



State Tax Exemption Standards

with Quantitative Thresholds

for Nonprofit Health
Care Organizations

AN ALLIANCE BRIEF

At last count, there are sixteen states mandating community benefit reporting by nonprofit hospitals and/or other nonprofit health care organizations. In sixteen other states, community benefits are reported on a voluntary basis by nonprofit hospitals through their state hospital associations.¹

In addition, there are three states with specific standards, including quantitative thresholds, for tax exemption: Utah (1990), Texas (1993), and Pennsylvania (1997)

- The **Utah** law applies only to property tax exemption, for only nonprofit hospitals and nursing homes (no other types of nonprofit health care organizations can be exempted from property taxes).
- The **Texas** law applies to all tax exemptions in the state, for only nonprofit hospitals.
- The **Pennsylvania** law applies to local property and state sales tax exemptions, for a wide range of charitable organizations (“institutions of purely public charity”).

This brief is intended to inform the nonprofit health sector about the requirements in these three states. The reasons are threefold:



1. Officials in other states, confronted with large numbers of uninsured residents and insufficient resources to fully address the problem, are scrutinizing more closely whether nonprofit hospitals and other health care organizations are doing as much as they can to help out. As part of this scrutiny, such officials can be expected to analyze what other states have done or are contemplating to ensure that these organizations merit their state tax exemptions.
2. Senator Charles Grassley (R-IA), ranking member of the Senate Finance Committee, has asked the Government Accountability Office to investigate, among other issues, individual state tax-exemption requirements for nonprofit hospitals, as he continues to press for reform of the federal tax-exemption standards for these institutions.
3. Cash-strapped local units of government may increasingly challenge the property tax exemption of nonprofit health care institutions. Where such institutions are confronted with annual compliance determinations by multiple jurisdictions, based on varying and subjective standards, they may want to preempt such regulation by developing and advocating a single set of more objective state standards. In such instances, they are likely to want to analyze what other states have done in this regard.
2. None of its net earnings and no donations made to it inure to the benefit of private shareholders or other individuals, with compliance under Section 501(c)(3) creating a rebuttable presumption along with signed statements or other evidence related to the uses of revenues and donations and payments to officers, employees, suppliers, and contractors.
3. It has open-access policies to treat members of the public without regard to race, religion, gender, or ability to pay as well as to provide free or discounted care to the indigent in accord with their ability to pay and to provide evidence of its efforts to affirmatively inform the public of its open access policy and the availability of services for the indigent.
4. Its policies integrate and reflect the public interest, with a rebuttable presumption of compliance with this standard consisting of *all* of the following:
 - a. The provision of evidence that its governing board has a broad-based membership from the community as required by federal law (“community” may be defined by the institution to be narrower or broader than a specific county’s geographic boundaries).
 - b. It confers at least annually with the county board of equalization or its designee concerning the community’s clinical needs that might appropriately be addressed by the institution.
 - c. It has a charity plan to ensure compliance with the above open access and public interest standards.

Following is a summary of the qualitative and quantitative standards that must be met in these three states for tax exemption.

Utah

In Utah, nonprofit hospitals and nursing homes must meet *all* of the following standards for property tax exemption:

1. The hospital or nursing home is organized on a nonprofit basis to promote health care or provide health-related assistance to the general public. Upon dissolution of the organization, the assets are required to be distributed only for exempt purposes or to the government for public purposes.
5. Its total “gift” to the community (defined as a substantial imbalance in the exchange between the institution and the recipient of its services or the lessening of a government burden through its operations) exceeds on an annual basis its property tax liability for that year. The following quantifiable activities and services are to be counted toward the institution’s total gift, but are not intended to be an exhaustive list:

- Financial assistance to patients unable to pay for the cost of care they receive.
- Unreimbursed costs of volunteer and community service, including education and research, rendered **for or by** the institution.
- Losses under Medicare, Medicaid, and other government programs.
- Donations of time by individuals **to** the institution.
- Donation of money **to** the institution.
- Community value, whether or not precisely quantifiable, of the operation of tertiary care units or other critical services that may not be otherwise offered to the community, and/or the continued operation of hospitals where costs exceed revenues, such as a primary care hospital in a rural area.

Descriptions of intangible or unquantifiable gifts are to be included.

6. For satellite health care facilities and centralized support facilities to be included in the property tax exemption of the institution, it must demonstrate that such facilities help it to better meet its mission. Individual physician offices which are off-site and owned by the institution are deemed not to relate directly to the institution's mission and are not exempt from property taxes.

Texas

Nonprofit hospitals must meet **at least one** of the following three charity care and community benefit criteria. However, these criteria are to be considered guidelines along with other factors that may be unique to the hospital and are therefore not determinative factors:

1. Charity care and losses from government-sponsored indigent health care (excludes Medicare) must be at a level that is reasonable (guided by the prudent business judgment of the hospital) in relation to the community needs, as determined through a community needs assessment, the available resources of the hospital or hospital system, the tax-exempt benefits received, and other factors unique to the hospital such as its volume of Medicare and Medicaid patients.

2. Charity care and losses from government-sponsored indigent care must be equal to at least 100 percent of the hospital's or system's tax-exempt benefits, excluding federal income tax.
3. Charity care and community benefits (including charity care, losses from government-sponsored indigent care programs, donations, as well as subsidized education, research, and patient care services, but excluding any taxes or government assessments) must be provided in a combined amount equal to at least 5 percent of the hospital's or system's net patient revenues, provided that charity care and government-sponsored indigent health care are provided in an amount equal to at least 4 percent of net patient revenue.

The following are considered to be in compliance with any of the above criteria:

- Disproportionate share-designated hospitals under Medicaid.
- Hospitals located in counties with less than 50,000 residents which are designated health professions shortage areas.
- Hospitals providing inpatient or outpatient services without receiving any public or private payments other than charitable donations, legacies, bequests, or grants/payments for research.

The standards do not apply to:

- Hospitals or systems able to demonstrate that reductions in the amount of community benefits, charity care, and government-sponsored indigent health care are necessary to maintain financial reserves at a level required by a bond covenant or to enable it to continue operations.
- Hospitals or systems that are required to substantially curtail operations as a result of a natural or other disaster.

Pennsylvania

For state sales and local property tax exemptions, an institution of purely charitable purpose must meet **all** of the following standards:

1. It must advance a charitable purpose, being organized and operated primarily to fulfill any one or a combination of six purposes (which, in the case of nonprofit health care organizations, includes prevention and treatment of disease or injury).
 2. It must operate entirely free from private profit motive, meeting **all** of the following criteria:
 - a. Neither net earnings nor donations inure to the benefit of private shareholders or other individuals as interpreted under section 501(c)(3).
 - b. All revenues in excess of expenses are applied or reserved in furtherance of its charitable purpose or to funding other charitable organizations.
 - c. Compensation, including benefits, of any director, officer, or employee is not based primarily on the financial performance of the institution.
 - d. Its governing body has adopted as part of its articles of incorporation a provision that expressly prohibits, in the case of a sale or dissolution of the institution, the use of any surplus funds for private inurement to any person.
 3. The institution must provide community service through compliance with **all** of the following:
 - a. It must donate or render free a substantial portion of its services by providing **any** of the following:
 - It has a written policy of providing services to all who seek them without regard to their ability to pay, published in a reasonable manner, with uncompensated services at least equaling 75 percent of its net operating income but not less than 3 percent of its operating expenses.
 - It has implemented a written policy and a written schedule of fees based on individual or family income, which are consistently applied, with at least 20 percent of patients paying no or a reduced fee, and at least 10 percent of patients receiving a reduction of fees of at least 10 percent.
 - b. It provides free care to at least 5 percent of its patients receiving similar care.
 - It provides free or discounted care to at least 20 percent of its patients receiving similar care, with at least 10 percent of patients paying no fees or fees discounted by at least 10 percent.
 - Uncompensated services or goods represent at least 5 percent of its costs (“uncompensated services” includes free and discounted care, subsidies provided for education and research programs, losses under any government program, subsidies for community services, and donations to other institutions of purely public charity or to a government agency, and the reasonable value of volunteer assistance provided by its employees).
- The institution may elect to average the applicable data for its five most recently completed fiscal years in determining compliance with these any of the above quantitative standards.
- b. The institution must benefit a substantial and indefinite class of persons who are legitimate subjects of charity, which in the case of nonprofit health care institutions requires them to qualify for federal tax exemption under section 501(c)(3) or section 501(c)(4).
 - c. The institution must relieve the government of some of its burden, as determined by compliance with **any** of the following:
 - Provides a service to the public that government would otherwise be obliged to fund or to provide directly or indirectly or to assure that a similar institution exists to provide the service.
 - Provides services which are the responsibility of government by law or which historically have been assumed or offered by government.
 - Receives on a regular basis payments for services under a government program that are less than costs.
 - Provides services which directly or indirectly reduce dependence on government programs or lessen the burden borne by government for the advancement of social, moral, educational, or physical objectives.

¹ “Comparison Between the Recommendations of the Catholic Health Association and VHA, Inc.’s *A Guide for Planning and Reporting Community Benefit and State Community Benefit and Related Laws, Guidelines, and Standards*”, CHA/VHA, Inc.