Presentation to Special Committee on Tax Exemptions for Residential Property

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It is an honor to be here today and to speak with you about an issue of major importance. That issue, as I see it, is how our state will best provide residential facilities for and care of its elderly and physically and mentally challenged citizens.

While this special committee is charged with looking into the issue of property tax exemptions, the outcome of your deliberations and your recommendations will in fact shape the amount, type and cost of living and care services available to our state's most vulnerable populations and who will be providing those services. This issue is not a partisan issue. It is an issue which affects thousands of our state's elderly and disabled citizens.

I have been asked to speak about WHEFA's role in supporting our state's tax-exempt provider infrastructure for these populations through our facilitation and expediting of bonding for projects which will be directly affected by your decisions.

I would like to offer comment on WHEFA operations, the tax-exempt organizations we work with and some thoughts which may assist in your future discussions.

WHEFA Background

WHEFA has been providing active capital financing assistance to tax-exempt organizations throughout the state since 1979. With original emphasis on working with health care providers (hospitals, nursing homes and CBRFs) the portfolio of financing assistance has grown so that today our state's private colleges, private K-12 schools and community providers of services to disabled populations all have access to our assistance and services.

When thinking about WHEFA and its services, keep the following facts in mind.

- WHEFA services its constituents and this state with a staff of 4 persons and a budget of less then $675,000.
- WHEFA receives no state funds for its operations, which are instead entirely funded by user fees.
- Bonds issued by WHEFA are payable solely from payments received from the borrowing institutions. They are not a debt, liability or "moral" obligation of the state.

- The availability of financing and its terms depend in each case upon the credit worthiness of the borrowing institution.

- Interest on bonds issued by WHEFA is exempt from federal taxation, but is subject to state taxation.

- All WHEFA borrowers are tax-exempt, 501(c)(3) organizations.

WHEFA Activity

This year marks the completion of WHEFA's 25th year of bonding activity. In that time, over $9 billion in bonding has occurred (1/3 of which represents refinancing existing debt for savings and 2/3 of which is the permanent financing of new capital projects). A little more then $6 billion remains outstanding today.

75% of this activity is for acute health care providers, 6% for education and 19% for long term health care and community providers. While I am not sure of this committee's ultimate scope of review, i.e. will hospitals, nursing homes and educational facilities ultimately be included in these discussions, I am for this moment assuming it is the long term care segment and particularly those providers which offer levels of care below skilled nursing which are of most interest.

Thus it is a small portion of our portfolio and financing activity which is currently in jeopardy. In fact, most of the financings we do in long-term care are of a mixed purpose, with bonding done to create a campus setting and a continuum of care from independent living (with health care and personal care services available) all the way to a skilled nursing facility. In WHEFA's loan portfolio there are 23 providers who have WHEFA debt totaling $330 million outstanding which could be immediately impacted by your findings.

As previously stated, WHEFA works exclusively with tax-exempt organizations who, only after application, and through review by the Internal Revenue Service, have obtained a 501(c)(3) status.

My experience shows that obtaining this exemption is rigorous and that the benevolent purpose of the applicant must be well documented. There is recently an expanded IRS enforcement program which audits and insures that the charitable purposes outlined in original applications are being met on an ongoing basis. 501(c)(3)'s become a part of our societal safety net, providing programs and services which would otherwise fall to government to provide. Any diminution of their effectiveness or ability to operate will require the employment of increased government resources and efforts.

Impact of Change in Property Tax Exemption Status

Tax-exempt, long term care providers are a fragile sector of our state's health care service network for elderly and disabled citizens. This is the only sector of our bond portfolio in which payment defaults have occurred. Faced with reimbursement limitations and shortfalls, rising costs of operations, labor shortages and tort liability, only to name a few issues, the balancing act of continued operation is often tenuous.

Consider the following partial list of potential risks listed in a recent bond disclosure document for a WHEFA long-term care borrower.

- Payment for Services
    - Third-party payment programs
    - Medicare
    - Medicaid
- Competition
- Regulation of Health Care Industry
    - State laws
    - Balance Budget Act of 1997
    - Taxpayer Relief Act of 1997
    - HIPAA
    - Federal "Fraud and Abuse" laws
    - Restrictions on referrals
    - Compliance / OIG investigations
    - Licensure
    - Environmental laws and regulations
- Failure to achieve or maintain occupancy
- Antitrust
- Increased competition
- Risks related to tax-exempt status
- Nursing shortage
- Limited alternative uses of facilities
- Cost and availability of insurance
- +14 miscellaneous risk factors (including new adverse legislation, increased costs of operation, and exemption from property tax).

To operate successfully and over time in this industry and environment requires good business skills, a respected product and service, and some luck. Would the imposition of property taxes alone cause massive bond defaults in the WHEFA portfolio and the closure of several facilities? My answer is no. However, not all the business risks just outlined will fall in favor of this industry. As these and other negatives to continued operations become a reality, their combination with tax payments will become unbearable to several providers.

If the ultimate outcome of this process is the full property taxation of residential projects, I would offer the following observations. WHEFA borrowers will immediately be forced to re-price their services. Residents will be forced to spend down their assets more quickly. Borrowers will also look to reposition themselves either looking to serve less of a lower income population, or changing the mix of units and services offered. This will leave a previously served market sector that will need to be served in some instances by an increase in government operated programs. And finally our borrowers will retrench (either downsizing current operations or shelving plans for future growth). The bottom line result will be fewer services for our elderly and disabled populations at a time when demographics show an increasing need. Those resulting unmet needs will thus fall in some major way to government.

As I have worked these past 20 years on bond issues I have visited many of these facilities. I have looked in the eyes of the persons being served. I have heard their voices. These men and women, who for years served their country, and their community, must be our first priority in these deliberations. Outcomes which jeopardize meeting their needs are, I believe, unacceptable.

How Can WHEFA Help?

Today may be the only time this committee asks for WHEFA's assistance and involvement. I truly hope it is not. While limited in our staff resources, we are strong in our connections to the private capital markets and others who serve this industry.

As this subcommittee develops alternatives and structures to address the issue of property tax exemption, we offer our assistance as a facilitator or reviewer, so that the impact of proposals can be measured and quantified prior to their adoption as a recommended solution.

Final Thoughts from WHEFA

I do not envy the task you have been given. This is an issue which has been left unresolved for years, and now because of differences between judicial findings and legislation, it falls to you to find the remedy. I do however feel that an answer lies out there, waiting to be discovered. An answer that maintains the integrity of the current system for providing these most needed services.

As you proceed in the following months, I encourage you to first diverge your thinking, to think creatively about who is affected, how differing interests may be best addressed, how similar situations here or in other venues or industries have been resolved and what longer list of options may be available. Then as you converge on a possible solution, consider looking to WHEFA and others, including lenders and financial feasibility consultants, to help verify that the outcome will be the best possible for all the citizens of Wisconsin.