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Supreme Court Rules Against Provena

Many of our Illinois hospital clients—especially those we represent on pending real estate tax exemption applications—have been awaiting the Illinois Supreme Court's decision in the *Provena* matter with the hope that the decision would provide a "bright line" test and clarity. As discussed below, the decision leaves many unanswered questions.

In a case closely watched across the nation, on March 18 the Illinois Supreme Court upheld the 4th District Appellate Court's decision affirming the denial of real estate tax exemption for property owned by Provena Hospitals. Because less than a majority of the court (a "plurality") agreed on all aspects of the opinion, key parts of the opinion are not binding, and the broader question of what hospitals must do to receive real estate tax exemption in Illinois remains unsettled. The practical effects of the decision may ultimately prove significant and far-reaching for Illinois hospitals (and other charitable health care organizations), whether currently exempt or seeking exemption from real estate taxes. For this reason, it is critical that Illinois charitable health care organizations understand the decision and how it may affect their operations.

Below is a summary of the decision and key practical implications for Illinois hospitals.

<u>Charitable Ownership of the Property</u>. In order to be eligible for charitable exemption from real estate taxes in Illinois, a property must be <u>owned</u> by a charitable institution. The Department of Revenue previously determined that Provena failed this test. The appellate court concluded that the Department of Revenue's determination was not clearly erroneous, and the Supreme Court agreed. Importantly, the Supreme Court cited the following factors that argued against characterizing Provena Hospitals as a charitable institution:

- Provena Hospitals failed to show that it dispensed charity to all who needed and applied for it and did not place obstacles in the way of those in need of charitable benefits. Though the record was full of details regarding the charitable activities of Provena Covenant Medical Center (PCMC), Provena Hospitals (and not PCMC) was the legal owner of the property. The record did not contain any evidence as to Provena Hospitals' charitable expenditures.
- Provena Hospitals' funds were not derived mainly from private and public charity. Rather, they were generated—overwhelmingly—by providing medical services for a fee. The relevance of this factor in modern times has been questioned; however, the Supreme Court gave no indication as to the relative importance of this particular factor.

<u>Charitable Use of the Property</u>. In order to be eligible for charitable exemption from real estate taxes in Illinois, a property must also be used exclusively (i.e., primarily) for charitable purposes. The justices were split in their interpretation of the charitable use test, and therefore, this portion of the decision is not binding. However, it is important to note that three of the five justices based their determination on the following rationale:

For assistance in determining whether your current policies and procedures support continued exemption or if you have any questions regarding real estate tax exemption applications, charity care policies and related analysis, please contact your Katten Muchin Rosenman LLP attorney or:

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- Charity is defined as a "gift" and treating patients for a fee is not a gift.
- Neither Medicaid nor Medicare shortfalls may count as charity.
- Both the number of uninsured patients receiving free or discounted care, and the amount of charity care provided, was "de minimis" (nominal). With limited exception, the property was devoted to treating patients in exchange for compensation. The minimal amount of charity care dispensed could not be rationalized on the grounds that the area's residents did not require additional services.
- The record showed that Provena Hospitals did not advertise the availability of charity care; billed patients as a matter of course; automatically referred unpaid bills to collection agents; and discounted or waived charges only after it was determined that a patient had no insurance coverage, was not eligible for Medicare or Medicaid, lacked requisite resources and could provide documentation sufficient to qualify.
- The "community benefit" standard—the basis for federal tax exemption—is not the basis for real estate tax exemption in Illinois. To this end, the plurality stated that Provena's free health screenings, volunteer classes and classes on handling grief, while beneficial for the community, were not necessarily charitable. Indeed, these same benefits are frequently offered by for-profit companies to generate publicity and goodwill. Similarly, the plurality stated that Provena's donations to other charitable institutions did not demonstrate that the *PCMC property* was used exclusively for charitable purposes.
- To qualify for real estate tax exemption, the charitable hospital must relieve a burden on government. The plurality opinion states that, "while a direct, dollar-for-dollar correlation between the value of the exemption and the value of the goods or services provided by the charity is not required, those seeking exemption must be able to demonstrate that their activities will help alleviate some financial burden incurred by the affected taxing bodies in performing their governmental functions." The plurality opinion asserts that, while Provena Hospitals' entitlement to a charitable property tax exemption did not depend on its ability to show that its use of the PCMC parcels reduced the burden of *each* of the affected taxing districts, it was required to demonstrate that its use of the property helped alleviate the financial burdens faced by the county or at least one of the other entities supported by the county's taxpayers.

Dissenting Opinion. Although two justices agreed with the other three justices that Provena failed to demonstrate that it was a charitable institution based on the inadequacy of the record (i.e., the fact that all the evidence related to PCMC, which was not the legal owner of the property), they did not join their colleagues in the charitable use portion of the opinion. Specifically, the dissenting opinion argues that:

- A minimal threshold of charity care is not necessary to qualify for real estate tax exemption. By imposing a quantum of care requirement and monetary threshold, the plurality is injecting itself into matters best left to the legislature.
- Alleviating the burden on government is not a condition of eligibility for charitable exemption from real estate taxes.

Implications. Accordingly, the Court's decision leaves the standard for establishing charitable use of hospital property unsettled. The plurality's views on charitable use, though not binding, also should not be ignored. Absent a legislative solution, the Department of Revenue will likely continue to closely scrutinize real estate tax exemption applications, and the Department and local assessors may reexamine long-standing exemptions. For example, this may occur when there is any substantial change in the property, such as building a new hospital facility, renovating an existing hospital facility, transferring title or leasing the hospital to another charity or an affiliate of the current charity. In light of this likely practical impact, it is paramount that all Illinois hospitals review their charity care policies and practices.