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TESTIMONY BEFORE THE SENATE FINANCE COMMITTEE
ON ACT 55, INSTITUTIONS OF PURELY PUBLIC CHARITY

Presented by
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Good morning. I am Douglas E. Hill, Executive Director of the County Commissioners Association of Pennsylvania. CCAP is a non-profit, non-partisan association providing legislative, training, insurance, research, technology, and similar services to all of the Commonwealth's 67 counties.

We appreciate this opportunity to offer our comments on Act 55 of 1997, the Institutions of Purely Public Charity Act, to members of the Senate Finance Committee.

Article VIII of the Pennsylvania Constitution provides for governmental finance, and section 2 delineates allowable exceptions from taxation. Among these is an exemption for "institutions of purely public charity", a phrase that was part of the Constitution since about 1874 but never adequately defined, and thus for more than 100 years the subject of litigation. Finally, in 1985 in *Hospital Utilization Project v. Commonwealth*, the Pennsylvania Supreme Court combined standards judicially established over the prior century into a five-prong test for determining whether an entity is qualified as a purely public charity within the meaning of the Constitution.

Under HUP, the entity must meet all of the following: 1) it advances a charitable purpose; 2) it donates or renders gratuitously a substantial portion of its services; 3) it benefits a substantial and indefinite class of persons who are legitimate subjects of charity; 4) it relieves the government of some of its burden; and 5) it operates entirely free from profit motive.

The Constitution also provides that the exemption is extended only to parcels that are "actually and regularly used for the purposes of the institution."

While the HUP tests established standards for application of the Constitutional provision, even that was the subject of continuing uncertainty and continuing litigation as parties on both sides sought better definition and uniformity of each of the tests, for example better clarity of "a substantial portion of its services", "a substantial and indefinite class of persons", or "governmental burden".

As a consequence of this ongoing cycle of litigation, the General Assembly convened interest groups in the mid-1990s to develop legislation that would bring some definition and clarity to the matter, an exercise that resulted in Act 55 of 1997, the Institutions of Purely Public Charities Act.

The working premise of the negotiations that led to the Act was formed around a basic consensus among the groups on the tests enumerated in HUP by the Courts, and development of statutory criteria around those tests. Our Association was an active participant in those negotiations, representing counties' dual role as a taxing body and as the entity responsible in the first instance for determination of the taxability, and assessed value, of real property.

In general, we ultimately signed off on the final work product, based primarily on a notion that the statute constituted better defined standards, giving better direction to our assessment offices and resulting in greater certainty and less litigation.

The statute represents several trade-offs and compromises. Most notably, it includes an expansive section on “community service” (Section 5(d)) that defines a number of alternative ways the institution can assert that it “donate(s) or render(s) gratuitously a substantial portion of its services”. While some argued that the wealth of alternatives and the seemingly low percentages of activity would allow an institution to meet this community service test with relative ease, the statute also included a provision (Section 7), not specifically enumerated in either the Constitution or HUP, that affirms that the institution can enter into a voluntary agreement with a political subdivision to make contributions to that political subdivision “to help ensure that essential governmental, public or community services will continue to be provided in a manner that will permit an institution to continue to fulfill its charitable mission”. Taken together, the intent of the legislature was to clearly target several classes of properties for exemption, but at the same time to allow local governments a means to negotiate what amount to payments in lieu of taxes as a middle ground.

In practice, the statute has had a reasonably positive effect on the manner and process of determination of exemption. Although political subdivisions may argue that the bar for exemptions was set too low, the standards were a public policy determination by the General Assembly. Regardless, the application of the statute has given county assessment offices a relatively clear standard to apply in determining an entity’s qualification as an institution of purely public charity.

That is not to say that there has been universal agreement on the standards or their application. Indeed, we continue to litigate matters of qualification, and the case law continues to evolve. Interestingly, the Courts still apply the HUP tests as their primary measure, but informed by the standards contained in Act 55. The difference is that the cases that go to litigation tend to be either ones that dispute whether the institution meets one or more of the tests, or ones that are for a class of institutions not previously tested as charitable.

The former are most frequently matters of fact determination, while the latter are more challenging in that they represent potential precedents for new classes of exemptions. These typically are institutions not considered when Act 55 was under development, including for example some types of assisted living facilities, and some types of university housing. What we have seen in some of these cases is an attempt on the part of an institution to recast its structure in a way that attempts to meet the tests of the Act and gain an exemption.

The other issue that we face is a somewhat inconsistent application of both the statute and the case law by the lower courts. While this typically gets resolved as cases proceed on appeal, and is more likely to improve in consistency as the body of case law evolves, in the interim it remains problematic.

We are pleased to note that many counties and institutions have successfully negotiated contributions of payments-in-lieu-of-tax. Often these agreements are reached to avert or to settle litigation, most frequently where the fact situation is in dispute or where an institution is testing corporate or service structure not clearly covered by the Act.

Regardless of its relative success or issues that remain to be resolved, Act 55 must be placed in the larger context of local revenue generation and local tax equity. We must note that property taxes are the only form of tax revenue available to counties, and are a predominant revenue source for municipalities and school districts. Each exemption that is granted becomes a burden that must be borne by other taxpayers. Our tax base continues to erode by degrees, either by legislative action (Public Utility Realty Tax Act restructuring, Keystone zones, wind farms, billboards,) or by judicial fiat (oil and gas). Governmental entities clearly recognize the value in charitable institutions that reduce the need for taxpayer-funded services, but the trade-off in value for the taxes foregone needs to be appropriate and defensible. The Association, on behalf of the general class of property tax payers, would resist any efforts to make charitable exemption more broadly available or easier to attain.

To close, let me place another issue on the table. The CCAP Pennsylvania County Platform, a compilation of resolutions adopted by our counties, calls for tax revenue foregone or lost by grant of special status to be reimbursed by the state. Noting that any grant of exemption or special tax status increases the burden on other taxpayers, perhaps this is a matter that should be included in the Legislature's ongoing discussions on local property tax relief. The Pennsylvania Constitution already acknowledges this concept, albeit in a limited fashion, where in Article VIII, Section (b)(ii) it allows the Legislature to establish "a class or classes of subjects of taxation the property or privileges of persons who, because of age, disability, infirmity or poverty are determined to be in need of tax exemption or of special tax provisions". . . (provided) "no exemption from any tax upon real property shall be granted by the General Assembly under this clause unless the General Assembly shall provide for the reimbursement of local taxing authorities by or through the Commonwealth for revenue losses occasioned by such exemption."

Thank you for the opportunity to present our remarks. I will be pleased to answer your questions.