaid shortfalls, 6) Medicare shortfalls, 7) price discounts to privately insured patients, and 8) losses on medical education. As the study acknowledges, the first four have strong justification for why they should be considered public benefits, whereas the last four are more debatable.
VII. Conclusion

This report explores important details in the relationship between the non profit sector and local government public finance, with an emphasis on the property tax. This relationship has two important dimensions. First, the property tax revenue foregone because property owned by non profits is exempt from the real property tax exacerbates the current fiscal stress faced by local governments. Second, because non profit organizations are exempt from paying the real property tax, other taxpayers pay higher property taxes than they otherwise would raising questions of fairness.

The research discussed in this report finds that PILOTs remain the most effective and widespread means of collecting revenue from organizations that are otherwise exempt from property taxes. There is no authority in any state for requiring the imposition of PILOTs, but there are many options to using PILOTs. PILOTs may not be appropriate for small non profits with limited resources; they are typically most effective in offsetting the costs of locally provided services when they are negotiated with larger non profit organizations like universities and hospitals. PILOTs, however, are not used by most local governments as a means of collecting revenue.

Another “best practice” is for state governments to reimburse local governments for the loss of revenue due to property tax exemptions. This option, however, has not been discussed in recent years because of fiscal pressure on the states.

Non profits also have entered into SILOT agreements with local governments. These agreements have included provisions by which non profits pay for specific services such as a fire and police protection. Local governments have also imposed user fees and charges on non profits. But there are legal and economic limits as to the extent charges
and fees can be applied. More controversially, local governments have sought to impose direct taxes on non profits. These proposals are almost always unsuccessful and are used more as a means of convincing non profits to enter into PILOT agreements.

The laws concerning non profit engagement in commercial activities vary widely from state to state. Generally, some states allow non profits to engage in commercial activity, some will completely revoke an exemption, while most provide for partial exemptions. Nationwide, there is little legal authority for local governments to prevent taxable property acquired by a non profit from becoming exempt from property tax. At least one state, Virginia, gives local governments the authority to approve exemption for property acquired by non profits. This authority is strongly suggested by public finance experts and supported by local government officials.

Local governments across the country have a plethora of property tax relief mechanisms to reduce property taxes on favored groups, e.g., current use assessment for farmland, assessment limits on residential properties, and tax exemptions for non profits or selected disadvantaged individuals, e.g., blind, disabled. In an era of fiscal stress confronting state and local governments nationally, it is good public policy to explicitly consider and discuss on a regular basis the benefits and costs of each relief mechanism to see if the intended benefits of such preferential treatment can be achieved at a lower overall cost to the government and other property tax payers.
References


Lemov, Penelope. 2010. Taxing Away Exemptions, GOVERNING THE STATES AND LOCALITIES (May 1).


McConner, R.J. and a.L. Wellever. 1989. The Economic Impact of Montana Hospitals. Department of Agricultural Economics Staff Paper 89-2, Montana State University, Bozeman, MT.


Moore, C.L. 1974. “The Impact of Public Institutions on Regional Income; Upstate Medical Center as a Case in Point.” Economic Geography. 50(2), 124-129.


Appendix A  
Legal Authorities for Property Tax Exemptions

Charitable Property Tax Exemption, 2012

<table>
<thead>
<tr>
<th>State</th>
<th>Constitution Mandates Exception</th>
<th>Constitution Grants Authority to Legislature</th>
<th>Constitution Silent</th>
<th>Constitution &amp; Statute(s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>x</td>
<td></td>
<td></td>
<td>Ala. Const. art. IV, § 91</td>
</tr>
<tr>
<td>Alaska</td>
<td>x</td>
<td></td>
<td></td>
<td>Alaska Const. art. IX, § 4</td>
</tr>
<tr>
<td>Arizona</td>
<td></td>
<td>x</td>
<td></td>
<td>Ariz. Const. art. IX, § 2(2)</td>
</tr>
<tr>
<td>Arkansas</td>
<td>x</td>
<td></td>
<td></td>
<td>Ark. Const. art. 16, § 5(b)</td>
</tr>
<tr>
<td>California</td>
<td></td>
<td>x</td>
<td></td>
<td>Cal. Const. art. XIII, § 4</td>
</tr>
<tr>
<td>Colorado</td>
<td>x</td>
<td></td>
<td></td>
<td>Colo. Const. art. X, § 5</td>
</tr>
<tr>
<td>Delaware</td>
<td></td>
<td>x</td>
<td></td>
<td>Del. Const. art. VIII, § 1</td>
</tr>
<tr>
<td>Florida</td>
<td></td>
<td>x</td>
<td></td>
<td>Fla. Const. art. VII, § 3(a)</td>
</tr>
<tr>
<td>Georgia</td>
<td></td>
<td>x</td>
<td></td>
<td>Ga. Const. art. VII, § 2, para. IV</td>
</tr>
<tr>
<td>Idaho</td>
<td></td>
<td>x</td>
<td></td>
<td>Idaho Const. art. VII, § 5</td>
</tr>
<tr>
<td>Illinois</td>
<td></td>
<td>x</td>
<td></td>
<td>Ill. Const. art. IX, § 6</td>
</tr>
<tr>
<td>Indiana</td>
<td></td>
<td>x</td>
<td></td>
<td>Ind. Const. art. 10, § 1</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Ind. Code § 6-1.1-10-16(a) (2009)</td>
</tr>
<tr>
<td>Iowa</td>
<td></td>
<td>x</td>
<td></td>
<td>Iowa Code § 427.1 (2009)</td>
</tr>
<tr>
<td>Kansas</td>
<td></td>
<td>x</td>
<td></td>
<td>Kan. Const. art. 11, § 1</td>
</tr>
<tr>
<td>Kentucky</td>
<td></td>
<td>x</td>
<td></td>
<td>Ky. Const. § 170</td>
</tr>
<tr>
<td>Louisiana</td>
<td></td>
<td>x</td>
<td></td>
<td>La. Const. art. VII, § 21</td>
</tr>
<tr>
<td>State</td>
<td>Property Tax Exemption</td>
<td>Statute</td>
<td></td>
<td></td>
</tr>
<tr>
<td>------------</td>
<td>------------------------</td>
<td>-------------------------------------------------------------------------</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maine</td>
<td>x</td>
<td>Me. Const. art. IV, pt. 3, § 23</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maryland</td>
<td>x</td>
<td>Md. Code Ann., Tax-Prop. § 7-202(b) (LexisNexis 2007)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minnesota</td>
<td>x</td>
<td>Minn. Const. art. X, § 1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mississippi</td>
<td>x</td>
<td>Miss. Const. art. 4, § 112 Miss. Code Ann. § 27-31-1 (1972)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

13 The Maryland statute (sec. 7-202) governing property tax exemptions reads:

(b) (1) Except as provided in subsection (c) of this section, property is not subject to property tax if the property:

(i) is necessary for and actually used exclusively for a charitable or educational purpose to promote the general welfare of the people of the State, including an activity or an athletic program of an educational institution; and

(ii) is owned by:

1. a nonprofit hospital;

2. a nonprofit charitable, fraternal, educational, or literary organization including:
   A. a public library that is authorized under Title 23 of the Education Article; and
   B. a men’s or women’s club that is a nonpolitical and nonstock club;

3. a corporation, limited liability company, or trustee that holds the property for the sole benefit of an organization that qualifies for an exemption under this section; or

4. a nonprofit housing corporation.
<table>
<thead>
<tr>
<th>State</th>
<th>x</th>
<th>Text</th>
</tr>
</thead>
</table>
| New Mexico |   | N.M. Const. art. VIII, § 3  
| New York   | x | N.Y. Const. art. XVI, § 1  
|            |   | N.Y. Real Prop. Tax Law § 420 (McKinney 2008)                        |
| North Carolina | x | N.C. Const. art. V, § 2(3)  
|            |   | N.C. Gen. Stat. § 105-278.7 (2009)                                   |
| North Dakota | x | N.D. Const. art. X, § 5  
|            |   | N.D. Cent. Code § 57-02-08 (2009)                                    |
| Ohio       | x | Ohio Const. art. XII, § 2  
| Oklahoma   | x | Okla. Const. art. X, § 6(a)  
| Pennsylvania | x | Pa. Const. art. 8, § 2(a)  
| Rhode Island | x | R.I. Gen. Laws § 44-3-3(8) (2005)                                    |
| South Carolina | x | S.C. Const. art. X, § 3  
| South Dakota | x | S.D. Const. art. XI, § 6  
| Tennessee  | x | Tenn. Const. art. II, § 28  
| Texas      | x | Tex. Const. art. VIII, § 2(a)  
| Utah       | x | Utah Const. art. XIII, § 3(1)(f)                                     |
| Virginia   | x | Va. Const. art. X, § 6(a)  
| Washington | x | Wash. Const. art. VII, § 1  
| West Virginia | x | W. Va. Const. art. X, § 1  
| Wisconsin  | x | Wis. Stat. § 70.11(4) (2010)                                         |
| Wyoming    | x | Wyo. Const. art. 15, § 12  
Appendix B Alternatives to PILOTs Survey

Survey Design

A survey was created and administered to further investigate the incidence and prevalence of alternatives to payments in lieu of taxes. On February 6th and 7th 2012, 10 cities and counties with the authority to assess property taxes were sent an email survey to either a publicly listed email address or through an online email submission section on the government’s website. The 10 cities/counties were King County, Washington (Seattle); Shelby County, Tennessee (Memphis); Travis County, Texas (Austin); Boston, Massachusetts; Oklahoma County, Oklahoma (Oklahoma City); Louisville-Jefferson County, Kentucky (Louisville); Davidson County, Tennessee (Nashville); Fairfax County, Virgina; Multnomah County, Oregon (Portland); and Denver, Colorado. These counties/cities were selected for to survey based on the presence of medium-large size urban areas within the taxing jurisdiction (500,000 – 700,000 residents) and/or a metropolitan area population of over 1 million residents. As of February 17th 8 of the 10 local governments (the exceptions being Travis County and the city of Denver) responded to the survey.

Each survey contained the following three questions:

1. Do local property tax exempt organizations have payments in lieu of taxes (PILOT) voluntary arrangements?
2. Beyond PILOTs, do local exempt organizations voluntarily provide any public services in lieu of property taxes?
3. Are there any user fees or other taxes that exempt organizations must pay within your jurisdiction?

All of the respondents answered these questions point-by-point. Some respondents elaborated further by attaching relevant legal statutes to their emails. A follow-up phone conversation occurred on February 10th with the lead assessor of Oklahoma County.

Survey Results

<table>
<thead>
<tr>
<th>Response</th>
<th># of Governments</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>No PILOTs, No Alternatives, No Other Tax</td>
<td>1 (King County, Washington)</td>
<td>The respondent for King County responded that exempt organizations do not engage in PILOTs, SILOTs or have to pay any county taxes.</td>
</tr>
<tr>
<td>PILOTs, No Alternatives, No Other Tax</td>
<td>2 (Shelby County &amp; Davidson County, Tennessee)</td>
<td>Both of the surveyed Tennessee counties responded that exempt organizations within their jurisdictions have payment in lieu of taxes relationships with both the county and the</td>
</tr>
</tbody>
</table>
municipal government in certain situations. The Davidson County respondent cited Tennessee law which allows for local governments to enter into PILOT arrangements with exempt entities that provide low-income housing for the elderly as long as the PILOT amount does not exceed 25% of their potential non-exempt tax liability. The respondent for Shelby County stated that a special separate government body, entitled the Memphis-Shelby County Industrial Development Board administers PILOTs in that jurisdiction. Both respondents stated that exempt entities are not subject to any other county taxes or PILOT alternative arrangements.

| No PILOTs, No Alternatives, No Other Tax | 3 (Multnomah County, Oregon)\(^{14}\), (Oklahoma County, Oklahoma), (Louisville-Jefferson County, Kentucky) | While the respondents from these three counties stated that exempt entities do not engage in PILOT relationships nor pay any additional taxes, they all similarly stated that state laws and/or state constitutions required a demonstration of “public service” from an organization in order to receive tax exemption. In Multnomah County, the stated purpose of a nonprofit or charity must be to provide a service. |

---

\(^{14}\) The respondent for Multnomah County stated that exempt entities that file for their exemption past a due date have to pay a late fee and categorized this as a fee/tax. However, this is more the category of a penalty rather than a user fee or a municipal tax.
benefiting the public rather than members in order to become exempt. Kentucky law directs assessors in Louisville-Jefferson County to take into account whether an organization that is filling for exemption relieves some governmental burden in their decision to grant or withhold exemption. The Oklahoma constitution requires exempt charities to provide a service that primarily benefits the people of Oklahoma and requires taxes to be paid on properties that used for commercial purposes.

<table>
<thead>
<tr>
<th>PILOTs, Alternatives, and Other Taxes</th>
<th>1 (Boston, Massachusetts)</th>
<th>The City of Boston has conducted PILOT programs since the 1970s. For the 2012 fiscal year Boston is reforming the PILOT structure by eliminating individual contracts and instead basing PILOT payments based on a percentage of their property value. Exempt entities can deduct up to 50% of their PILOT burdens by providing social benefits that uniquely impact the Boston residents (like providing scholarships for Boston residents). Exempt entities must pay inspection and permit fees but can file for a waiver for vehicle inspection fees if vehicles are central to the organization’s mission.</th>
</tr>
</thead>
<tbody>
<tr>
<td>No PILOTs, No Alternatives, Other Taxes</td>
<td>1 (Fairfax County, Virginia)</td>
<td>The respondent for Fairfax County stated that while</td>
</tr>
</tbody>
</table>
exempt entities do not engage in PILOT or alternative arrangements with the county, the entities are responsible for paying garbage collection fees and other municipal fees.
Appendix C
Legal Treatment of Commercial Activity on Exempt Property

I. States with Statutory Authority Permitting Partial Exemption

California

CAL.REV. & TAX.CODE § 214.05 provides that when business income derived from exempt property can be reasonably attributed to a portion of such property, that portion of the property shall be taxed in a manner reflecting the value of that portion as bears to the total value of the property.

Connecticut

CONN.GEN.STAT.ANN. § 12-81 provides for property tax exemptions for various types of property. § 12-88 provides further: “[i]f a portion only of any lot or building belonging to, or held in trust for, any such organization is used exclusively for carrying out one or more of such purposes, such lot or building shall be so exempt only to the extent of the portion so used and the remaining portion shall be subject to taxation.” The organizations to which this partial exemption provision applies includes, but is not limited to: property use for scientific, educational, literary, historical, or charitable purposes; property belonging to agricultural or horticultural societies; property held for cemetery use; and property of religious organizations.

Florida

FLA.STAT.ANN. § 196.192(2): “All property owned by an exempt entity, including educational institutions, and used predominantly for exempt purposes shall be exempted from ad valorem taxation to the extent of the ratio that such predominant use bears to the nonexempt use.” Predominant use is defined use of property for exempt purposes in excess of 50%. See § 196.012(3).

Hawaii

HAW.REV.STAT. § 246-32 provides for general property tax exemptions for certain property. § 246-32(d) provides: “If any portion of the property which might otherwise be exempted under this section is used for commercial or other purposes not within the conditions necessary for exemption (including any use the primary purpose of which is to produce income even though such income is to be used for or in furtherance of the exempt purposes) that portion of the premises shall not be exempt but the remaining portion of the premises shall not be deprived of the exemption if the remaining portion is used exclusively for purposes within the conditions necessary for exemption. In the event of an exemption of a portion of a building, the tax shall be assessed upon so much of the value of the building (including the land there under and the appurtenant
premises) as the proportion of the floor space of the nonexempt portion bears to the total floor space of the building.”

Idaho

IDAHO CODE ANN. § 63-602B(1) exempts property belonging to religious entities. § 63-602B(2) provides: “If any such property is leased in part or used in part by such religious limited liability company, corporation or society for such business or commercial purposes, the assessor shall determine the value of the entire exempt property, and the value of the part used or leased for such business or commercial purposes, and that part used or leased for such business or commercial purposes shall be taxed as any other property.”

Indiana

IND.CODE ANN. § 6-1.1-10-16(a): “All or part of a building is exempt from property taxation if it is owned, occupied, and used by a person for educational, literary, scientific, religious, or charitable purposes.”

Iowa

IOWA CODE ANN. § 427.1(14)(a): “The assessor, in arriving at the valuation of any property of the society or organization, shall take into consideration any uses of the property not for the appropriate objects of the organization and shall assess in the same manner as other property, all or any portion of the property involved which is leased or rented and is used regularly for commercial purposes for a profit to a party or individual. If a portion of the property is used regularly for commercial purposes, an exemption shall not be allowed upon property so used and the exemption granted shall be in the proportion of the value of the property used solely for the appropriate objects of the organization, to the entire value of the property.”

Massachusetts

MASS.GEN. LAWS ANN. Ch. 59 § 5(11) provides for tax exemption for property of religious entities. The statute also provides that the tax exemption shall not be extended to any portion of property otherwise exempt that is not used for religious purposes.

Nevada

NEV. REV. STAT. ANN. § 361.157(1) provides: “When any real estate or portion of real estate which for any reason is exempt from taxation is leased, loaned or otherwise made available to and used by a natural person, association, partnership or corporation in connection with a business conducted for profit or as a residence, or both, the leasehold interest, possessory interest, beneficial interest or beneficial use of the lessee or user of the property is subject to taxation to the extent the: (a) Portion of the property leased or
used; and (b) Percentage of time during the fiscal year that the property is leased by the lessee or used by the user . . . .”

New Jersey

N.J.S.TAT.ANN. § 54:4-3.6 exempts, among other property, “all buildings actually used in the work of associations and corporations organized exclusively for religious purposes, including religious worship, or charitable purposes, provided that if any portion of a building used for that purpose is leased to a profit-making organization or is otherwise used for purposes which are not themselves exempt from taxation, that portion shall be subject to taxation and the remaining portion shall be exempt from taxation . . . .”

New York

N.Y. REAL. PROP. TAX LAW § 420-a provides the general tax exemption for certain classes of property. § 420-a(2) provides in part: “If any portion of such real property is not so used exclusively to carry out thereupon one or more of such purposes but is leased or otherwise used for other purposes, such portion shall be subject to taxation and the remaining portion only shall be exempt . . . .”

North Carolina

N.C. GEN. STAT. ANN. § 105-278.3(e): “Notwithstanding the exclusive-use requirement of subsection (a), above, if part of a property that otherwise meets that subsection's requirements is used for a purpose that would require exemption if the entire property were so used, the valuation of the part so used shall be exempted from taxation.”

Ohio

OHIO REV. CODE ANN. § 5713.04 provides: “If a separate parcel of improved or unimproved real property has a single ownership and is so used so that part thereof, if a separate entity, would be exempt from taxation, and the balance thereof would not be exempt from taxation, the listing thereof shall be split, and the part thereof used exclusively for an exempt purpose shall be regarded as a separate entity and be listed as exempt, and the balance thereof used for a purpose not exempt shall, with the approaches thereto, be listed at its taxable value and taxed accordingly.”

Oregon

OR. REV. STAT. ANN. § 307.140(1): “All houses of public worship and other additional buildings and property used solely for administration, education, literary, benevolent, charitable, entertainment and recreational purposes by religious organizations, the lots on which they are situated, and the pews, slips and furniture therein. However, any part of any house of public worship or other additional buildings or property which is kept or used as a store or shop or for any purpose other than those stated in this section shall be assessed and taxed the same as other taxable property.”
South Dakota

S.D. CODIFIED LAWS § 10-4-9 exempts property owned by religious societies. § 10-4-12 provides: “If property owned by any health care organization or charitable, benevolent, or religious society . . . is used partly by such health care organization or charitable, benevolent, or religious society for health care, charitable, benevolent, or religious purposes, and the remaining part is occupied, rented, or used for other than health care, charitable, benevolent, or religious purposes, the portion of property that is so occupied, rented, or used for other purposes, shall be taxed as other property of the same class is taxed. For the purpose of determining the value of the taxable portion of the property, the appraised value of the entire property shall be multiplied by the percentage of the entire property used for other than health care, charitable, benevolent, or religious purposes. The resulting value shall be multiplied by the percentage of time the property is used for other than health care, charitable, benevolent, or religious purposes. The resulting value shall be the assessed value for taxation purposes.”

Tennessee

TENN. CODE ANN. § 67-5-212(a)(1) provides the general property tax exemption for certain classes of property. § 67-5-212(a)(3)(B) provides: “The real property of any such institution not so used exclusively for carrying out thereupon one (1) or more of such purposes, but leased or otherwise used for other purposes, whether the income received there from be used for one (1) or more of such purposes or not, shall not be exempt; but, if a portion only of any lot or building of any such institution is used purely and exclusively for carrying out thereupon one (1) or more of such purposes of such institution, then such lot or building shall be so exempt only to the extent of the value of the portion so used, and the remaining or other portion shall be subject to taxation.”

Virginia

VA. CODE ANN. § 58.1-3603(A) provides: “When a part but not all of any such building or land, however, is a source of revenue or profit, and the remainder of such building or land is used by any organization exempted from taxation pursuant to this chapter for its purposes, only such portion as is a source of profit or revenue shall be liable for taxation.”

Washington

WASH. REV. CODE ANN. § 84.36.020 provides for tax exemption for churches and religious property. However, the Regulations for the Department of Revenue suggest that: “When property is not used for church purposes, the exemption is lost. If a portion of the exempt property is used for commercial rather than church purposes, that portion must be segregated and taxed whether or not the proceeds received by the church from the commercial use are applied to church purposes.” WASH. ADMIN. CODE § 458-16-190 (6).
West Virginia

W. Va. Code R. § 110-3-12.5.2 provides: “Where a portion of the property is used for divine worship and the remainder is not being used primarily and immediately for purposes which may be classified as exempt purposes . . . the property is fully and completely taxable like any other taxable property. Example: A church has its sanctuary on the first floor of the structure and a basement immediately below the sanctuary. As a result of the location and construction of the structure, a portion of the basement is used as a neighborhood coffee shop where food is sold. Due to the fact that the sale of food on a continuing basis and in an on-going business environment is not an exempt purpose, the entire structure is subject to property taxation.”

Wisconsin

Wis. Stat. Ann. § 70.11 provides for exemption from property tax for certain classes of property. § 70.1105 provides: “Property that is exempt under s. 70.11 and that is used in part in a trade or business . . . , shall be assessed for taxation at that portion of the fair market value of the property that is attributable to the part of the property that is used in the unrelated trade or business.”

II. States Where Case Law Provides Authority For Partial Exemptions

Alaska

“The assessor found that the administrative services supporting exempt and nonexempt programs were not used exclusively for charitable purposes. The superior court relied on that finding in classifying the fund-raising as nonexempt when the court spatially apportioned the sixth floor to determine the part entitled to exemption. It did not commit legal error in doing so. TCC has not demonstrated on appeal that the facts compel application of either of the recognized exceptions to the ‘exclusive use’ rule. We consequently discern no error in the superior court's spatial apportionment on the basis of the fund-raising activity.” Fairbanks North Start Borough v. Dena Nena Henash, 88 P.3d 124, 141 (Alaska 2004); see also City of Nome v. Catholic Bishop of Northern Alaska, 707 P.2d 870 (Alaska 1985) (holding in part that spatial apportionment of applicable property is mandated under the exemption statute).

Arizona

In Volunteer Center of Southern Arizona v. Staples, 147 P.3d 1052 (Ariz. Ct. App. 2006), the court addressed the implications of non-profit organization leasing part of its property to a separate non-profit organization. As the case discusses, the leased part of the property was assessed for tax purposes while the remainder would be exempt. The court ultimately held, however, that the lease did not affect the exempt status of the
building in its entirety. While not directly addressed, the court seemed to recognize the possibility of a partial exemption.

Colorado

*See Hanagan v. Rocky Ford Knights of Pythias Building Association*, 75 P.2d 780 (Colo. 1938) (holding that the ratio of the proportionate part of a building used for exempt purposes as related to the whole building must be determined to properly apply a partial exemption).

Delaware

While no cases were found directly on point, the court in *New Castle County Department of Land Use v. University of Delaware*, 842 A.2d 1201 (Del. 2004), affirmed a lower court’s unreported opinion regarding exemption of property leased by a university to a bank. In that unreported opinion, the court addressed a tax assessor’s determination that a particular building belonging to the university should only be partially exempt. However, that court ultimately found that the once determined nonexempt use was in fact an exempt use, which qualified the entire building for the tax exemption. The court, therefore, did not discuss the viability of a partial exemption directly.

District of Columbia

“The complaint alleges that from 1921 to 1926 there was a synagogue as well as a ‘Mickva’ on this property. Certainly a church which provided in the basement a place where small children could be entertained would not thereby lose its character as a church. Nor would a synagogue lose its character as a church if a ‘Mickva’ were attached. However, we cannot tell from the petition whether the structure or structures then existing were of such a character that all or a part of the property should have been exempted during those years.” *Combined Congregations of District of Columbia v. Dent*, 140 F.2d 9, 10 (D.C. Cir. 1943). Although not entirely on point, the court seemed to recognize the potential for a partial property tax exemption when a portion of the property is used for nonexempt purposes and the remainder for exempt purposes.

Georgia

“Since the appellant is a purely public charity and meets the requirements of Code Ann. s 92-201, that portion of the property which is being used as a home for the aged is tax exempt. However, that part of the building consisting of two retail stores which are leased would not be tax exempt. The area where the stores are located is being used to gain rental and not for the primary purpose of operating the inn.” *Peachtree on Peachtree Inn, Inc. v. Camp*, 170 S.E.2d 709, 715 (Ga. Ct. App. 1969).

Illinois
“[E]ven where nonexempt use is more than merely incidental, the property may nonetheless qualify for a partial exemption where an “identifiable portion” of the property is used for exempt purposes.” Streeterville Corp. v. Department of Revenue of State of Ill., 714 N.E.2d 497, 498-99 (Ill. 1999) (citing Illinois Institute of Technology v. Skinner, 273 N.E.2d 371 (Ill. 1971))

Kentucky

See City of Louisville v. Louisville Board of Trade, 14 S.W. 408 (Ky. Ct. App. 1890) (recognizing a partial exemption for a building used in part for exempt purposes).

Louisiana

“The constitutional exemption is limited to the portion of the property of an organization which is actually devoted to charitable undertakings, and does not include all the property of a charitably-purposed organization . . . .” Ruston Hospital, Inc. v. Riser, 191 So.2d 665, 666-67 (La. Ct. App. 1966); see also Beta Xi Chapter of Beta Theta Pi v. City of New Orleans, 137 So. 204 (La. Ct. App. 1931) (mentioning the same).

Maryland

“In our opinion, the statute only contemplates, in the exemption granted, such building or parts thereof as may be reasonably necessary for the corporate purposes of the institution or association; and any building or part of a building devoted to other purposes and let to rent should be taxed as other property in the State.” City of Baltimore v. Grand Lodge A.F. & A.M., 60 Md. 280 (Md. 1883).

Michigan

“Similarly, in the case of Gull Lake Bible Conference Association v. Township of Ross (1958), 351 Mich. 269, 88 N.W.2d 264, the Court allowed exemption for certain portions of plaintiff's realty, including employees' lodging, parking facilities, and services, as they were closely connected with the religious purpose to gather people together upon the land for conferences, and we note that such established facilities were frequently used to promote such stated purposes.” Lake Louise Christian Community v. Township of Hudson, 159 N.W.2d 849, 854 (Mich. Ct. App. 1968); see also McFarlan Home v. City of Flint, 307 N.W.2d 712 (Mich. Ct. App. 1981) (recognizing that property may be apportioned for the purpose of exempting property used for charitable uses).

Minnesota

“The better rule, which we now adopt and which is followed by many other jurisdictions wherein property is entitled to tax exemption only if it is used exclusively for a tax-exempt purpose, is that when a building is owned by a charitable or other tax-exempt institution and one substantial part thereof is directly, actually, and exclusively occupied by such institution for the purposes for which it was organized and another
substantial portion thereof is primarily used for revenue by rental to the general public, such building with the grounds thereof is pro rata exempt from taxation and pro rata taxable according to its separate uses, and it should be assessed and taxed on that portion of its proper assessable value allocated to the taxable use, after deducting from its overall assessable value the portion thereof properly allocated to the proportionate tax-exempt use.” Christian Business Men’s Committee of Minneapolis, 38 N.W.2d at 811.

Missouri

“We hold that Mo.Const. art. X, s 6 and s 137.100, RSMo 1978, which exempt from taxation property “used exclusively for purposes purely charitable,” authorize a partial exemption of a building or tract, where that building, or tract, is used in part for charitable purposes and in part for non-charitable purposes.” Barnes Hospital v. Leggett, 589 S.W.2d 241, 244 (Mo. 1979).

Montana

“‘By the great weight of authority, a statute which in effect exempts from taxation property or buildings used for certain purposes authorizes a partial exemption of a building in case the building is used in part for exempt purposes and in part for nonexempt purposes.’” Northwestern Imp. Co. v. Rosebud County, 288 P.2d 657, 660 (Mont. 1955) (quoting 159 A.L.R. 685).

Nebraska

“That part of a building owned by a religious, charitable and educational institution, but leased and used by the tenant for business purposes, is not exempt from taxation.” In re Masonic Temple Craft, 261 N.W. 569, 570 (Neb. 1935) (citing YMCA v. Lancaster County, 182 N.W. 593 (Neb. 1921) (finding no reason why an assessor cannot arrive at a just valuation for a portion of a building used for nonexempt purposes)).

New Hampshire

“The taxpayer next argues that the statute does not allow apportionment between exempt and non-exempt uses in religious exemption cases. This assertion is unsupported by our case law. In Franciscan Fathers, we recognized that certain property may be exempt, while other property, not used for religious activity, would not be exempt from taxation. Additionally, in considering other statutory exemptions, we have consistently utilized apportionment when appropriate. We find nothing in the language of the religious exemption statute to suggest that the legislature intended to treat religious exemptions differently than other tax exemption statutes.” Appeal of Emissaries of Divine Light, 669 A.2d 802, 805 (N.H. 1995).

New Mexico

“[W]e hold that where one substantial part of a building that is owned by a charitable institution is directly and actually occupied and used for charitable purposes,
and another substantial portion is primarily used for commercial leasing, such building is pro rata taxable according to its separate uses.” *Sisters of Charity of Cincinnati, Ohio v. Bernalillo County*, 596 P.2d 255, 259 (N.M. 1979).

**Oklahoma**

“We, therefore, have reached the conclusion that such unit of real estate is taxable on an assessed valuation reflecting a reduction to the extent of the value of that portion of the property which is used for tax exempt purposes.” *Chapman v. Draughons School of Business*, 287 P.2d 903, 905 (Okla. 1955).

**Pennsylvania**

“‘The parts rented and producing income are liable to taxation. There is in fact no express warrant in the act for dividing the building for purposes of taxation and exempting any part of it when other parts produce income; but such division was sustained in Association v. Donohugh, 7 W. N. C. 208, upon grounds of equity and the broad intent of the statute, and has been received with general acquiescence.’” *Board of Home Missions and Church Extension of Methodist Episcopal Church v. City of Philadelphia*, 109 A. 664, 666 (Pa. 1920) (quoting *Philadelphia v. Barber*, 160 Pa. 123, 128 (Pa. 1894)).

**Rhode Island**

“The words ‘so far as the same is used exclusively,’ etc., are words of extent, and not of exclusion. The whole estate is not excluded from exemption if any part of it is used for other purposes, but it is exempt to the extent of the exclusive religious or educational use.” *In re City of Pawtucket*, 52 A. 679 (R.I. 1902) (referring to the statutory exemption).

**South Carolina**

Court found that the statutory exemption extended only to portions of the property “actually occupied” by the organization. *Westview Baptist Church v. Rembert*, 331 S.E.2d 382 (S.C. Ct. App. 1985). While this case did not involve multiple uses of a single building, it does seem to imply that partial tax exemptions would be available in certain situations.

**Texas**

“We see no reason why that separate portion of the building that is used ‘primarily as a place of regular religious worship’ cannot be exempt. Here, the jury in Special Issue 4 found that 35% of the building at 301–303 S. Pioneer Drive was used during 1980 by the church primarily as a place of regular religious worship. We hold there is some evidence to support that finding.” *Highland Church of Christ v. Powell*, 644 S.W.2d 177, 181 (Tex. App. 1983).
Utah

See Odd Fellows’ Building Association v. Naylor, 177 P. 214 (Utah 1918) (finding no reason to unreasonably apply a strict construction of the exemption and holding that a building may properly be segregated for tax purposes).

Vermont

“While the precise question has not, to our knowledge, been heretofore presented to this Court, it has been held that where property of a tax exempt institution is devoted partly to public uses, a building may be divided, for the purpose of taxing that part of it engaged in business use and exempt that part devoted to public use.” Medical Center Hospital of Vermont v. City of Burlington, 303 A.2d 468, 470-71 (Vt. 1973).

Wyoming

“We are of the opinion that under the agreed facts the exemption would not apply to any other part of the main building or to the building on lot 14, and that the trial court did not err in denying the injunction.” Independent order of Odd Fellows of Casper, Wyoming v. Scott, 163 P. 306, 307 (Wyo. 1917).

III. States Where Case Law Requires Denial of Entire Exemption

Alabama

“Further, the property must be exclusively used for religious worship, schooling, or charity, in the sense that the property must be used solely, only, or wholly for a religious, educational, or charitable purpose. Bridges, 246 Ala. at 498-90, 21 So.2d at 319-20. No partial § 91 exemption is available. Id.” Most Worshipful Grand Lodge of Free & Accepted Masons, 603 So.2d at 1000.

Kansas

“We therefore hold that in the absence of a statute to the contrary, where a single building is under single ownership so that it is listed for taxation as an entity, the nonexempt use of any portion of the building renders the entire building taxable. Here, the first floor of the building was concededly used for a nonexempt purpose. It follows that the board of tax appeals and the district court correctly denied exempt status for the entire building, regardless of the use made of the remainder.” Defenders of Christian Faith v. Board of County Commissioners of Sedgwick, 547 P.2d 706, 712 (Kan. 1976).

Maine
See City of Lewiston v. Marcotte Congregate Housing, Inc., 673 A.2d 209 (Me. 1996) (holding that when a property is not used “solely” for exempt purposes the entire property must be taxed).

Mississippi

Where part of a Masonic Lodge was rented out to commercial tenants, the entire building was held to be taxable. Senter v. City of Tupelo, 136 Miss. 269 (Miss. 1924). However, that court found that since a large portion of the rents received were used by the lodge in making payments on the purchase price of the property, such use could not be considered anything but business purposes.

IV. States With Statutory Authority Preserving Entire Exemption

Arkansas

At least as far as church property is concerned; when such property is used for commercial purposes it is fully taxable. However, according to ARK. CODE ANN. § 26-3-206: “in the event any property is used partially for church purposes and partially for investments or other commercial or business purposes, the property shall be exempt from the ad valorem tax.” Beyond application to church property, no other authority was found on the issue.

V. States Where No Clear Authority Exists

North Dakota

N.D.CENT.CODE. § 57-02-08 provides the general exemption for certain types of property. However, neither the statute itself nor any case law found addresses the viability of a partial exemption. Because the statute appears to take a negative approach to the derivation of profit from rentals, it is probably safest to assume a loss of the entire exemption in the event of such rental.