From the Fault Line on Nonprofit Property-Tax Exemptions

By: David L. Thompson

As regular readers of *Nonprofit Advocacy Matters* know, the epicenter of attempts to alter nonprofit tax policy is in the Commonwealth of Pennsylvania. That is why I accepted an invitation to testify last week before the Pennsylvania Senate Finance Committee about attempts by governments across the country to take money away from nonprofit missions through new taxes, fees, and PILOTs. The immediate issue before the Pennsylvania General Assembly is a proposed constitutional amendment to resolve who defines the term "institutions of purely public charity" – the courts or the legislature. The greater context, and the presumptions and misconceptions about charitable nonprofits that I witnessed at the hearing, are the substance of this report from the fault line.

The State Senators were well prepared and, based on their questions and comments, seemed open to new information regardless of whether it supported their pre-hearing beliefs. Despite those positive observations, there is much that nonprofits can learn from this one hearing, and the ongoing debate in Pennsylvania that is presaging rumblings elsewhere. Here are three observations:

Beware the Siren Song

The prospect of free or extra money (the siren song) causes the most informed and committed policymaker to lose focus. The Pennsylvania Auditor General spoke of his research that found governments in the commonwealth could raise $3 billion in new revenues if tax-exempt properties were not exempt. Hearing that number, the Senators at the hearing sat up and took copious notes. It is not farfetched to presume that several were imagining which priorities they could pursue with that much “new” money on the table.

It turns out, however, that the $3 billion figure was misleading in the context of this hearing, as it has been elsewhere. That amount was based on **all** tax-exempt property, including “government-owned property” – which would include the property of the federal government, commonwealth, counties, municipalities, and school districts in Pennsylvania – and not just charitable nonprofits. As a result, the basis of the $3 billion figure was irrelevant at best and certainly misleading.

In Pennsylvania, nonprofits have seen this unfortunate tactic before. A few years ago, the former Mayor of Harrisburg made the push for payments in lieu of taxes (PILOTs) from nonprofits based on the argument that 50 percent of the property of the capitol city was tax exempt (80 percent of which was government owned), and then alleged that tax-exempt nonprofits were the reason for the city’s budget woes. This same misleading argument continues to be used in localities across the country.

Key takeaway: Data points are often cherry picked to back up arguments; question the veracity of all figures used in these debates.

Even Nonprofit Supporters Don’t Understand How Nonprofits Operate

Charitable nonprofits like YMCAs have been dedicated to healthy living, family support, and community impact for more than 100 years. This fact of longevity of community service can quickly get forgotten when lawmakers receive allegations from for-profit businesses, such as health clubs, that a charitable nonprofit is competing for the same dues-paying members but not paying the same taxes. In conversations in Pennsylvania, I found that the surface appeal of the allegation was not challenged, even by lawmakers who know how nonprofits operate. Serious consideration was being given to perhaps taxing part of a nonprofit’s operations that to an outside observer “looked like” for-profit businesses.

The good news is that facts about the nonprofit business model – e.g., serving all individuals regardless of their ability to pay, using revenues to support the nonprofit mission, providing a range of additional charitable services beyond promotion of healthy lifestyles, education, and much more – can trump the partial statements of fact by the for-profit types. But the facts have to be stated out loud; presumptions that the work of nonprofits will be automatically seen and understood can be unfounded in the policymaking arena.

Key takeaway: Even lawmakers who have served on nonprofit boards may not fully understand the nonprofit business model or the unique mission-driven aspects of charitable nonprofits.

The Elephant in the Room: Shrinking Local Government Resources

Twice during the hearing a Senator stated that the way nonprofits operate is markedly different from when Pennsylvania last updated its property-tax exemption law, suggesting that it is time to revise the law. This gave me the opportunity to set the record straight. Based on input from colleagues at state associations of nonprofits and hundreds of their members, I felt confident in asserting that the nonprofit business model is under extreme stress due to increasing needs for services without an equivalent rise in resources, but is still largely in place in most subsectors of the nonprofit community. Indeed, the budget holes that local governments are experiencing are smaller today because of the work of charitable nonprofits in their communities – solving problems, reducing the cost of government, and improving quality of life and property values.

It became clear from questioning that the real problem is not property-tax exemption, but the much larger change in municipal finances that has occurred in recent decades. Governments at all levels have yet to come to terms with the Great Recession and its aftermath. Cities in Pennsylvania and across the country are finding they cannot rely on federal or state funds as much as they could in the past. In many communities, tax bases also are shrinking as businesses close shop and populations decline. The federal government has shifted its financial burdens to the states and cities, and the states have compounded it by shifting their financial burdens onto local governments. **In short, cities need revenue; they see charitable nonprofits as an untapped resource; so they marshal the**

arguments that will enable them to take those resources through new taxes, fees, and PILOTs.

This exact scenario is playing out in Maine. Maine's Governor LePage is seeking to balance the state's budget by ending revenue sharing between the state and local governments, a goal that will greatly disrupt the finances of municipalities across the state. To fill the budget gaps that this policy would create, the Governor is proposing giving local governments the ability to replace that lost revenue by granting them greater authority to tax the property of nonprofits valued at $500,000 or more. And to set the stage for the proposal, Governor LePage infamously declared in November that Maine nonprofits "don't pay their fair share", and that "they are takers, not givers" – allegations that have been aggressively and thoroughly rebutted by the **Maine Association of Nonprofits** and others.

Key Takeaway: Charitable nonprofits have alleviated, rather than created, fiscal problems in the cities, yet desperate public officials are liable to seize on changing property-tax exemptions as a panacea, or follow the siren song (see observation #1, above), to solve their immediate balance sheet problem.

Readers can find my written statement here.