
Coates' Canons Blog: What Does It Mean to be Charitable?

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Last year I [blogged](#) about the increasing willingness of local governments to push back against charitable property tax exemptions for non-profit organizations. Two recent law review articles demonstrate that this trend continues to gather steam. Although the articles involve different types of non-profits and different types of property, they both focus on the same key property tax exemption question: What does it mean to be “charitable?”

In [“Lay of the Land: Where Does Property Tax Exemption for Health Care Entities Stand Now?”](#) 28 *Taxation of Exempts* 38 (Jan. 2017), Janice M. Smith and John V. Woodhall analyze a New Jersey court decision denying a property tax exemption for a large non-profit hospital. In [“Charitable Commerce: Examining Property Tax Exemptions for Community Economic Development Corporations,”](#) 116 *Columbia Law Review* 1503 (Oct. 2016), Catriela Cohen discusses a New York court decision removing the property tax exemption from property owned by a non-profit economic development organization.

While property tax exemption categories and definitions vary widely from state to state, one constant is the charitable purpose and charitable use test. A property owner seeking a charitable exemption must demonstrate both that it is organized for charitable purposes and that it uses the property in question for charitable purposes. Read more about these requirements under North Carolina law [here](#).

In the New Jersey case analyzed by Smith and Woodhall, Morristown Memorial Hospital (“MMH”) owned a million-square foot medical campus that included 700 hospital beds. MMH is organized as a non-profit corporation and treats all patients without regard for their ability to pay. However, like many other large medical centers, MMH also owned several physician practices, provided home care and nursing services, and was engaged in other for-profit activities. Of the many doctors who provided care at the hospital, some were employees of the non-profit MMH while many others were private, for-profit doctors with staff privileges or service contracts with the hospital.

Faced with the hospital’s “labyrinthine” corporate and operational structure, the New Jersey court concluded that MMH did not qualify for the charitable property exemption because it could not “distinguish where the non-profit activity end[ed] and the for-profit activity beg[an].” In other words, MMH satisfied the ownership test (it was an organization organized for charitable purposes) but failed the use test (it could not prove that it used the property for charitable activities).

The Cohen article involves a similar issue and a similar result, with a New York City non-profit losing its charitable property tax exemption due to its for-profit activities. Instead of a non-profit hospital, the owner was a charitable non-profit community economic development corporation (“CEDC”) organized to “promote the development of the business-commercial-retail district of Jamaica, Queens. The article first examines whether CEDCs in general can satisfy the “charitable purpose” requirement for property tax exemptions and then looks at the specific CEDC activity—operation of a commercial parking lot—that was at issue in the New York case.

Much like large medical centers, CEDCs are often involved in wide variety of activities, some of which are clearly charitable (offering housing and job training for low-income residents) and some of which seem to be commercial (serving a small business incubators, leasing office space to local entrepreneurs). The parking lot operated by the Jamaica CEDC falls into the latter category. A reasonably priced, well maintained public parking would certainly benefit local businesses and help further the CEDC’s community goals. However, the Jamaica CEDC generated a profit from that parking lot, which led the court to conclude that the principal use of the property was commercial and not charitable. As a result, the court denied the non-profit’s exemption.

Cohen points out that the court did not explicitly address the question of whether economic development alone is sufficient charitable purpose to justify a property tax exemption. The court's decision seems to suggest otherwise, because it was clear from the case that the parking lot in question was directly connected to the community's economic health yet the court still concluded that the parking lot should be taxable.

The authors of both articles believe that the charitable purpose and use tests were applied too harshly by the respective courts. In their view, MMH and the Jamaica CEDC were providing valuable charitable services to their communities and should have been exempt from property taxes. The authors suggest that these organizations are being penalized with the loss of their exemptions simply because their organization and reach far exceeds what existed decades ago when the relevant property tax statutes were drafted. In today's world, many non-profits are engaged in a much more diverse collection of activities, some of which lean toward the commercial side of the spectrum. In the authors' view, that fact should not threaten the organizations' property tax exemptions.

Local government officials would likely agree about the tremendous benefits provided by their local non-profits, but would also point to the gaping holes in their tax bases as these non-profits expand their reach and their property holdings. Lowering the bar on the charitable purpose and use tests would have an immediate and long-lasting impact on local governments' finances, especially where local governments are facing reduced financial support from the state.

The non-profit exemption challenges analyzed by Smith, Woodhall, and Cohen are not unique. Communities across the country are wrestling with the appropriate balance between encouraging non-profit activity and protecting their tax bases. Some are actively questioning the validity of property tax exemptions for non-profits that are engaged in quasi-commercial activities. In addition to the examples I discussed in [my earlier post](#), see [this recent article](#) about Michigan local governments seeking to tax more non-profits and [this discussion](#) of what the decision by Princeton University to settle a legal challenge to its property tax exemption might mean for other private universities.

Here in North Carolina, it appears that most counties exempt property used as headquarters for local CEDCs. But there is less unanimity about how to treat quasi-commercial activities undertaken by CEDC's and other non-profits such as job incubators.

Absent more guidance from our state legislature or the courts, local tax officials will need to decide for themselves where to set the boundary between exempt charitable programs and taxable for-profit activities. Those decisions will affect millions of dollars in local government revenue.

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