Non-Profit Hospital Real Property Potentially Exempt from County Property Taxes

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Double-check the Tax Man by Double-checking your Parcel Usage

Understandably, most hospital accounts payable departments are good at paying bills that come in the mail. However, when it comes to paying any bills that come in from the county tax collector, Arkansas non-profit hospital accounts payable departments should pause briefly before issuing payment. This is because there is a fair chance that a tax bill for property taxes is a tax bill that an Arkansas non-profit hospital does not owe.

For the reasons detailed below, Arkansas non-profit hospital accounts payable departments would be wise to pause to double-check which specific parcel (e.g., a specific area of real estate similar to a defined lot) the bill is for and whether that parcel is used exclusively for its hospital operations and whether other certain legal requirements are met. If all of the requirements are met, it is time for the hospital to communicate with the county assessor with the goal being to have the parcel removed from the taxable list and placed on the county's exempt property list.

Arkansas has a long history of exempting non-profit hospitals from county property taxes. This exemption comes from the Arkansas Constitution itself. Article 16, § 5(b) of the Arkansas Constitution of 1874 mandates exemption from taxation of all "buildings and grounds and materials used exclusively for public charity." This Constitutional provision was first recognized as potentially applying to hospitals in 1893.[1] It was the religious Sisters of Mercy in Hot Springs who, in 1907, first won exemption under Article 16, § 5(b) of the Arkansas Constitution for a hospital they operated which had 24 beds for "charity patients" and other beds for "patients who pay."[2]

One recent reaffirmation of the property exemption holding from the *Sisters of Mercy* case occurred in 1988, and it actually applied its hospital exemption standard not to a hospital but to a mental health counseling facility. In *Sebastian Cty. Equalization Bd. v. W. Ark. Counseling & Guidance Ctr., Inc.*, 296 Ark. 207 (1988), the Arkansas Supreme Court summarized as follows the standard for hospital exemption first established by the *Sisters of Mercy* hospital case:

a benevolent and charitable organization's property used as a hospital may be constitutionally exempt from taxation if (1) it is open to the general public, (2) no one may be refused services on account of inability to pay, and (3) all profits from paying patients are applied to maintaining the hospital and extending and enlarging its charity.

Here is a check-list of what a non-profit Arkansas hospital should do when it receives a tax bill for a real estate parcel it owns or leases under a term exceeding ten (10) years:

Step One

Confirm whether your hospital satisfies the three operational requirements discussed in the *Sebastian County* case:

1. is the hospital open to the general public?
2. is it the hospital's practice that no one is refused services on account of inability to pay?
3. are all profits from paying patients applied to maintaining the hospital and extending and enlarging its charity?

Note that requirement two is distinct from whether a patient might or might not qualify (after services have already been provided) for a reduction or cancellation of a hospital bill under a hospital's financial assistance policy.[3] Requirement two is focused on whether the providing of medical care is conditioned, at the outset, on the hospital's determination of one's ability or inability to pay. The authors are not aware of any hospital that utilizes such a litmus test.

Step Two

If the three operational requirements discussed in the *Sebastian County* case are satisfied, next determine if the specific parcel on which property taxes have been levied is directly used for hospital operations. This issue goes to the "used . . . for" requirement under Article 16, § 5(b) of the Arkansas Constitution. For example, parcels that a hospital rents or leases out to private parties, such as nearby houses and commercial buildings that generate rental income for the hospital, will likely not make the cut for exempt status because they are not directly used for hospital operations. Undeveloped parcels held for *future* hospital development could safely be classified as non-exempt because they are not directly used for hospital operations. However, the tax exempt status of undeveloped parcels has been called into question by a recent development in the law, and so if a hospital wishes to pursue exempt status for undeveloped parcels it may do so but could expect resistance and will likely need to involve an attorney.[4] On the contrary, parcels used for hospital parking lots, hospital maintenance or storage, hospital clinics, or hospital helicopter or ambulance staging should all satisfy the direct use requirement.[5]

Step Three

If the specific parcel on which property taxes have been levied is confirmed to be used directly for hospital operations, next determine whether *only* the hospital uses the parcel or if other non-hospital users also use the property. This issue goes to the "exclusivity" requirement under Article 16, § 5(b) of the Arkansas Constitution. To qualify for exempt status under the Arkansas Constitution, the property must be used "exclusively" for public charity. This means that if other, non-hospital uses are made of the property, it may not make the cut for exempt status. For instance, if two floors of a four story hospital clinic are occupied by hospital-affiliated doctors and medical professionals, but the other two floors are leased out to a private physician practice group for its use, the parcel likely will not qualify for exempt status. Likewise, if retail coffee shops and floral shops lease and occupy the ground floor of a hospital building, the parcel likely will not qualify for exempt status. On the other hand, if a hospital permits another company to install profit-making vending machines in its four floor office building that is occupied solely by hospital-employed doctors and medical professionals or if it rents out to the public on occasion the building's auditorium, such de minimus income is not likely to destroy eligibility for exempt status.[6]

Step Four

If the specific parcel on which property taxes have been levied is believed to meet all the requirements discussed in steps 1 – 3, the next step is to compare the parcel to other similarly situated parcels. Online tools to search all nearby parcels are found at Data Scout (https://www.actdatascout.com/) and AR County Data (https://www.arcountydata.com/index.asp). You might find that other similarly situated parcels have been correctly classified as exempt and that the assessor simply made a mistake and

overlooked the subject parcel for which a bill was sent. If such is the case, it could be something as simple as a phone call to the assessor's office to bring about a correction of the parcel's classification to exempt and to cancel the tax bill received.

On other occasions, you may find that your county assessor insists that the hospital complete and turn in a sworn-to application for exemption to document its satisfaction with all the requirements discussed above. See page 28 of the Assessor's Guide here. Given its formality, prudence counsels having the hospital's attorney review any such an application and its attachments before it is submitted.

If things cannot be resolved in working with the assessor's office, litigation is your next step. Because it involves county taxes, the suit must first be filed in County Court and decided by the County Judge. If either side does not like the ruling, they can appeal it to the Circuit Court in the County and ultimately on to the Arkansas Supreme Court.

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Modern non-profit hospitals often occupy sprawling campuses spread over many acres of land and are comprised of a multitude of buildings housing various hospital departments and clinics. Hospitals often buy adjacent land and buildings over a period of time when they become available, which to hospital personnel may be considered one "campus," while county tax records may reflect a patchwork of different pieces of land. Such a campus could be comprised of dozens of distinct parcels on file at the county assessor's office.[7] A single property tax bill for a single parcel used for hospital purposes may not warrant much thought, but a handful of such erroneous bills, paid year-after-year by a non-profit hospital, are likely to add up to a sizable amount of money out the door. Care should be taken to investigate all county tax bills that come to a non-profit hospital to determine which may be for properties that Arkansas law deems to be exempt from taxation.

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[1] *Brodie v. Fitzgerald*, 57 Ark. 445 (1893).

[2] *Hot Springs Sch. Dist. v. Sisters of Mercy of Female Academy of Little Rock*, Ark., 84 Ark. 497 (1907).

[3] Tax exemptions based on public charity have been granted where the evidence showed various percentages of patients who ultimately proved to be charity patients. *See, e.g.*, *Sebastien Cnty.*, 296 Ark. at 211, 752 S.W.2d at 758 (35% of patients were seen without charge); *Burgess v. Four States Mem. Hosp.*, 250 Ark. 485, 489, 465 S.W.2d 693, 694 (1971) ("only three charity patients have been treated at the hospital")

[4] *Hardesty v. N. Ark. Med. Servs., Inc.*, 2019 Ark. App. 410, 2, 585 S.W.3d 177, 179 (2019) (vacant lot was held to be exempt).

[5] *Hardesty*, 2019 Ark. App. 410, 2, 585 S.W.3d 177, 179 (exempting parcels used for clinic buildings and parking areas located across the street from the main hospital campus).

[6] *Sebastian Cty.*, 296 Ark. at 211.

[7] *Hardesty*, 2019 Ark. App. 410, 2, 585 S.W.3d 177, 179 (there was no dispute that the main hospital itself and the adjacent lots and facilities were already considered tax exempt. It took extensive litigation to get declared as exempt seven across-the-street parcels that had been acquired at a later date by the hospital).