

Advisory

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Connecticut Supreme Court Clarifies Application of Property Tax Exemption For Charitable Organizations

On March 24, 2009, the Connecticut Supreme Court issued a landmark property tax decision in *St. Joseph's Living Center, Inc. v. Town of Windham* — a case litigated on behalf of St. Joseph's by Wiggin and Dana. The decision provides a detailed analysis of the requirements for property tax exemption as a charitable organization under § 12-81(7) of the Connecticut General Statutes. We summarize below the Court's most significant holdings.

St. Joseph's involved a non-profit nursing home that provided, on a first-come, first-served basis, regardless of patients' ability to pay, both long-term care for the elderly and short-term rehabilitative care for all ages. The trial court had found that St. Joseph's was not entitled to exemption for a host of reasons, relying primarily on the fact that the nursing home (1) accepted private-pay patients in addition to its larger roll of Medicaid and Medicare recipients, and (2) ran an operating surplus for the tax years at issue. On appeal, the Supreme Court squarely rejected the trial court's holdings on these two issues, but nonetheless upheld the denial of St. Joseph's tax exemption on the ground that rehabilitative care was not identified in St. Joseph's Certificate of Incorporation as one of its charitable purposes.

In a comprehensive majority opinion, the Court provided guidance on a number of questions facing all non-profit facilities seeking to qualify for property tax exemption as charitable organizations — especially health care facilities not

otherwise exempt under Connecticut General Statutes §§12-81(16) (exemption for hospitals and sanatoriums) or 12-81(75) (exemption for non-profit nursing homes which were not on a taxable grand list as of October 1, 1999).

PROVISION OF HEALTH CARE TO THE INDIGENT IS A CHARITABLE ACTIVITY

It is now undisputed that, in Connecticut, a non-profit's provision of long-term health care to the elderly without regard to their financial circumstances is a charitable activity, at least if the facility has indigent patients. An entity engaged in such an activity is not in danger of losing its tax exemption simply because it accepts some private pay patients, or because it runs a surplus of revenues over expenses.

Because St. Joseph's provided primarily long-term care to the elderly, the Court's opinion focused on that charitable purpose and activity. Nevertheless, the Court's decision accepted a very broad definition of what is "charitable," making it reasonably clear that a non-profit entity that renders health care services of any kind, if it is structured to and actually does provide care to the indigent, would be deemed charitable.

On the other hand, the Court seemed to question whether short-term rehabilitative services to patients of all ages would be charitable, raising the question whether the Court might view some kinds of health care services, or the provision of

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health care to the young and middle aged, not to be charitable. We do not think either is the case. Rather, we suspect that the Court's concern stemmed from its impression that St. Joseph's rehabilitative program was principally intended to increase its revenues and was not structured or operated so as to provide such care to Medicaid recipients, and from the Court's view that such a program would not be charitable. We do not believe the Court would find that a rehabilitation program that is open to all, regardless of age or financial means, and is structured and operated to provide care to the indigent, would be inconsistent with a nursing home's charitable exemption, provided that such purpose was expressly stated in its certificate of incorporation.

ORGANIZED EXCLUSIVELY FOR CHARITABLE PURPOSES

In the words of the Court, any entity seeking a property tax exemption as a charitable organization under § 12-81(7) must be "organized to carry out an exclusively charitable purpose."

Satisfaction of this requirement is based on a review of the organization's formative documents (*e.g.*, Articles of Incorporation or Charter). This corporate requirement is, according to the Court, "the sine qua non of a charitable organization."

Charitable entities should therefore review their corporate documents to be certain that all their charitable purposes, and no other purposes, are clearly and specifically stated therein.

If the organization is found to have an exclusively charitable purpose, then two other factors are considered "under the totality of the circumstances to determine whether the organization is, in fact,

fulfilling its charitable purpose." First, a charitable organization should not be entirely "self-supporting," and second, a charitable organization's activities should "relieve a burden on the state." While the Court noted that the failure to satisfy either factor may not be fatal, it is unclear whether and in what circumstances this would be so. The Court did, however, provide specific guidance about how these factors are satisfied in the health care context.

Self-supporting. So long as an entity is "structured in such a way that it is intended to function with the aid of at least some private charitable support" and so long as the charitable entity does "seek out and receive such support," it will not be deemed "self-supporting." Importantly, the required "charitable support" need not be limited to cash contributions. For example, in concluding that St. Joseph's satisfied this requirement, the Court noted that the facility received a land donation and a subsidy for its employees' health insurance from the local Diocese and received support in form of volunteer services from the community. While an entity is required to seek out and actually receive some charitable support, it is not required to depend on the monetary value of these cash or in-kind donations to stay afloat.

Further, an entity is not deemed to be "self-supporting" because it has an excess of revenues over expenses, so long as the entity uses the excess revenue in a manner that is consistent with its charitable purposes.

Finally, the Court cleared up confusion about the statutory bar (in Connecticut General Statutes § 12-88) against a charitable organization deriving "rents,

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profits or income” from its property, holding that the bar applies only to property that is not being used for charitable purposes because the buildings that will house the charitable activity are still under construction. For other property, the bar does not apply, and the income that the organization receives will be analyzed in the context of determining whether the organization is self-supporting, so long as no “profits” are distributed to its officers or employees.

Relieving a government burden. As to the second factor, the Court held that a charitable entity may lessen the burden on government either (1) by relieving the government of a financial burden or (2) “by pursuing a publicly mandated moral obligation.” In the health care context, an entity that provides health care on a first-come, first-served basis regardless of ability to pay meets both prongs because (1) it provides care to the indigent (Medicaid patients) and does not receive full reimbursement for that care, even if it makes up the shortfall with revenues from private pay patients, and (2) accepting indigent patients is a publicly mandated moral obligation. Importantly, a health care facility will not lose its tax exempt status simply because it receives government funds or payments from private pay patients.

Private pay patients. In the view of the trial court, St. Joseph’s admission of private-pay patients meant that its purpose was not exclusively charitable. The Supreme Court rejected that position, noting that it has never held that “accepting payment or charging a fee, without more, alters the character of a charitable or otherwise tax-exempt organization.”

USED EXCLUSIVELY FOR CHARITABLE PURPOSE

To satisfy the Court’s test for property tax exemption as a charitable organization, an entity must also use its facility exclusively for carrying out its charitable purposes. In *St. Joseph’s*, the Court took a restrictive view of this requirement. First, by holding that St. Joseph’s provision of rehabilitative care was outside the purposes stated in its certificate of incorporation, even though that document included the purpose to “operate and maintain a chronic and convalescent care nursing home,” the Court implicitly determined that such purpose clauses must be carefully worded to refer specifically to each charitable purpose (e.g., “convalescent care” was not specific enough to mean “rehabilitative care” to the community at large). Second, any activity other than the specific charitable activities specified in the entity’s certificate of incorporation and other formative documents must be “necessary for” or “indispensable to” the accomplishment of the organization’s tax-exempt purpose.

The Court held that St. Joseph’s provision of rehabilitative care to people from the community was not necessary to accomplish the charitable purpose that was identified — providing long-term care for the elderly. The Court indicated that St. Joseph’s could obtain tax-exempt status by providing rehabilitative care only to its long-term care patients, or by amending its certificate of incorporation to include such care for the elderly in the community as one of its charitable purposes. In light of the Court’s holding, it is important that charitable organizations review their formative documents to ensure that they

specifically address all charitable activities that take place on their property.

The Court did leave some wiggle room, stating that non-charitable uses that are “incidental” or “secondary” may not defeat a tax exemption. It is unclear, however, what the Court will find to be an “incidental” use that is permissible even though it does not further the entity’s charitable purposes. There appears to be room in the Court’s opinion for infrequent, non-charitable uses (e.g., an annual social function), but only time will tell how infrequent or insignificant such uses need to be in order to be deemed “incidental” or “secondary.” Hence a charitable entity using its facility (or a portion thereof) for an activity outside of the charitable purposes specified in its charter or articles of incorporation should be cautious if the activity is substantial or takes place with any regularity.

PARTIAL EXEMPTION FOR MULTI-USE FACILITIES

Under § 12-88, if a portion of real property is used for charitable purposes and another portion is not, then the property may be divided into taxable and tax-exempt portions. The Court in *St. Joseph’s* clarified that such a division must be physical and complete—i.e., that the tax-exempt portion of the facility must be physically segregated and dedicated solely to the specified charitable activities. In this case, the Court held that St. Joseph’s was entitled to an apportioned exemption for a chapel at the center of the nursing home, which was physically separate and used exclusively for religious worship, but not for its rehabilitative facilities because they were not physically separate.

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In practice, determining whether a specific use is “physically segregated,” and how to apportion space used for both the charitable and non-charitable activity, may be difficult. The Court in St. Joseph’s did not have occasion to address these issues. Thus, a charitable entity using its facility for dual purposes would be well advised to keep all aspects of the non-charitable use physically separate if it wishes to seek property tax exemption for the charitable portion.

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