

March 6, 2009

## Property Tax Exemption for Nonprofit Hospitals Proposed Revision of the Washington Administrative Code 458-16-260

The Department of Revenue is preparing to revise Washington Administrative Code 458-16-260 as it relates to the property tax exemption provided for nonprofit hospitals under RCW 84.36.040. This formal, public process will begin in a few weeks, and the Department seeks to notify all stakeholders that they will have an opportunity to participate in this process.

This notice is being sent to nonprofit organizations that currently benefit from the exemption, representatives of the hospital industry, county assessors, and individuals that have already expressed an interest in this topic. If you, as a recipient of this notice, are aware of an individual or an organization that should be notified of the rule-making process, we invite you to share this notice with them or contact Harold Smith at (360) 570-5864 or [HaroldS@dor.wa.gov](mailto:HaroldS@dor.wa.gov). They will be added to the list of stakeholders that will be notified of the public hearings to be held on this issue. They will be encouraged to offer their input during the review period and help to shape the final revision of WAC 458-16-260.

The revision will be made according to chapter 34.05 RCW, the Administrative Procedure Act. The process will be conducted by Alan Lynn, Rules Coordinator, Interpretations and Technical Advice Division, with the assistance of Jim Winterstein, Policy Counsel, Property Tax Division.

### Background

For more than 15 years, the property tax exemption for nonprofit hospitals has been granted only to those hospital facilities that are exclusively used for 24-hour inpatient care and certain medical facilities that are uniquely found in hospitals rather than clinics. This interpretation had been consistently upheld by the courts and the Washington State Board of Tax Appeals (BTA).

However, with extraordinary changes in the healthcare industry, hospitals have evolved from the traditional 24-hour care model into wide-ranging healthcare delivery systems. The hospital industry believes that the nonprofit exemption should be updated to reflect those changes and exempt more of the property they use to deliver today's hospital services. The Department acknowledged the changes in the industry, but has always held that only the Legislature has the authority to change the nature and extent of the exemption.

In August 2007, the BTA ruled in *Legacy Salmon Creek Hospital v. Department of Revenue* and then, in March 2008, the BTA issued its decision in *Franciscan Healthcare v. Department of Revenue*. The specific circumstances were different, but in both decisions the BTA found some property to be exempt, contrary to the Department's rule which limits the exemption to areas that are exclusively used for inpatient care. Specific areas used by outpatients in the two hospitals were found to be exempt.

The *Legacy* decision was appealed by the Department to Thurston County Superior Court. In June 2008, the court ruled that the outpatient facility at the center of the controversy in the *Legacy* case was, in fact, integrated into the hospital unit and found it to be exempt. The court appeared to conclude that the Department's inpatient/outpatient test was not the appropriate measure of whether property is integrated into the hospital unit and thereby eligible for property tax exemption.

### Proposed Interpretation

The Department has concluded that the rule must be revised to remove the conflict between WAC 458-16-260 and the court's decision with regard to the inpatient/outpatient test. That revision must still satisfy both RCW 84.36.040 and RCW 84.36.800. To the extent possible, the revision will be reconciled with both recent and historical decisions made by the BTA.

## Property Tax Special Notice

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To that end, the Department will propose a revised rule that no longer uses the 24-hour inpatient criteria to determine whether property qualifies for exemption. The revised rule will focus on whether property is licensed as a hospital under chapter 70.41 RCW, is integrated into the hospital unit, and exclusively serves patients of the hospital unit. If the revision is adopted, certain clinic or service areas in hospitals that were denied exemption in the past would qualify for exemption. All hospitals that might benefit from the new interpretation would be invited to apply to the Department's Property Tax Division to update their property tax exemption.

### Questions

If you have questions regarding a current exemption or the preparation for the rule-making process, please contact Harold Smith at (360) 570-5864 or [HaroldS@dor.wa.gov](mailto:HaroldS@dor.wa.gov).