
POLICY MATTERS OHIO

2912 EUCLID AVENUE • CLEVELAND, OHIO, 44115 • TEL: 216/931-9922 • FAX: 216/931-9924
HTTP://WWW.POLICYMATTERSOHIO.ORG

MEMORANDUM

TO: James Rokakis, Cuyahoga County Treasurer
FROM: Zach Schiller, Research Director
RE: PILOTs
DATE: December 17, 2004

Policy Matters Ohio was commissioned by the Cuyahoga County treasurer to research issues related to the possible development of a program under which local nonprofit hospitals would make payments in lieu of property taxes (PILOTs). This report summarizes our work relating to PILOTs and similar arrangements made by major nonprofit hospitals and some other leading nonprofit institutions in the United States.

Hospital payments in lieu of taxes

A number of the nation's elite hospitals make some kind of payment to the cities in which they are located, in lieu of taxes or for specific services. These range from very little to nearly \$2 million a year. The Cleveland Clinic is ranked fourth on the *U.S. News & World Report* Honor Roll of best hospitals that excelled in at least six of 17 specialties. University Hospitals (UH) also is ranked among the top in various specialties. Both the Clinic and UH prominently use these rankings in their marketing. Four of the other 13 hospitals listed on the *U.S. News* Honor Roll are state institutions.¹ Of the remaining nine, five have been making some kinds of contributions (two of these, Stanford and Duke, pay for fire services). The parent of a sixth, the University of Pennsylvania, made such payments to the city of Philadelphia in the 1990s but stopped doing so five years ago. The table on the next page lists the private hospitals included in the *U.S. News* 2004 Honor Roll, whether and what they pay in lieu of taxes, and the number of employees.

¹ See <http://www.usnews.com/usnews/health/hosptl/honorroll.htm>, retrieved Oct. 26, 2004. The four public institutions are the UCLA Medical Center; the University of California, San Francisco Medical Center; the University of Washington Medical Center and the University of Michigan Medical Center.

U.S. News Honor Roll Hospitals (private only), Payments made in lieu of taxes, and number of employees					
U.S. News Rank 2004	Hospital	City	Amount paid	Full-time employees ^a	Part-time employees ^a
1	Johns Hopkins Hospital	Baltimore, MD	\$3.1 million in FY04, \$2.1 million in FY05 ^b	6,820	1,353
2	Mayo Clinic	Rochester, MN	Does not pay PILOTs	not listed	not listed
3	Massachusetts General Hospital	Boston, MA	\$1,917,430 in FY04 ^c	12,000	4,146
4	Cleveland Clinic	Cleveland, OH		15,000	2,493
6 (tied)	Duke University Medical Center	Durham, NC	\$300,000 Fire Service Fee ^d	not reported	not reported
8	Barnes-Jewish Hospital	St. Louis, MO	Does not pay PILOTs	6,765	2,227
9 (tied)	New York-Presbyterian Hospital	New York, NY	Does not pay PILOTs	15,000	879
12	Brigham & Women's Hospital	Boston, MA	\$787,781 in FY04	7,964	3,216
13	Hospital of the University of Pennsylvania	Philadelphia, PA	Does not pay PILOTs now; its parent used to do so	6,751	778
14	Stanford Hospital & Clinics	Stanford, CA	\$5.2 million fire service fee, \$586,000 police fee for 2001-2002 fiscal year ^e	4,038	1,398
^a Total facility personnel as shown by www.usnews.com based on data from the American Hospital Association. Individual hospitals may report different employment levels than those shown above, but these data have been used for the sake of consistency (http://www.usnews.com/usnews/health/hospitals/search/basic_search.htm , accessed November 2004).					
^b Includes Johns Hopkins institution as a whole.					
^c Includes \$603,555 from Massachusetts Biomedical Research Corp., an affiliate.					
^d Covers Duke University as a whole. It also agreed in June to pay \$153,500 for some one-time police-related capital items, and pays impact fees under a program that requires new development to pay part of the cost of streets, parks and open space. Based on an outside study, the city council last June reduced the amount the university had to pay in such one-time fees for building and expansion from \$1,403,061 to \$773,885.					
^e Covers Stanford University as a whole, including those parts outside Palo Alto; payments to police cover only city of Palo Alto, not other areas in Santa Clara County.					

Payments in lieu of taxes may be made by the larger university that includes the hospital, as in the case of Johns Hopkins, Stanford and Duke. As a total entity, including its medical center, Hopkins paid \$3.1 million last fiscal year to Baltimore and will pay \$2.1

million in the year ending next June.² Including \$603,555 paid by a separate affiliated entity, the Massachusetts Biomedical Research Corp, Massachusetts General Hospital paid \$1.9 million to Boston in the fiscal year ended last June.³ In most instances, PILOT payments go to the city, although voluntary contributions in Philadelphia were given entirely to the school district in recent years.

These payments stem sometimes from financial crisis or duress. In Baltimore, Hopkins and other nonprofits agreed to start making such payments in 2001, when they were faced with the likelihood of a city energy tax. They agreed to pay \$20 million over four years, of which Hopkins is paying \$10.4 million. In mid-June of this year, Baltimore imposed new taxes on nonprofit institutions, including energy and phone levies that will cost Johns Hopkins \$2.1 million a year.⁴ These will replace the payments in lieu of taxes, which will not continue.⁵

Boston's PILOT program is perhaps the best established of a major city. It began in the 1980s, and now covers 43 entities contributing a total of more than \$12 million a year. These range from broadcaster WGBH to Boston University, the largest payer in fiscal 2004 at \$3.3 million.⁶ Brigham and Women's Hospital paid \$787,781 last fiscal year, and at least six other hospitals in the city besides Mass General are making PILOT payments.

The voluntary program⁷ covers what Boston would lose if a property was purchased by a tax-exempt not-for-profit and the addition in value if a building was expanded or newly constructed. The city uses different methods to calculate what the PILOT should be, but it generally attempts to obtain about a quarter of what the owner would have paid in regular property taxes on the property.⁸ This amount reflects the share of the city's operating budget that is devoted to basic services such as fire and police protection and public works. Under some circumstances, institutions may pay up to a quarter of this amount in services, such as scholarships or free use of facilities, not provided previous to the

² "Mayor O'Malley Bridges Historic Agreement; Secures Much Needed Revenue for City," Press advisory, Office of the Mayor, June 15, 2001, and "Mayor drops plan to tax nonprofits," by M. Dion Thompson, *The Baltimore Sun*, June 9, 2001.

³ Statistical information on PILOTs in Boston was supplied in an Accounts Summary from the Assessing Department, City of Boston. The city is currently negotiating a PILOT on a new Mass General outpatient center, and another one of the hospital's facilities may be subject to a PILOT contract this year. Both Mass General and another of the top hospitals in the *U.S. News* ranking, Brigham and Women's Hospital, are members of a larger health-care delivery system, Partners HealthCare.

⁴ The city approved monthly fees on conventional and cell phones, doubled the tax on real estate sales and extended its existing energy tax. Nonprofits will pay a 6 percent rate starting in July 2005. Residents and manufacturers will pay 2 percent, compared to the 8 percent already paid by other businesses. See "Higher city taxes causing high anxiety," by Laura Vozzella, *The Baltimore Sun*, June 23, 2004.

⁵ Interview with Raquel Guillory, press office, Baltimore Mayor Martin O'Malley, June 28, 2004.

⁶ Accounts Summary, Assessing Department, City of Boston. The total of \$12.6 million excludes \$11 million in payments made by the Massachusetts Port Authority, or Massport, which manages area airports, the port and other facilities.

⁷ Some nonprofits do not choose to participate. Also, churches aren't asked to do so if their property is being used only for church purposes.

⁸ Interview with Richard Cohen, chairperson, board of review, June 29, 2004.

agreement.⁹ Boston's PILOT agreements also contain an escalator clause that increases the payments annually, using the U.S. Department of Commerce's Implicit Price Deflator for State and Local Government.

In Pennsylvania, a state Supreme Court decision in 1985 created a five-prong test to determine if an institution was a "purely public charity."¹⁰ As a 1994 report by a mayor's special committee in Philadelphia pointed out, this test "provided dozens of cities, counties, and school districts in Pennsylvania with the legal underpinning to challenge a nonprofit's tax-exempt status or to settle for PILOTs/SILOTs (services in lieu of taxes) for a portion of a nonprofit's potential tax liability."¹¹ By its own account, Philadelphia took a somewhat less confrontational approach than some other municipalities, though it still caused an uproar. The city's Voluntary Contribution Program brought in nearly \$8.8 million in 1996, and included more than 40 institutions, mostly hospitals, colleges and universities. They were acting like for-profit businesses, said David B. Glancey, chairman of the Philadelphia Board of Revision of Taxes, "doing everything you'd do, including compensating their staff, the way a big business does." Under the Philadelphia program at that time, most participating nonprofits contributed 33 percent of what they would have paid in property taxes were they not exempt; 33 percent of this amount could be paid in services. Certain nonprofits were given \$10,000 "hardship" exemptions.¹²

⁹ City of Boston, Payment in Lieu of Tax Program, Guidelines for Tax-Exempt Institutions, Fiscal Years 2004-2005, p.2.

¹⁰ Under the test, the institution had to: 1) advance a charitable purpose, 2) donate or render gratuitously a substantial portion of its services, 3) benefit a substantial and indefinite class of persons who are legitimate subjects of charity, 4) relieve the government of some of its burden, and 5) operate entirely free from the private profit motive. Cited in *Report of the Mayor's Special Committee on Payments-in-Lieu-of-Taxes (PILOTs) and Services-in-Lieu-of-Taxes (SILOTs)*, June 30, 1994, p. 4.

¹¹ *Ibid*, p. 4. The report described how various communities in the state had taken advantage of this decision, *Hospital Utilization Project v. Commonwealth of Pennsylvania (HUP)*. "The City of Pittsburgh and Allegheny County have been leaders in the use of an actual or potential legal challenge to a nonprofit organization's tax-exempt status to encourage a negotiated settlement for a PILOTs agreement. When Pittsburgh examined its nonprofit hospitals in light of the *HUP* decision, the City discovered that the majority of hospitals were providing less than two percent of their total annual revenues in charitable services. Pittsburgh challenged Presbyterian University Hospital's tax exemption for a newly acquired administration building. When Presbyterian responded by taking the case to Common Pleas Court, the City challenged the tax exemption of the entire institution, not just the offices. Presbyterian settled out of court for PILOTs of \$1.2 million per year for a ten-year period in exchange for Pittsburgh's dropping its challenge to the institution's tax-exempt status. Pittsburgh went on to invoice six other hospitals, including Allegheny General, St. Francis, Eye and Ear, Montefiore, the Central Blood Bank, and ShadySide Hospital."

¹² "PILOTs: Philadelphia and Pennsylvania," by David B. Glancey, in *Property-Tax Exemption for Charities*, Evelyn Brody, ed., The Urban Institute Press, Washington, D.C. 2002. The city calculated that about half of its General Fund expenditures were devoted to providing police and fire protection, criminal justice-related services, and Streets Department functions other than trash collection. After excluding most nonprofits from the program because they were clearly fulfilling their charitable missions, the city asked about 50 to make a monetary contribution of 40 percent of what they would have had to pay in property taxes to the city and school district if they did not have tax-exempt status. It reduced that to 33 percent for those that committed to the program early, as nearly all did. See also "Summary of Philadelphia's Voluntary Contribution Program for Nonprofit Organizations," June 1996.

The city treated the agreements as though they were litigation settlements, pledging not to challenge or revoke the tax exemptions. Early on, hospitals wanted to sign contracts for 10 or 15 years, Glancey says, but the city only agreed for up to five, something he now considers a mistake.

That's because a new state law and the Pennsylvania Supreme Court's interpretation of it later made it easier for nonprofits to qualify as public charities, reducing the bargaining clout of cities seeking PILOT payments. The program now includes just 22 institutions pledging annual cash payments of \$605,467.¹³ The University of Pennsylvania, which includes the Hospital of the University of Pennsylvania ranked 13th by *U.S. News*, had a PILOT agreement with the city, but it expired in 1999. Similarly, in Pittsburgh contributions peaked at roughly \$10 million a decade ago before falling to just \$620,000 in 2003.¹⁴

In Pittsburgh, a financial crisis has brought new life to the subject, and likely new contributions from nonprofits. Under a financial recovery plan put forward by a state financial oversight board, Pittsburgh sought \$6 million a year from the city's nonprofit universities, hospitals and other institutions to help fill its budget hole. In mid-November, officials from about 50 nonprofit groups including universities, hospitals, religious institutions and arts agencies agreed to help the city. They will set up a foundation through which to funnel the funds. The *Pittsburgh Post-Gazette* has reported that they are committed to \$6 million a year, though the amount in 2005 may be somewhat short of that because the effort began so late this year.¹⁵

Pittsburgh also decided earlier this year to file a challenge to the nonprofit status of an apartment building acquired by Duquesne University for \$22 million to use as student housing. City Council President Gene Ricciardi said in a newspaper account that the city could no longer shoulder the burden of so much exempt property.¹⁶ If it were fully taxed at the \$22 million value, the property would pay up to \$600,000 to the city, the schools and the county, according to Mayor Tom Murphy.¹⁷ A council resolution authorizing the challenge also called for examination of future property purchases by nonprofits, and Murphy argues that all nonprofits should pay something for city services.

Some institutions make payments for specific services. For instance, Duke University contributes \$300,000 a year to the city of Durham, N.C., for fire service. This amount

¹³ Interview with Mimi Choksi, divisional deputy city solicitor, City of Philadelphia Law Department, June 23, 2004, and City of Philadelphia Current PILOT Program Participants. This amount may change slightly due to sliding-scale payments by Wills Eye Hospital.

¹⁴ Interview with Craig Kwiecinski, spokesman for Mayor Tom Murphy, July 1, 2004, and "Nonprofits line up to aid city," by Timothy McNulty, *The Pittsburgh Post-Gazette*, Nov. 18, 2004.

¹⁵ See "Nonprofits line up to aid city," "Stepping Up—Pittsburgh nonprofits want to help the recovery," Editorial, *The Pittsburgh Post-Gazette*, Dec. 8, 2004.

¹⁶ "Cities increasingly challenge tax status of universities," Associated Press, *USA Today*, March 16, 2004. City officials have conservatively estimated that 35 percent of the property in Pittsburgh is held by non-taxpaying nonprofits, costing at least \$72 million a year to the city government.

¹⁷ "Mayor to duke it out with university," by Andrew Conte, *Pittsburgh Tribune-Review*, Nov. 24, 2004. Murphy testified at a hearing Nov. 23 on the challenge, which includes both a dispute over the value of the property and the city's claim that two-thirds of it should be taxable.

was roughly based on the formula used by the state to reimburse cities for fire protection of state-owned buildings, according to Durham Budget Director Julie Brenman. The city, which estimates it would receive about \$9 million a year in additional property taxes and \$6 million in sales tax if the university were not exempt, sought \$1 million a year from Duke in discussions earlier this year. After what the Durham *Herald-Sun* called “months of wrangling between town and gown,” the university agreed to make a voluntary one-time payment of another \$153,500 in fiscal 2004-05, mostly for police-related capital items.¹⁸ Stanford University, parent of Stanford Hospital & Clinics, also pays the city of Palo Alto, Calif., for fire and police dispatch services. In 2001-02, this amounted to \$5.2 million and \$586,000, respectively, and has probably grown by 3 to 4 percent a year since then.¹⁹

Hospitals besides those listed on the *U.S. News* Honor Roll also make PILOT payments. For instance, Dartmouth-Hitchcock Medical Center agreed in 2001 to make payments in lieu of taxes over 20 years to Lebanon, N.H. The medical center currently pays about \$1 million a year in lieu of taxes, according to City Assessor Normand Bernaiche.²⁰ Under the agreement, Dartmouth-Hitchcock increases its payments by 2½ percent a year. If it acquires additional property, it continues paying the amount of taxes that had been paid on that property, plus the 2½ percent. In addition, when it builds additional facilities, payments increase in proportion to the square-footage added (the inflation factor is added there, too). The agreement came after the city denied the medical center’s 1997 tax exemption applications for its Lebanon facility and billed it for taxes from 1997 through 2001. After the medical center appealed in court, the two sides agreed to settle the dispute.²¹ Dartmouth-Hitchcock employs 5,000 in a town of just 13,000, and would account for 20 percent of the town’s tax base were it fully taxable, according to Bernaiche.

Other institutions that *U.S. News* ranks high in certain specialties also make PILOT payments. For instance, these include the Dana-Farber Cancer Institute in Boston and the Fox-Chase Cancer Center in Philadelphia. These two are ranked 4 and 11 on the magazine’s cancer list, where University Hospitals is No. 17. Less well-known hospitals in other communities also make such payments, but are beyond the scope of this report.

In short, some of the top nonprofit hospitals in the country or their parent institutions make these payments. These include two of the three that *U.S. News* ranks above the

¹⁸ “Duke will give city additional \$153,500,” by Hunter Lewis, *The Durham Herald-Sun*, June 20, 2004. Duke also pays impact fees under a program that requires new development to pay part of the cost of streets, parks and open space. Based on an outside study, the city council last June reduced the amount the university had to pay in such one-time fees for building and expansion from \$1,403,061.88 to \$773,885.62.

¹⁹ Interviews with Joe Saccio, deputy director of administrative services, Palo Alto, California, June 22, 2004, and Nov. 29, 2004.

²⁰ Interview with Normand Bernaiche, Lebanon city assessor, July 2, 2004.

²¹ Interview with Bernaiche, and Agreement between the City of Lebanon and Mary Hitchcock Memorial Hospital, Dartmouth-Hitchcock Clinic, Dartmouth-Hitchcock Medical Center, and Trustees of Dartmouth College, January 24, 2002.

Cleveland Clinic, #1 Hopkins and #3 Massachusetts General.²² In all cases these are voluntary arrangements, though pressure may have been brought to bear on the institution.

Other PILOT payments

“PILOT payments are not restricted to non-profits,” attorney Janne G. Gallagher pointed out in a 1997 essay. “Larger governments sometimes pay them to smaller ones, as when a state or the federal government contributes to a local government that hosts a disproportionate amount of state or federal property. Some businesses granted temporary tax exemptions as an incentive to relocate also pay PILOTs to local governments.”²³ In Ohio, businesses that are granted property tax abatements sometimes pay PILOTs to school systems. The Cuyahoga Metropolitan Housing Authority paid \$10,910 to Cuyahoga County this year, as required by Ohio state law and regulations of the U.S. Department of Housing and Urban Development.²⁴

As indicated above, some PILOT agreements cover universities that may or may not have hospitals under their umbrella. Led by Harvard University, a number of the nation’s most elite private universities make PILOT payments. Harvard has been making payments to Cambridge, Mass., since the late 1920s. This year, Harvard and Massachusetts Institute of Technology are paying \$1,772,000 and \$1,223,000, respectively. Cambridge sends out in-lieu-of-tax notices to all nonprofits, asking for 19 cents per square foot of property. This rate was arrived at by dividing the entire land area of the city by the property taxes paid. Perhaps 20 organizations pay something, according to Kevin Mcdevitt, one of the city’s principal assessors.²⁵

Harvard also makes payments in neighboring communities where it has been expanding. After secretly buying 52 acres of land in Allston, in Boston across the river from the university’s main campus, Harvard in 1999 agreed to increase its PILOT to the city by \$12 million over 20 years for a total of \$40 million.²⁶

²² The Mayo Clinic, which had the #2 ranking, does not make payments in lieu of taxes. Mayo does not pay taxes on its hospitals in Rochester, Minn., or on facilities used for research or education. But it does pay taxes on its clinic buildings that contain outpatient facilities and offices, according to Dan Hall, director of property records and licensing for Olmsted County, Minn. In calendar 2004, Mayo Clinic is paying \$7.8 million in property taxes, or 5.7 percent of the total, making it the biggest single taxpayer in the county (these taxes are shared by the county, the city and the school district) Interview with Dan Hall, June 18, 2004. Hall estimated that something like 40 to 45 percent of the Mayo Clinic’s property is taxable, down from perhaps 75 percent years ago, when the hospitals were a separate entity.

²³ “When Local Governments Come Calling: The Movement to Tax Charities and its Implications for the Arts,” by Janne G. Gallagher, Caplin and Drysdale, Chartered. An essay prepared for Creative America, a report by the President’s Committee on the Arts and the Humanities describing the system of support for cultural life in the United States today. 1997. <http://pubs.artsusa.org/library/ARTS078/html/1.html#pagetop>

²⁴ Nov. 15, 2004, letter and Nov. 22, 2004, e-mail from Natoya J. Walker, deputy executive director, Cuyahoga Metropolitan Housing Authority; Ohio Revised Code, Sect. 3735.35; Chapter 8, Low-Rent Housing Accounting Handbook, U.S. Department of Housing & Urban Development.

²⁵ Interview with Kevin Mcdevitt, June 25, 2004

²⁶ “In Bid to Ease Town-Gown Tensions, Harvard Increases Its Payments to Boston,” by John L. Pulley, *The Chronicle of Higher Education*, Sept. 10, 1999.

More recently, when Harvard in 2001 bought a 30-acre property known as the Arsenal in Watertown, Mass., it sparked a negative reaction. “After \$100 million, mostly federal money, was spent cleaning up and renovating the Arsenal site, Watertown officials learned that Harvard had acquired it for \$162 million from the previous owner,” reported the *Boston Business Journal*. That could mean the property would go off the tax rolls, and Watertown has no other large undeveloped areas. “The community, which was counting on the Arsenal site to account for roughly one-third of its tax revenue and more than 10 percent of its total revenue once fully developed, was shocked.”²⁷

Harvard in 2002 agreed to make payments in lieu of taxes to the town of \$3.8 million a year, along with a 3 percent increase each year, through fiscal 2054. Under the agreement, Harvard will not have to seek rezoning to use the property for a range of academic purposes. Harvard President Lawrence H. Summers said he had adopted the following principle: “When Harvard is able to utilize newly acquired property to support its mission of education and research, resulting in the withdrawal of the property from the tax rolls, Harvard will make voluntary payments for a substantial interval and at a level that reflects the impact of the acquisition on tax collection.”²⁸

Last year, Brown University, Rhode Island School of Design, Providence College and Johnson & Wales University signed an agreement with the City of Providence to make almost \$50 million in payments over a 20-year period. The agreement calls for \$8.472 million in cash payments over four years beginning in July, 2003; voluntary contributions totaling \$1.73 million in fiscal 2003-2004 and increasing 1.5 percent a year for 20 years; and a schedule of payments for new properties the schools might acquire in the future.²⁹

Yale University pays New Haven more than \$2 million a year for fire service under an agreement dating back to 1990.³⁰ Other elite private schools such as Cornell and Princeton also pay PILOTs. Some others, however, have opposed them.

The states of Connecticut and Rhode Island reimburse municipalities for property taxes they do not receive because of nonprofit exemptions. Connecticut has nine separate reimbursement programs of this kind, including one that covers exempt real property of private colleges and hospitals. The amount paid by the state under this program fluctuates, as it depends on the appropriation process. According to testimony last spring

²⁷ “Harvard land deal puts area towns on the defensive,” by Bill Archambeault, *Boston Business Journal*, July 27, 2001.

²⁸ “Watertown, University announce agreement: Harvard to make annual payments to Watertown,” *Harvard University Gazette*, Sept. 26, 2002. See also “The Watertown Agreement,” John Harvard’s Journal, *Harvard Magazine*, March-April 2003.

²⁹ “Mayor Cicilline reaches an historic agreement with Providence colleges and universities,” press release from the City of Providence, June 5, 2003, and “New agreement nurtures and sustains Brown’s relationship with city,” Brown University News Service, June 7, 2003. The schedule calls for “five years at 100 percent of the property’s existing taxes at the time of purchase; five years at 66.67 percent and five years at 33.33 percent. These payments would be reduced to zero after 15 years and remain at zero for as long as the respective college or university owned the property.” Brown News Service.

³⁰ “Yale and New Haven Partnerships,” <http://www.yale.edu/ppsf/partnerships.html>

by the mayor of Norwalk, Alex Knopp, Connecticut's statutory standard for reimbursement to municipalities for tax-exempt property of private colleges and hospitals is 77 percent.³¹ The reimbursement rate for the current fiscal year is 60.6 percent. Policy Matters Ohio expects to examine state practices in this area in more detail later.

³¹ Testimony of Hon. Alex Knopp, Mayor of Norwalk, to the Appropriations Committee, March 17, 2004. See web site of the Connecticut Conference of Municipalities, <http://www.ccm-ct.org/advocacy/2004testimony/031704knopp.html>