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Legislative Council Special Committee on Tax Exemptions for Residential Property Hearing,
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Property Tax Treatment of Leased Residential Housing Subsequent to the *Columbus Park* Decision and 2003 Wisconsin Act 195

Description of Current Law and Historical Background

- 2003 Wisconsin Act 195 provides a property tax exemption for housing leased by a benevolent association. The Act reversed the Wisconsin Supreme Court decision, *Columbus Park Housing Corporation v. Kenosha* (2003 WI 143), that such housing was not exempt because it was not leased to persons or entities exempt from property tax, as required by statutes.
- Columbus Park Housing Corporation is a non-stock, non-profit corporation that buys residential property and rents it to qualified low-income persons and families. The City of Kenosha challenged the corporation's claim to an exemption for its property and the Supreme Court ruled in favor of the city. The decision was unexpected: property like that owned and leased by Columbus Park had long been considered exempt.
- Sec. 70.11 (4), Wis. Stats., exempts property owned and used exclusively by educational, religious and benevolent associations, as well as other specified organizations. Columbus Park Corporation, whose mission is to improve the living conditions of the poor and underprivileged in Kenosha by providing safe and affordable housing, is considered a benevolent association within the meaning of this subsection.
- Sec. 70.11 (4) specifically identifies nursing homes and retirement homes as benevolent associations. The Benevolent Retirement Home for the Aged Task Force, created by 1997 Wisconsin Act 27, addressed issues similar to those raised by *Columbus Park* when it investigated the property tax exemption for benevolent retirement homes. The group failed to reach agreement on recommendation: some on the task force supported the existing exemption, with a clearer definition of the term "benevolent," while others argued for additional standards relating to guaranteed care and the income levels of residents.
- A benevolent association qualifies for the exemption under sec. 70.11 (4) only when two conditions outlined in the introduction to sec. 70.11 are met, and the Court denied the exemption for Columbus Park on the basis of the one of these conditions. Under that condition, property leased by a non-profit entity to another person retains its exemption only if the lessee also can claim exemption from property tax. In *Columbus Park*, the court ruled that since the low-income families that rent from Columbus Park are not exempt from property tax, they do not satisfy this "lessee identity condition" and therefore the property was not exempt.

- Act 195 provided an exception to this condition for residential housing, and thus restored and potentially broadened the commonly held interpretation of the statutes that existed prior to the *Columbus Park* decision: housing owned by an entity that can be considered "benevolent" is exempt from tax.
- The second condition requires the lessor to use all income from the property for maintenance or debt retirement. Under widely used definitions, "maintenance" refers specifically to expenditures that maintain the condition or value of a property. It is just one component of operating expenses, a larger category that includes such expenses as management charges, heat, decorating and cleaning.
- Kenosha and Columbus Park currently are disputing the meanings of "maintenance" and "debt retirement", and other issues in circuit court. The corporation contends that maintenance includes depreciation, out-of-state travel, salaries and utilities, and that debt retirement include payment against a line of credit since the corporation has no mortgage. Finally, Columbus Park is arguing that assessors should not consider the rent subsidy for low-income families under Section 8 of the Federal Housing Act as part of the corporation's income.
- The *Columbus Park* decision and Act 195 raised the issue of what types of housing leased by non-profit entities should be exempt from the property tax. That would require an explicit definition of "benevolent association" that indicates the activities such an association must perform to be considered benevolent when it rents housing. The Benevolent Retirement Home for the Aged Task Force considered components of such a definition, among which were the following:
 - Defining "benevolent association" utilizing language from Section 501 (c)(3) of the Internal Revenue Code (IRC), which provides a federal income tax exemption for nonprofit organizations.
 - Exempting facilities that provide certain kinds of services, such as assisted living, community-based residential and skilled nursing facilities.
 - Establishing an income standard or other means test.
 - Requiring guaranteed care regardless of ability to pay for retirement communities that provide independent living, assisted living and nursing care facilities.

Fairness/Tax Equity

- The rationale for a property tax exemption for housing leased by benevolent associations is that these associations perform the socially desirable function of providing affordable housing to needy individuals.
- However, not all the rental housing that is exempt from the property tax is rented to persons in need. For example, some elderly persons live in high-rent housing units with market rents that are owned by entities that meet the statutory definition of "benevolent association", and thus are exempt from the property tax. It is not clear that these associations are performing the socially desirable function for which the exemption is intended.

- Another argument for narrowly targeting the exemption is that taxes that the exemptions shifts to other taxpayers the taxes that otherwise would fall on the exempt property and its owners or lessees. Some of the persons paying higher taxes as a result include low-income homeowners and renters who live in housing subject to the tax.
- The state, through its Homestead Tax Credit, provides property tax relief to low-income renters and owners who live in property subject to tax. Renters living in property owned by a municipal housing authority that makes payments in lieu of property tax to the municipality in which the property is located also may claim the Homestead Credit.
- The credit equals up to 80% of property taxes, or rent constituting property taxes (20% of rent if heat is included in rent, and 25% of rent if rent does not include heat), up to \$1,450 when household income does not \$8,000. The credit is phased out as household income rises from \$8,000 to \$24,500. Thus, the credit relieves only a portion of property taxes, not the full amount, as is the case with an exemption. In FY04, about 238,000 households received Homestead Credits totalling \$119.8 million.
- Benevolent associations owning housing that is exempt from property tax may be in competition with entities providing to similar populations housing that is subject to tax. Their competitors may argue that the benevolent associations have an unfair advantage.

Impact on Economic Development

- Narrowing the property tax exemption for housing provided by benevolent associations may impact on the provision of such housing. In particular, developers may argue that the property tax exemption is essential to the economic viability of such low-income and elderly housing projects.

Administrative Impact/Fiscal Effect

- Definitions in the federal Internal Revenue Code and Fair Housing Act may be useful in defining "benevolent association" for purposes of the property tax exemption for leased housing. However, the state can maintain greater control over determining who qualifies for the exemption by defining that term explicitly rather than by reference to federal law.
- Clear definitions of the types of associations and activities that qualify for the property tax exemption will limit efforts to avoid property tax by establishing non-profit organizations whose sole purpose is to obtain the benefit of the tax exemption.
- Only limited data are available on the value of exempt housing in the state. Exemption summary reports filed in 2002 by owners of exempt housing with municipalities and submitted to the Department of Revenue, the total value of exempt housing (excluding nursing, retirement, and religious housing) is estimated to be about \$862 million. The portion of this amount affected by the *Columbus Park* decision and Act 195 is not known. If the entire amount was affected by the court decision and the act, about \$17.7 million in property taxes were made taxable by the decision, and the exemption provided by Act 195 shifted this amount of tax to other property taxpayers.

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