Policy Matters Ohio

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MEMORANDUM

TO: James Rokakis, Cuyahoga County Treasurer
FROM: Zach Schiller, Research Director
RE: PILOTs – tax values
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 estimates the value of property-tax exemptions for the major hospital systems, and finds it to be substantial.

Policy Matters Ohio has used data from Cuyahoga County, including the treasurer and the auditor, among others, to calculate the size of property holdings of the county's two major private nonprofit hospital systems. This also allows a determination of the property taxes foregone because these institutions do not pay on most of their holdings.

Nonprofit, government and tax-abated property accounted for 15.6 percent of the overall value of real property in Cuyahoga County in tax year 2003.[1] Charitable institutions own $2 billion worth of real property in Cuyahoga County, or 13.9 percent of the total $14.4 billion in exempt property (this property owned by charitable institutions excludes that of churches and private educational institutions).[2]

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[1] In tax year 2002, the most recent year for which comparable data are available from the state, the 16.31 percent tax-exempt share of real property in Cuyahoga County outstripped that of all neighboring counties except Portage: Geauga, 6.32 percent; Lake, 8.08 percent; Lorain, 12.15 percent; Medina, 8.27 percent; Portage, 19.23 percent, and Summit, 11.97 percent. *2003 Annual Report*, Ohio Department of Taxation, page 138.

[2] The largest share of tax-exempt property is owned by government. Federal, state, county and local governments own $4.6 billion, school districts $1.8 billion, and park districts $577 million. Private schools and colleges accounted for $1 billion, churches and public worship, $1.1 billion, and other, $1.1 billion. Tax abatements amounted to $2.1 billion. Tax Year 2003. Abstract of Exempted Real Property, Cuyahoga County Auditor. Figures here as elsewhere in this report are market values for Tax Year 2003, unless otherwise indicated.

In Tax Year 2002, the most recent year for which data are easily available, Cuyahoga County had 13.2 percent of Ohio's taxable real property, and 21.4 percent of the exempt property owned by charitable institutions. While it had less taxable property than the total of six surrounding counties, Cuyahoga County had nearly twice as much exempt property owned by charitable institutions as the combined total of these counties.[3]

Tax-exempt property is especially concentrated in the City of Cleveland. In Tax Year 2003, exempt property of all kinds – that owned by governments and nonprofits, as well as tax-abated property owned by businesses – accounted for 36 percent of the real property in the city.[4] Charitable institutions own nearly $1.3 billion worth of real property in the city, or 16 percent of Cleveland's exempt property.

Both in the city and the county, the two nonprofit hospital systems, the Cleveland Clinic Health System and University Hospitals Health System, are the major owners of charitable-owned property. County-wide, they together account for at least $1.3 billion in such tax-exempt property, according to records supplied by the Cuyahoga County auditor and treasurer. This represents close to two-thirds of the tax-exempt charity holdings and 1.4 percent of all the real property, taxable and exempt, in Cuyahoga County. If these institutions paid taxes on all of their exempt real property in the county as it is now valued, local school districts and governments would receive more than $34 million a year in additional taxes.

These data are not comprehensive. For example, they exclude properties owned by UHHS partners such as St. John West Shore Hospital and Southwest General Health Center. Some other hospital properties also are not included in the data base.

On the other hand, these are the values as they appear on the books, and likely overstate the properties' real value. Unlike for-profit property holders, nonprofit institutions that do not pay taxes have no incentive to appeal the valuations given to their exempt properties, since they are not paying taxes. Though the county auditor's office disagrees, some informed observers believe that most such property is highly overvalued. Indeed, some hospitals valued on the books for many millions of dollars sold for a fraction of that after closing down. Thus, if all of these properties somehow began paying taxes, one could not expect they would add up to the full $34 million shown above.

Still, it is clear that tax-exempt properties in the county owned by the area's nonprofit hospital giants are worth many hundreds of millions of dollars, and would produce millions of dollars in additional taxes were they required to pay. Several Cleveland hospitals were operated by for-profit companies during the 1990s, which paid taxes and made efforts to try to reduce them by challenging their valuations. Their efforts provide some perspective on what nonprofit hospital properties may be worth.

[3] Policy Matters Ohio analysis of data from the Ohio Department of Taxation, Tax Data Series, Tables PE-1 and PE-2, March 2, 2004.
[4] Abstract of Exempted Real Property, Cuyahoga County Auditor, Taxing District 0740 – Cleveland.

After Mt. Sinai Hospital was purchased in 1996 by Primary Health Systems, a for-profit hospital chain, PHS sought to reduce the hospital's valuation by 35 percent.[5] By the time the complaint was resolved in 2001, Mt. Sinai was no longer operating and PHS was in bankruptcy. After for-profit operator Columbia/HCA took a stake in St. John West Shore Hospital, it asked to decrease the hospital's assessed valuation for tax year 1996 by nearly $5 million, or 46 percent, from $10.9 million.[6] The Cuyahoga County Board of Revision rejected that bid, maintaining the same valuation. Ultimately, in 2001, the state Board of Tax Appeals approved a stipulation lowering the value by 36 percent, to $7 million, although by that time, the for-profit company had sold its interest in the hospital.[7]

These examples confirm what is obvious to most county residents, or to anyone who has visited the main campuses of these institutions: As billion-dollar enterprises and the largest private employers in the Cleveland area,[8] their property has very substantial value, even if the amount now shown on the books may overstate their worth.

A ranking of the top 200 property holders by the Cuyahoga County auditor reveals that the CCHS is one of the top property holders in the county.[9] Though this ranking shows the Clinic system trailing utilities such as the Cleveland Electric Illuminating Co. and Ohio Bell (SBC), many Clinic properties are not included in this listing. The list includes properties held under the same name, but does not necessarily include all the properties held by each entity. Hence, an exact ranking is not easily available.

Together, CCHS and UHHS have nearly $1 billion in exempt property in the city of Cleveland, or most of their total exempt property in Cuyahoga County.[10] Among properties identified in this study, CCHS has exempt property in the city valued at $629

[5] Oral Hearing Worksheet and Journal Entry, Complaint # 2683 & 5235 for 1997, Cuyahoga County Board of Revision

[6] Information supplied by Robert Chambers, Cuyahoga County Board of Revision

[7] Ibid, and Ohio Board of Tax Appeals, Columbia CSA HS Greater Cleveland Area Health Care vs. Cuyahoga County Board of Revision and Cuyahoga County Auditor, Case No. 98-A-137, June 15, 2001.

[8] According to *Crain's Cleveland Business*, the Cleveland Clinic Health System and University Hospitals Health System are the two largest employers in Cuyahoga County, with 23,567 and 14,270 full-time equivalent employees, respectively. *Crain's Cleveland Business*, Dec. 29, 2003-Jan. 4, 2004. Figures are as of Jan. 1, 2003 (these differ from the numbers available from the American Hospital Association cited in the separate Policy Matters Ohio report on payments in lieu of taxes, which were used to compare hospitals around the country). The figure for UHHS includes the total number of physicians and employees. It does not include UHHS/CSAHS-Cuyahoga Inc., the No. 16 employer with 2,800 employees. The Cleveland Clinic Health System reported 2003 unrestricted revenues of $3.45 billion. While a portion of that comes from Florida and non-Cuyahoga County operations, the bulk of this revenue comes from Cuyahoga County; the Cleveland Clinic Foundation, based here, was responsible for three-fifths of the health system's revenue last year. See The Cleveland Clinic Health System, Management's Discussion and Analysis of Results of Operations and Financial Position for the Three Months and Year Ended December 31, 2003. UHHS reported total 2003 revenue of $1.6 billion in its return to the Internal Revenue Service. It, too, has operations outside Cuyahoga County.

[9] Top Taxpayers by Property, Received from Cuyahoga County Auditor's office, Nov. 8, 2004

[10] As noted, not all of the institutions' property is included in this study, so the exact proportion is not available.

million, while UHHS properties are valued at $331 million.[11] Altogether, this $960 million adds up to 4.3 percent of the total real property in the city.

If the Clinic system were taxed on these properties, it would pay $17.8 million in annual taxes to the city. Including those properties where it is seeking exemptions, the figure rises to $20 million. These numbers are based on the values shown by the auditor, unadjusted downward as described above. Even knocking 40 percent off these values, CCHS would pay an additional $12 million a year if it were fully taxed on its Cleveland properties. UHHS's exemptions in the city are worth $9.2 million in annual taxes, or $5.5 million after a 40 percent adjustment.[12]

Under Ohio law, nonprofit institutions must pay property tax on properties they own if it is not being used for a charitable purpose. Thus, both CCHS and UHHS pay taxes on some of their properties, such as the Intercontinental Hotel & MBNA Conference Center located on the Clinic campus. Data from the auditor show that the two institutions hold at least $436 million of currently taxable property in the county, which would produce annual taxes of more than $10 million.

However, these numbers considerably overstate the value of the properties that are actually paying taxes and the amount of taxes being paid. That's because the hospital systems are seeking to have much of that property exempted from taxation. They have applied to the state to exempt at least 39 properties worth $197 million, liable for about $4.4 million in annual taxes.[13] The Clinic accounts for the vast bulk of the exemptions currently being sought. For example, the Clinic has filed with the state for exemption of Fairview Hospital property valued at $43.6 million, where it has remodeled and added new facilities.[14] Similarly, after building its Taussig Cancer Center in Cleveland, the Clinic sought an exemption for the property.[15] The Clinic has sought exemptions for family health centers in Beachwood and elsewhere.[16] According to county records, UH is seeking exemptions for properties in Cleveland and Richmond Heights. It also filed last summer to expand its exemption at its Bedford Medical Center to cover an expanded

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[11].According to county records, the UHHS figure includes the W.O. Walker Center in Cleveland, which includes $46.6 million in exempt property. However, according to UHHS, the center is co-owned 50-50 by it and the Clinic. Thus, half of that value could be attributed to CCHS and subtracted from UHHS, changing the above figures accordingly.

[12] If, as noted in Footnote 11, one attributes half of the W.O. Walker Center property to the CCHS, half of the $1.2 million in taxes it would pay annually if it were fully taxed would be CCHS's responsibility. This would also reduce the UHHS total by $600,000.

[13] As with most valuation and tax information in this report, numbers reflect tax year 2003 data and exemptions sought by spring 2004. Some of these cases may be refiled because of a recent decision by the Ohio Supreme Court. See footnote 13.

[14] State of Ohio Application for Real Property Tax Exemption and Remission, Fairview Hospital, Received by county auditor June 26, 2002, County Application Number HE2781.

[15] State of Ohio Application for Real Property Tax Exemption and Remission, The Cleveland Clinic Foundation, Received by county auditor July 5, 2002, County Application Number HE3121

[16] A recent decision by the Ohio Supreme Court involving the Clinic's request for an exemption in Strongsville may require that a number of these exemption applications be refiled.

emergency department, related medical office space and new property purchased for parking expansion.[17]

As this illustrates, nonprofits must seek exemptions from the state when they put up new buildings on exempt property. However, they must wait a year after acquiring new property before they can file for an exemption on it.[18] Additional hospital properties now shown as taxable may yet become exempt.

The above data on real property exclude tangible personal property the hospitals may own such as machinery, equipment, inventories, furniture and fixtures, which also are exempt from taxation. A study by what is now the Center for Community Solutions estimated based on data from the Internal Revenue Service that county-wide, such property held by nonprofits (excluding churches and grant-making organizations) was valued at nearly $1 billion in 1999. It pegged the value of that tax exemption at $20.8 million that year, including $12.1 million in the City of Cleveland.[19]

Nonprofit institutions also receive other exemptions, such as the state law that relieves them of paying state and local sales tax on their purchases. The Ohio Department of Taxation has estimated that in fiscal year 2005, which began July 1, 2004, this exemption will reduce state revenue by $172.1 million.[20] Nonprofit organizations, along with others, also benefit from a sales tax exemption on building and construction material sold to contractors for use in real property constructed for them.

In summary, nonprofit institutions in general and CCHS and UHHS in particular benefit from substantial state and local tax exemptions.

[17] State of Ohio Application for Real Property Tax Exemption and Remission, University Hospitals Health System Inc., Received by county auditor July 7, 2004, County Application Number KE2447
[18] Taxpayers may retroactively seek exemptions going back three years.
[19] The Impact of Demographic, Technological and Federal Policy Changes on Ohio's State and Local Tax Structure, *Taxing Issues*, the Federation for Community Planning, December 2002. Note that this estimate includes a broader variety of nonprofits, such as colleges and universities.
[20] State of Ohio, Executive Budget, Fiscal Years 2004 and 2005, Book Two, Tax Expenditure Report. Prepared by the Ohio Department of Taxation, February 2003. p. 50.