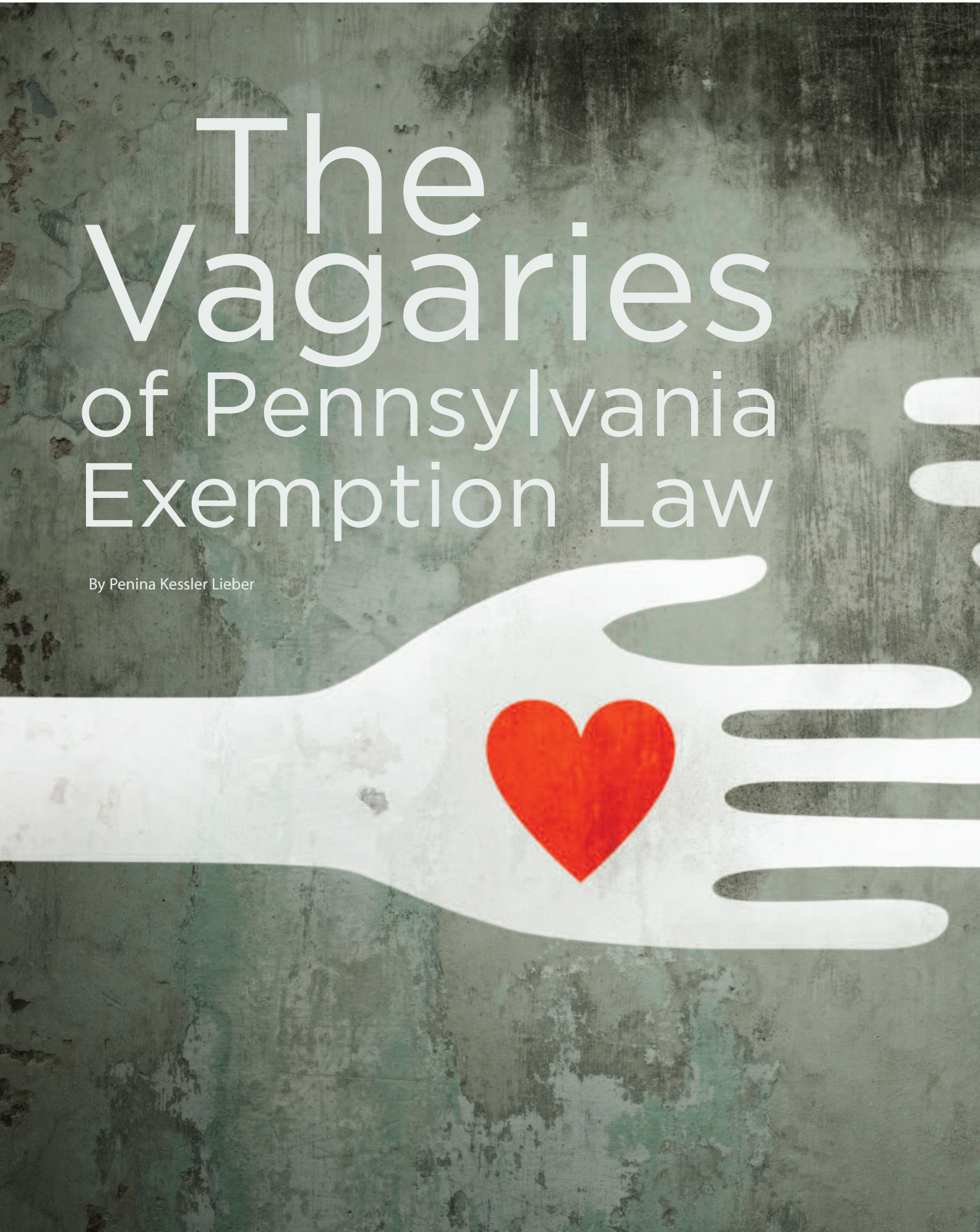

The Vagaries of Pennsylvania Exemption Law

By Penina Kessler Lieber

Editor's note: The Pennsylvania Lawyer *first looked at the implications of the Pennsylvania Supreme Court's decision in* Hospital Utilization Project v. Commonwealth *with the article "The Intersection between Pike County and America's Health Care Reform" in our January/February 2013 issue. This article takes a further look at the subject from a slightly different perspective and in light of recent legislative developments.*

At the end of February 2013, the Allegheny County solicitor mailed 2,800 letters to real estate parcels owned by nonprofit organizations designated as "institutions of purely public charity." The letters required a response within 60 days that would demonstrate how the organization satisfied the *HUP* test and would therefore be entitled to exemption from real estate tax. If no timely response was received, the organization risked losing its exemption for its parcels. Authority for this mandated review was a 2007 ordinance (Ord. 49-07) that directed a triennial review of exempt properties in Allegheny County. This was the first time that the ordinance had been enforced, and it heralded a new level of scrutiny on a uniform basis. The next rounds of review would focus on parcels held by nonprofit cemeteries, VFW posts, public places and places of religious worship. The current solicitor, Andrew Szefi, predicts that it will fall to the next county solicitor to complete this task.

The *HUP* test (*Hospital Utilization Project v. Commonwealth*, 507 Pa. 1 (1985)), has had a huge impact on the nonprofit community since it was decided by the Pennsylvania Supreme Court in 1985. It was not the first time, however, that the courts had wrestled with the inscrutable term found in the Pennsylvania Constitution in Article VIII, §2(a)(v): "The General Assembly may by law exempt from taxation … [i]nstitutions of purely public charity, but in the case of any real property tax exemptions only that portion of real property of such institution which is actually and regularly used for the purposes of the institution." In a line of cases that grew from *Episcopal Academy v. Philadelphia*, 150 Pa. 565, 25 A.55 (1892), continued through *YMCA of Germantown v. Philadelphia*, 323 Pa. 401, 187 A.204 (1936), and extended through *Ogontz School Tax Exemption*, 361 Pa. 284, 65 A.2d 150 (1949), Pennsylvania courts have struggled unsuccessfully to clarify the meaning of the term "institutions of purely public charity."

One would assume that the Supreme Court took the *HUP* case in the hope that it could resolve the long-standing confusion as to the meaning of this term. The problem, however, was that this was an inapposite case — with facts that

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did not fit the norm for real estate exemption cases. It was not a property tax case; rather, it arose from a sales-and-use tax matter. It did not involve a charity or a charitable program. The Hospital Utilization Project provided no direct charitable services and served a discrete number of member hospitals that paid a fee for service for the statistical utilization information provided. While the overall purpose of the project might have been initially laudatory — to improve the quality of health care — the actual mechanics of the program were in no way charitable.

The *HUP* court drew on earlier cases and prior precedents to arrive at the famous (or infamous) five-prong *HUP* test, which would thereafter serve as the litmus test by which all nonprofit owners of parcels would be measured. Under *HUP*, all five prongs must be satisfied. In other words, an organization must prove that it meets each of the following criteria:

- Advance a charitable purpose;
- Donate or render gratuitously a substantial portion of its services;
- Benefit a substantial and indefinite class of persons who are legitimate subjects of charity;
- Relieve government of some of its burden; and
- Operate entirely free of private profit motive.

The criteria are overbroad, ambiguous and unclear. What does a "charitable purpose" mean in today's world, where charity is no longer the sole domain of the poor, widowed and orphaned? What does it mean to render "gratuitously" a "substantial" portion of services? Who constitute "legiti-

mate subjects of charity" in our modern societal paradigm? What is government's burden? Is it defined by statute? Ordinance? Custom? Does this assertion of burden include public-private partnerships at a time when there is a dramatic overlapping of the sectors? And finally, what does "entirely free of private profit motive" mean? Does it contemplate reimbursement and third-party pay? Is it limited to private inurement (private person)? How do the profitable mega-health care institutions pass this test?

Soon after the *HUP* decision was handed down, the Supreme Court recognized the limitations of the test and tried to remedy the resulting confusion. Two later Supreme Court cases (*St. Margaret Seneca Place v. Board of Property Assessment Appeals and Review* (1994) and *Appeal of the City of Washington from the Action of the Board of Assessments, Appeals and Review on Property Situate in the City of Washington and W&J College* (1997)) helped by identifying a "charitable care component" in the variance between actual cost and reimbursed cost in nursing home settings and including private post-secondary education within the term "government burden."

In 1997 the General Assembly passed Act 55 (Institutions of Purely Public Charity Act), which codified *HUP* and added additional objective criteria to the otherwise subjective five prongs. Although the nonprofit community readily embraced Act 55, the problems did not disappear as a new debate regarding controlling law emerged. In 2002, *Community Options, Inc. v. Board of Property Assessment, Appeals and Review*, 571 Pa 672, 813 A.2d 680 (2002), concluded that "[a]n entity seeking a statutory exemption … must first establish that it is a 'purely public charity' under Article VIII, Section 2 of the Pennsylvania Constitution before the question of whether that entity meets the qualifications of a statutory exemption can be reached."

On April 25, 2012, a new shudder of concern swept through the nonprofit community when the decision in *Mesivtah Eitz Chaim of Bobov, Inc. v. Pike County*

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Board of Assessment Appeals and Delaware Valley School District and Delaware Township (Pike County case) was announced by the Supreme Court. The specific question before the Supreme Court was "[w]hether the Pennsylvania Legislature's enactment of criteria in Act 55 for determining if an organization qualifies as a 'purely public charity' under Pennsylvania's Constitution is deserving of deference in deciding whether an organization qualifies as a 'purely public charity' under Pennsylvania's Constitution, or has the test in *Hospital Utilization Project v. Commonwealth* … occupied the constitutional field, leaving no room for legislative influence and input." Justice J. Michael Eakin, writing for the majority, held that Act 55 cannot excuse the constitutional minimum — "if you do not qualify under the *HUP* test, you never get to the statute." In dissent, Justice Thomas G. Saylor argued that the Legislature gave appropriate deference to the constitutional rulings and had not displaced the *HUP* test in its entirety.

The effort to define "institutions of purely public charity" continues to resurrect itself in different forms. The General Assembly is now considering two bills that would amend the Pennsylvania Constitution and place authority in the Legislature to define the term. Senate Bill 4 (introduced by Sen. Mike Brubaker on Feb. 5) proposes to add the following clause: "The General Assembly, may, by law: Establish uniform standards and qualifications which shall be the criteria to determine qualification as an institution of purely public charity. …" House Bill 724 (introduced by state Rep. Kerry A. Benninghoff on Feb. 25) tracks that language. SB 4 was approved by the Senate Finance Committee and passed the Senate by a vote of 30-20. The process of amending the constitution is no task for the novice since it requires passage by both houses in two consecutive sessions and then approval by a public referendum.

The sides have lined up predictably. Those supporting the proposed amendment are the members of the nonprofit community, including the Hospital and Health System Association of Pennsylvania, the Association of Independent Colleges and Universities of Pennsylvania, the Pennsylvania Catholic Conference and United Way of Pennsylvania. Opposing the amendment are the municipal bodies, including the Pennsylvania Municipal League and the Pennsylvania State Association of Township Commissioners, which cite the escalating burdens carried by municipalities today.

Obviously, the war is not over. *HUP* continues to rear its head and continues to prompt incredulous responses from both large and small nonprofits as they struggle to make a convincing case. Other municipalities, like Allegheny County, are facing new challenges in light of scarce resources, budgetary demands and increasing numbers of exempt properties. The tensions that have marked this area of the law have continued since the phrase "institutions of purely public charity" was first coined. Has this confusion been resolved? One might have to admit, not likely! ✦


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