

NONPROFIT NURSING HOMES - SUMMARY

Current Law

Under current law, all real and personal property of nonprofit nursing homes is exempt from property taxes. The main requirement for this tax exemption is that the property be used exclusively for the purposes of the nursing homes and that the benefits of the exemption must be retained by the nonprofit organization. In Appendix 3 is the current law statute, RCW 84.36.040(1)(d), which provides for the property tax exemption.

Findings and Recommendations

This review of Washington's nonprofit nursing homes' property tax exemption has evaluated the legal history, public policy objectives, economic and revenue impacts and other states' similar tax preferences. The following were determined through this audit:

Legal History and Public Policy Objectives

- The property tax exemption for nursing homes dates back to an 1854 section exempting “benevolent, charitable, literary, or scientific” institutions, various government properties, schools, cemeteries, and public libraries from the tax base. As it was initially written, this tax preference is a definition of the tax base.
- The law in 1895 placed a requirement on homes for the aged and infirm that they must be supported in whole by public appropriation or by private charity, or all of the income and profits are devoted to charitable purposes. This indicates an historic public policy objective that nursing facilities had to be performing charitable services to communities.
- The original property tax exemption applied to all nursing homes that met the charity conditions. In 1973, the Legislature narrowed the exemption to nonprofit nursing homes only. The 1973 legislation did not include a clear statement of the Legislature's intent in making this change.
- The 1973 legislation created a direct connection between qualifying for this tax preference and meeting the federal requirements for nonprofit organizations in order to receive the “nonprofit” designation. There are various federal requirements for nonprofit organizations, which restricts their distribution of income and includes a requirement to provide community benefits.
- In 1984, the Legislature created a public policy objective that this property tax exemption is only allowed for the property of a nursing home that is used exclusively for the operating a nursing home.

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- A public policy objective of the property tax exemption for nonprofit nursing homes is to support quasi-public service activities performed for the aged and infirm. This tax preference has achieved its public policy objective of providing property tax relief to nonprofit nursing homes.
- It is not clear how well nonprofit nursing homes have performed charitable services and community benefits as compared to the performance of private for-profit nursing homes.

Beneficiaries

- The beneficiaries from this property tax exemption are 42 nonprofit nursing homes and 87 parcels of property statewide that received an exemption in property tax year 2006-07.
- There is no indication of this tax preference providing unintended benefits to other entities besides nonprofit nursing homes.

Economic and Revenue Impacts

- In property tax year 2006-07, the nonprofit nursing homes had an annual property tax savings of approximately \$2.8 million.
- The future property tax savings for nonprofit nursing homes over the next three years is between \$2.9 and \$3.0 million per year.
- Washington's nursing home industry in the first three quarters of 2006 had on average 190 firms and 24,998 employees and \$507 million in total wages.

Other States

- Twenty-three states, including Washington, have a specific property tax exemption for property used as homes for the sick or infirm. Most all states have property tax exemptions for nonprofit organizations when the property is used for charitable use so nursing homes may or may not fall into that charitable use category in those states.

Due to the fact that this tax preference was originally enacted to exclude all nursing homes from the property tax base and the beneficiaries of the tax preference are nursing homes, this tax preference has achieved that public policy objective of defining the tax base. It is less clear what the Legislature's additional intentions were in restricting this tax preference to nonprofits nursing homes beginning in 1973. The Legislature connected to the federal requirements of nonprofits in order to qualify for this tax preference but it is unclear what the expectations were for nonprofit organizations. The federal law has a "community benefit standard" to determine if health care organizations qualify as tax-exempt nonprofits. The "community benefits standard" does not specify a certain amount of care that must be provided to low income residents to qualify for tax-exempt status, even though it is a component of community benefit. In addition, there are limitations in federal law on the distribution of profits and assets of nonprofit

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organizations but it is unclear what characteristics the Legislature intended nonprofit nursing homes to possess.

In terms of meeting the charitable service requirements of nonprofits, JLARC's analysis shows that private for-profit nursing homes (that do not receive a property tax exemption) have traditionally had a higher percentage of total revenue from low-income Medicaid patients. In addition, the nonprofit nursing homes are charging private pay patients more than other private nursing homes that do not receive the tax exemption. Overall, the data do not support the premise that the nonprofit nursing homes are serving more low-income patients than other nursing homes. Information is not available that would allow for a comparison among all nursing homes of other community benefits that nursing homes may provide. So it is not clear that the current tax preference is accomplishing a public policy objective related to provision of additional charitable services or community benefits, as compared to other types of nursing home ownerships.

There is now different property tax treatment among homes for the sick and infirm and the aged. Other non-nursing home long-term care facilities must prove that a majority of their residents are low income residents or else their property tax exemption is prorated. In addition, nonprofit nonsectarian organizations have to meet a gift giving test that demonstrates that the nonprofit is performing charitable services to the local community it serves which is not required of nonprofit nursing homes. These issues raise questions about whether the tax preference is currently consistent with the charity care policy objective.

Recommendation 1

If the Legislature intended to provide the nonprofit nursing home property tax exemption under the assumption that these organizations were providing more charity or low-income care than other nursing homes, then the Legislature should modify the property tax exemption to be dependent on meeting a threshold of charity or low income care.

Legislation Required: Yes

Fiscal Impact: A change in revenue could be possible depending on how this is implemented.

Recommendation 2

If the Legislature wants information on community service activities performed by nursing homes, then it should require nursing homes to report an annual community service inventory.

Legislation Required: Yes

Fiscal Impact: None

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Statutory History

The property tax exemption for nursing homes dates back to an 1854 section exempting “benevolent, charitable, literary, or scientific” institutions, various government properties, schools, cemeteries, and public libraries from the tax base. The specific tax exemption for nursing homes was initially an 1891 section stating that “homes for the aged and infirm” were not to be part of the tax base.

All property in this section shall be exempt from taxation:

all free..., hospitals..., homes for the aged and infirm;

In 1893, the law restricted the size of the exempt parcel of the land to 120 feet by 200 feet. In 1895, the law placed a requirement on homes for the aged that they must be supported in whole by public appropriation or by private charity or supported in part by charity and all of the income and profits devoted to charitable purposes.

In addition to this specific requirement related to charitable purposes, the Legislature also added record-keeping requirements, which it then adjusted in the ensuing years. In order to qualify for the property tax exemption in 1895, the state Board of Health, county, and city officials had to have access to the financial records of the institutions, and the manager of the home had to swear before the county assessor that all income had been applied to actual expenses of maintaining the home and to charitable purposes. The homes for the aged and infirm had to annually file a report to the state Board of Health describing the source of its receipts and the expenses that were paid. The law required that the homes for the aged and infirm allow the mayor of the city and the chairman of the board of the county commissioners, where the institution was located, to be on its board of trustees.

In 1925, the law was changed to allow homes for the aged to rent or lease property for use in their institutions, and all the property used would qualify for the property tax exemption. In 1933, the Legislature removed the requirement that the mayor and chairman of the county commissioners needed to serve on its board. In addition, the law required that just the state Board of Health, not the city and county officers, had access to the nursing homes’ financial records.

In 1969, the reporting and auditing requirement for the nonprofit homes for the aged and infirm changed from the state Department of Health to the Department of Revenue. The law deleted the requirement that the manager of the home for the aged take oath before the assessor and instead

required the homes for the aged manager to sign a statement that the income and receipts have been applied to the actual expenses of maintaining the institution.

The Legislature made major changes in 1973 to the statutes regarding the property tax exemption for the homes for aged and infirm. The Legislature narrowed the exemption from all homes for the aged and infirm to only nonprofit homes. The Legislature also defined “nonprofit” in statute to mean that no part of income could be paid directly or indirectly to members, directors, stockholders, officers, or trustees except for services rendered. The revised property tax exemption was dependent on the property being used exclusively for the purposes of the nonprofit organizations, and the benefits of the exemption had to accrue to the nonprofit organization. All of the annual report filing requirements for homes for the aged and infirm were deleted.

In 1984, the Legislature specified that all property must be used exclusively for the purposes for which the exemption is granted, which are exclusively homes for the aged and infirm purposes.

In 1989, the Legislature passed HB 1097 which created a separate property tax exemption for the homes for the aged distinct from the nonprofit nursing homes’ property tax exemption. The property tax exemption for the homes for the aged was modified by requiring the nonprofit homes to have at least 50 percent of the dwelling units be occupied by eligible residents in order to receive a complete property tax exemption or the home must be subsidized by HUD. The eligibility guidelines for residents are based on the resident’s annual household income and if the entire home fails to qualify, then the exemption for real property is prorated based on the number of eligible residents. The homes for the aged property tax preference will be reviewed in future years by JLARC.

Federal Requirements for Nonprofits

The state Legislature’s change in 1973 to narrow the tax exemption to nonprofit homes for the aged and infirm created a direct connection between qualifying for this tax preference and meeting the federal requirements for organizations to receive the “nonprofit” designation. According to federal law, the promotion of health for the benefit of the community is a charitable purpose. A nursing home may qualify for tax-exempt status under IRC 501(c)(3) provided it is organized and operated exclusively for charitable purposes. There are various federal requirements for nonprofits including organizational tests and meeting a “community benefits” standard.

Organizational Test

The organizational test is the same for health care organizations as it is for any other IRC 501(c)(3) organizations.¹² The health care organization must be operated exclusively for charitable purposes and upon dissolution the nonprofit entity must distribute its assets exclusively for charitable purposes. Another requirement for nonprofit organizations is that the

¹² “Health Care Provider Reference Guide,” IRS by Janet Gitterman and Marvin Friedlander.

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organization must have only a small part of its activities which is not furthering its charitable health purpose. The federal law also stipulates that no part of an organization's net earnings can be distributed in whole or part to benefit private shareholders or individuals. Essentially, a nonprofit may not lawfully pay its profits to owners or to anyone associated with the organization. These requirements are also in Washington State law.¹³ Along with these tests, there are also restrictions placed on lobbying efforts and political activities to influence legislation.

Community Benefits

Federal policy requires health care organizations to provide community benefits in order to qualify as tax exempt nonprofit entities. The standard adopted in 1969 and still in place today does not require health care organizations to provide a specific level of care to the poor in order to qualify for tax exemption.¹⁴ Instead, health care organizations must demonstrate that they provide sufficient benefits to the community.¹⁵ Other factors that demonstrate that the health care organization is operating for the benefit of the public may also be considered. Washington State does not require health care organizations to identify and inventory their community benefits but the Washington State Hospital Association (WSHA) has conducted surveys of 32 of their nonprofit hospitals to completed Community Benefits Inventory Reports on Washington Hospitals. This audit did not find a similar type community benefits inventory report documenting the community services provided by Washington's nonprofit nursing home facilities.

Washington Nursing Homes

Providing care to the aged and infirm has had a long history in Washington. The first hospital, St. Joseph Hospital, opened in 1858 at Fort Vancouver and provided a variety of health care services to pioneers, including long-term care for the aged and infirm.¹⁶ By 1866, the Sisters had a contract with the Territory of Washington to provide care of the mentally ill and infirm at \$8 a week per person.¹⁷ Some of the earlier nursing homes were connected with a hospital. In examining a few nursing homes' individual histories in Washington, it was found that the Sisters of Providence nursing home claimed to have been in existence the longest at 150 years. Bethany of the Northwest is also one of the oldest nonprofit nursing facilities that is still in operation as they have been in operation for 70 years.

More than 100 years later in 2005, according to DSHS data, there were 204 nursing facilities operating in the state. Forty-two homes or 22 percent of all nursing homes were managed by nonprofit corporations. Eighteen percent were owned by municipalities, and the remaining 60

¹³ RCW 24.03.

¹⁴ IRS Ruling 69-545.

¹⁵ "A Review of the Tax-Exempt Hospital Sector," written statement of Mark Everson Commissioner of Internal Revenue Before the Committee on Ways and Means United States House of Representatives May 26, 2005.

¹⁶ A Century of Service 1858-1958 Washington Hospitals, Washington State Hospital Association, 1957.

¹⁷ A Century of Service 1858-1958 Washington Hospitals, Washington State Hospital Association, 1957.

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percent were private for-profit companies. In 2005, with more than 60 percent of the Washington nursing home facilities owned by for-profit companies, these nursing facilities had on average larger nursing facilities (96 beds per facility) than the nonprofit nursing homes (86 beds per facility).

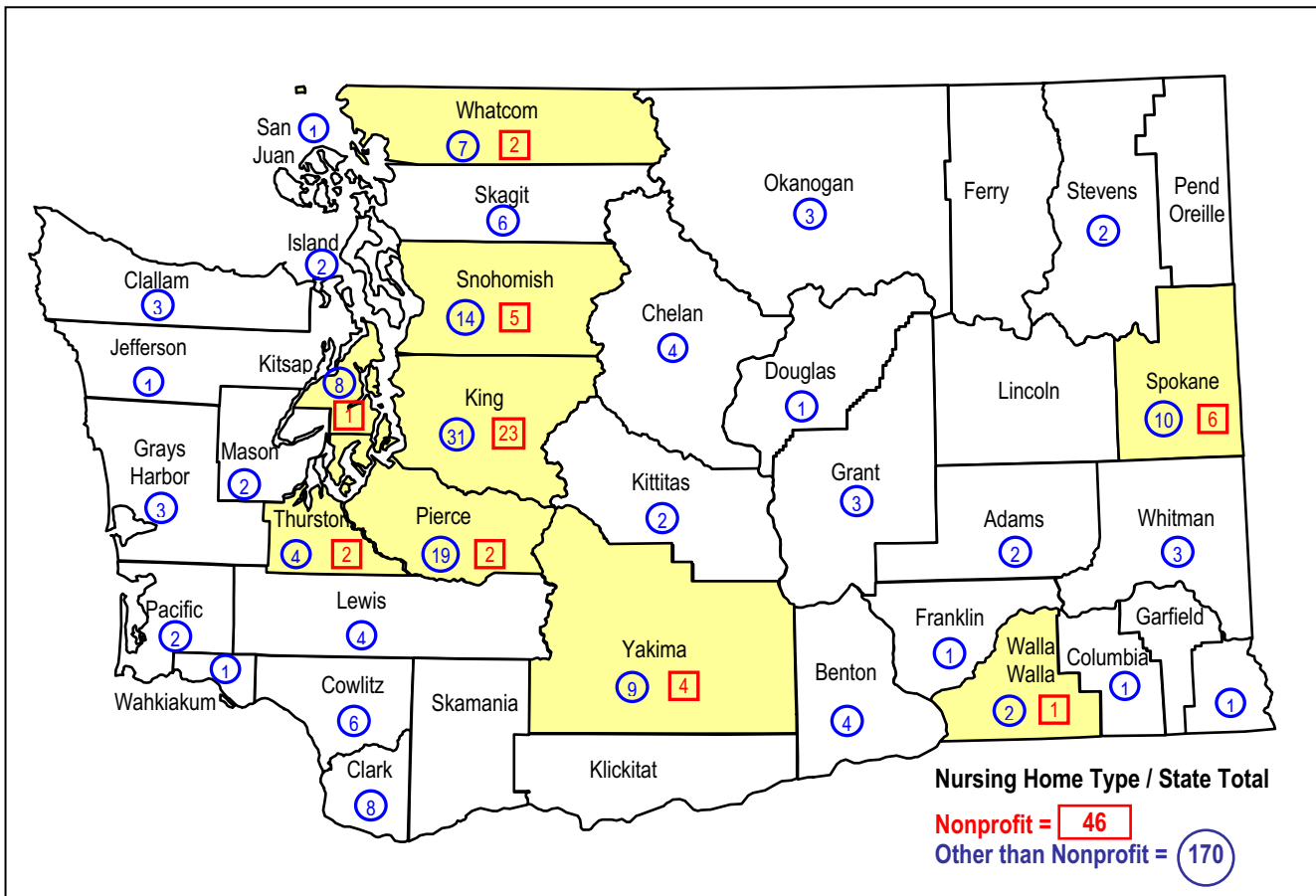
Nationwide for-profit companies have dominated the nursing home market as is also true in Washington. According to nationwide studies, on average in the early 1990s, for-profit nursing homes had 70 percent of all nursing facilities in the U.S. In the early 2000s, for-profit businesses owned 66 percent of all nursing homes.¹⁸

Washington nursing homes are located all throughout the state with the majority of the nonprofit nursing homes being in more urban counties like King, Snohomish, Spokane, Pierce and Thurston, see Figure 1. There are eight nonprofit nursing homes in rural counties like Whatcom, Walla Walla, Kitsap and Yakima.

Figure 1: Number of Nursing Homes in Washington by Type of Ownership - 2005

¹⁸ How Nonprofits Matter In American Medicine, And What To Do About It, Mark Schlesinger and Bradford Gray, Health Affairs 25 (2006).

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Public Policy Objectives

What are the public policy objectives that provide a justification for the tax preference? Is there any documentation on the purpose or intent of the tax preference?

The statutory history for this tax preference indicates several public policy objectives for this tax preference. The first objective is one of defining the property tax base since this tax preference was enacted at the time of statehood and is consistent with the general history of the U.S. and with exemptions for charitable institutions dating back to colonial days under British law. Since long-term care services for the aged and infirm were originally provided by hospitals, the public policy objectives for nursing homes are similar to hospitals. There has been a traditional public policy objective of exempting homes for the aged and infirm from the property tax base under one or more of the benevolent, charitable, or scientific institution categories. In an 1866 case, the U.S. Supreme Court recognized this long-standing exemption of hospitals from taxes:

It is known as sound policy that, in every well regulated and enlightened state or government, certain descriptions of property, and also certain institutions—such as

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churches, hospitals, academies, cemeteries, and the like—are exempt from taxation; but these exemptions have never been regarded as disturbing the rates of taxation, even where the fundamental law had ordained that it should be uniform.¹⁹

The specific exemption for “homes for the aged and infirm” appeared immediately following statehood, in 1891 and remained that way until 1973.

A second public policy objective for homes for the aged and infirm relates to homes’ work for charitable purposes and community benefits. In 1895, the Legislature placed a requirement on homes for the aged that they must be supported in whole by public appropriation or by private charity or are supported in part by charity and all of the income and profits are devoted to charitable purposes. This indicates a historic public policy objective for this tax preference that the nursing facilities had to be performing charitable services to communities. While this provision is no longer in place, in 1973, the Legislature narrowed the use of the tax exemption from all homes for the aged to nonprofit homes only. As discussed earlier, there are federal requirements related to charitable purposes and community benefits that the nonprofit nursing homes must meet in order to receive their official designation as a nonprofit organization.

Another public policy objective of the property tax exemption for nursing homes is that these organizations are being excluded from the taxable base as quasi-public properties. A Washington Supreme Court case in 1897 justified exemptions from the property tax base as properties that provide a benefit to the public and relieve the state of expense.²⁰ The property tax exemption for nursing homes is based on the service activities performed for the aged and infirm; if those services were not provided then the state would have to be performing those services.

¹⁹ People v. Commissioners, 71 U.S. 244, 256 (1866).

²⁰ Chamberlin v. Daniel, 17 Wash. 111, 113 (1897).

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For 78 years, from 1895 until 1973, all for-profit and nonprofit nursing homes and homes for the aged had annual reporting requirements in which they had to provide information on their revenue sources and expenditures. A fourth public policy objective for this property tax exemption was that this property tax exemption be limited to nonprofit nursing homes due to the profit and asset restrictions placed on these organizations so the net earnings will be used for charitable purposes. From the beginning of this tax preference, there was a public policy objective that these quasi-public institutions should be accountable for the sources of their revenue as well as their expenses. It appears that the Legislature assumed in 1973 that in restricting the property tax exemption to nonprofits, it would be meeting those requirements by connecting to the federal definition and requirements of charitable health care organizations. There was not a clear statement of any further change in public policy objective in the Legislature's narrowing of the exemption to nonprofit homes only.

A fifth public policy objective of this property tax exemption for nursing homes was that the exempt property had to be used exclusively for nursing home purposes. The property tax exemption does not apply to all property owned or used by nonprofit nursing homes but only that property which is used exclusively for nursing home purposes.

Is there any readily available evidence related to the achievement of any of these public policy objectives (in the past, present or future)?

After examining the Department of Revenue's property tax exemption database, the entities claiming this property tax exemption are nonprofit nursing homes. This tax preference has achieved the objective of defining the property tax base. Since there is a public policy objective for this tax preference that the exempt nursing home property be used exclusively for nursing home purposes and this audit did not uncover substantial evidence that this tax preference for property used for nursing home services were not implemented fairly uniform across homes throughout the state, this tax preference appears to have achieved this objective.

To assess whether the tax preference has achieved the second public policy objective of providing charitable services to low income residents, JLARC staff analyzed the available information on Washington nursing home data by different ownership types for Medicaid patients. Serving Medicaid patients is one way in which nursing homes serve their local communities. Medicaid is available for those individuals who cannot afford care. The Medicaid reimbursement rate in the state becomes a critical factor in nursing homes' financial picture. In Washington, Medicaid rates for long term care nursing facilities are set individually for each facility. It is a cost based rate system based on a facility's costs, its occupancy level, and the individual care needs of its residents. There are seven main cost components in the Medicaid rate: direct care, therapy care, support services, operations, variable return, property and financing allowance.

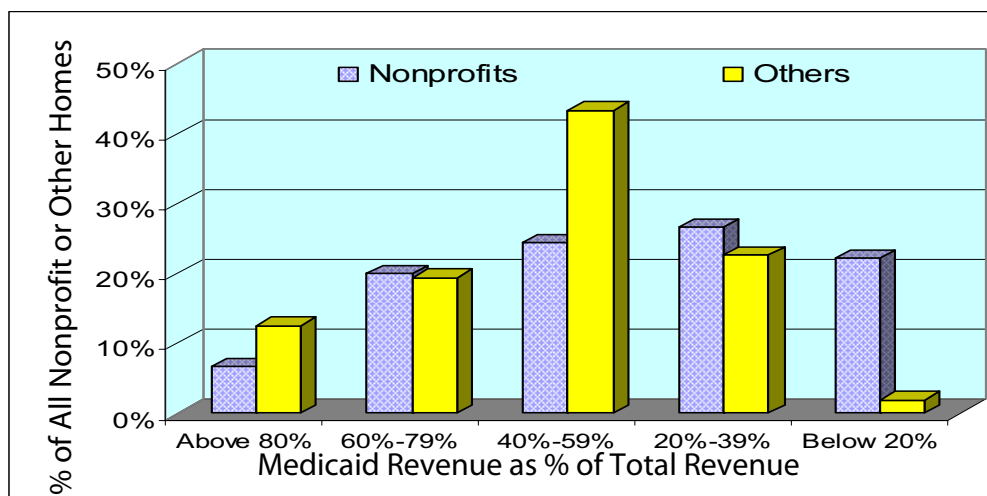
The accessibility to nursing care by low income residents was examined by comparing nonprofit and for-profit nursing homes Medicaid revenue as a percent of total revenue. In terms of serving low income residents, the nonprofit nursing homes have consistently over the past four years had a smaller portion of all patients being Medicaid eligible. This result is consistent with other

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studies in other states which also found that it is most likely that low income Medicaid recipients will be treated by for-profit nursing homes.²¹

On average in 2005, the nonprofit nursing homes had a lower number of Medicaid patients, (58.8 percent) than the for-profit nursing homes (64 percent). This average percentage of Medicaid patients has not changed much for nonprofit nursing homes over the past four years. Figure 2 reveals the distribution of nursing facilities by their percent of total revenue from Medicaid in 2005. For example, seven percent of the nonprofit nursing homes had 80 percent or more of their total patient revenue from Medicaid patients where for-profit nursing homes had 12.5 percent of their facilities with 80 percent or more of their total patient revenue from Medicaid. Over 43 percent of the for-profit nursing homes versus 24 percent of the nonprofit nursing homes had between 40 and 69 percent of their total patient revenue from Medicaid revenue. Nonprofit nursing homes had their largest portion of their homes, 22 percent, with low Medicaid revenue to total patient revenue percentage, below 20 percent versus the for-profit nursing homes had less than two percent of their facilities with the Medicaid portion of total revenue at less than 20 percent.

Figure 2: Distribution of Nursing Homes by Ownership Type and Medicare Revenue as a Percent of Total Revenue - 2005



Source: Department of Health Annual Hospital Reports 2005.

There are other community benefits, besides serving low income patients, that nursing facilities provide that affect the health of the community. As of the time of this audit, the nonprofit nursing home industry in Washington had not completed an inventory of the other charitable services they provide in their local communities. Based on this review of the percent of total patients which are Medicaid patients and the lack of information on other community benefits, it is not clear that the nonprofit hospitals currently receiving this property tax exemption are

²¹ How Nonprofits Matter In American Medicine, And What To Do About It, Mark Schlesinger and Bradford Gray, Health Affairs 25 (2006).

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providing relatively more charitable services and community benefits than nursing homes under other ownership types.

Tables 6a and 6b provide financial data about nursing homes in Washington, differentiated by type of ownership. The tables also allow for a comparison for changes in financial data over time, with one table in 2002 and the other in 2005 (the most recent data available). These statistics are cost reports that nursing homes must file annually with the Department of Social and Health Services (DSHS). There has been considerable debate at the federal level about whether there are differences in hospital financial performance due to the ownership of nursing homes. These two tables compare nursing home statistics by ownership type to determine if differences exist in Washington nursing homes by ownership type. Some other states have adopted thresholds related to some of these types of financial indicators as a basis for qualifying for nonprofit status and receiving a property tax exemption.

The two tables use the following seven financial measures:

- 1) **Routine Patient Revenue as Percent of Gross Revenue** – an indicator of share of revenue that is derived from providing routine care to patients
- 2) **Non-operating Revenue as Percent of Gross Revenue** – an indicator of share of revenue that is derived from other revenue sources like interest and dividend income and sales of real property or other financial assets and gifts and donations
- 3) **Average Charges to Private Pay Patients per day** – an indicator of how much the average private pay resident is charged per day while staying in the nursing home
- 4) **Expenses to Revenue (percent)** – a measure of the profit margin as total expenses are divided by total revenue
- 5) **Average Administrative Salaries and Fringe Benefits per hour** – an indicator of the average salaries and benefits to administrators only per hour
- 6) **Average Salaries and Fringe Benefits for all in-house employees per hour** - an indicator of the average salaries and benefits to all nursing home employees per hour
- 7) **Total Nursing Staff (RN, LPN and Nursing Aids) Hours per patient day** – an indicator of the amount of nursing staff time employed in the nursing home per patient day

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Table 6a: Washington Nursing Home Statistics By Ownership Type - 2002

	Description of Organizational Performance	Nonprofits	Others
Measures of revenue sources and economic performance			
1	Routine Patient Revenue as Percent of Gross Revenue	78.5%	89.3%
2	Non-operating Revenue as Percent of Gross Revenue	10.6%	.41%
3	Average Charges to Private Pay Patients per day	199	158
4	Operating Margin (%)	101.7%	100.6%
Measures of employee salaries and hours of nursing care			
5	Average Administrative Salaries and Fringe Benefits per hour	\$48.8	\$41.6
6	Average Salaries and Fringe Benefits for all in-house employees per hour	\$22.6	\$22.8
7	Total Nursing Staff (RN, LPN and Nursing Aids) Hours per patient day	3.97	3.43

Table 6b: Washington Nursing Home Statistics By Ownership Type
Most Recent Year 2005

	Description of Organizational Performance	Nonprofits	Others
Measures of revenue sources and economic performance			
1	Routine Patient Revenue as Percent of Gross Revenue	72.0%	87.31%
2	Non-operating Revenue as Percent of Gross Revenue	14.3%	0.24%
3	Average Charges to Private Pay Patients per day	\$242	\$182
4	Expense to Revenue (%)	99.50%	97.95%
Measures of employee salaries and hours of nursing care			
5	Average Administrative Salaries and Fringe Benefits per hour	\$52.12	\$46.91
6	Average Salaries and Fringe Benefits for all in-house employees per hour	\$25.87	\$24.68
7	Total Nursing Staff (RN, LPN and Nursing Aids) Hours per patient day	3.99	3.44

The source of revenue for nursing facilities is different depending on the type of ownership. In 2002, for-profit and other nursing facilities routine patient revenue as a percent of gross revenue from all revenue sources (operating and non-operating revenue) was 12 percent higher at 89 percent than the routine patient revenue percent of gross revenue for nonprofit nursing homes at 78.5 percent, see indicator (1). In 2005, for-profit nursing facilities' percent of gross revenue that was routine patient revenue was slightly lower than in 2002 at 87 percent where the nonprofit nursing homes' percentage of gross revenue that was patient revenue declined 6.5 percentage points to 72 percent and the difference between the two types of nursing homes' percent of gross revenue that was routine patient revenue grew to 21 percent. This reveals that nonprofit nursing homes are receiving a larger share of their total revenue from other sources besides routing patient care.

Other sources of revenue for nursing homes are non routine patient revenue and non-operating revenue, see indicator (2). Nonprofit nursing homes receive a sizably larger share of their gross revenue, 10.6 percent, from non-operating revenue than for-profit and other nursing homes

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which received .4 percent of their gross revenue from non-operating revenue in 2002. In 2005, the nonprofit nursing homes received a slightly higher percentage of gross revenue for non-operating revenue at 14 percent. This result is not surprising given the fact that nonprofits have a restriction on what they can do with their profits and that non-operating revenue includes gifts and endowments which is a more common source of revenue for nonprofits.

Due to the differences in the sources of revenue for nonprofit versus for-profit and other nursing homes, there are sizeable differences in the average charge to private pay patients, see indicator (3). In 2002, the average charge to private pay patients per day was \$199 in nonprofit nursing homes versus \$158 in other for-profit nursing facilities. This is a difference of 27 percent between for-profit and nonprofit private pay charges per day. In 2005, the nonprofit nursing homes' private pay charge per day was \$242 and for-profit nursing homes' private pay charge was \$182, and the difference between the two types of nursing homes' private pay charges is growing and is more than 30 percent.

Indicator (4) which is expenses to revenue percentage demonstrates the differences between the nonprofit and for-profit structure and the amount of profit or net income that the nursing homes receive. When the percentage is above 100 percent then the nursing homes have net income losses because expenses are above revenue. A percentage below 100 percent means the nursing homes have positive profits. Nonprofit nursing homes in 2002 has on average total expenses to revenue of 101.7 percent and in 2005, the percentage fell very slightly to 99.5 percent. Since nonprofits cannot distribute their income as profits to anyone, they may not have the same motivation for-profits to minimize expenses. Since the Medicaid reimbursement rate is based on costs, if nursing homes can spend more on their facilities or labor and increase costs, they can receive higher Medicaid reimbursement payments. Nonprofit nursing homes may operate under the assumption that if they spend their profits on nursing care services then this will likely lead to better care, resulting in new patients and higher Medicaid payments that will increase revenues. On the other hand, for-profit nursing homes have a bigger incentive to minimize costs because the profits can be distributed to share holders. In 2002, the average total expense to revenue for for-profit nursing homes was 100 percent and it improved slightly to 97.9 percent.

Other considerations between nonprofit and for-profit nursing homes are differences in wages and the amount of nursing care in each home, indicator (5) reveals that nonprofit nursing homes in 2002 paid their administrators on average \$52 per hour which was approximately \$7 more per hour than for-profit and other nursing homes. That wage difference has declined slightly to a difference of \$5 per hour in 2005 between the different nursing home ownership types. The total average salaries and fringe benefits for all in-house employees, indicator (6), was nearly the same between nonprofit and for-profit nursing homes in 2002 at a little more than \$22 per hour. Now, the difference between the average salaries and fringe benefits for all in-house employees has slightly grown so nonprofit nursing homes on average pay \$25.9 per hour and for-profit nursing homes pay \$24.7 per hour in 2005. The nonprofit nursing homes pay \$1.20 more per hour on average for all their in-house employees. Some specific types of nursing care employees also receive higher wages in nonprofit nursing homes than in for-profit homes, like RNs and nursing assistants' who received more than \$1 more per hour in nonprofit nursing homes in 2005.

The number of hours of nursing care, indicator (7), also varies between different ownership types of nursing homes. The number of hours of registered nurse (RN) care per patient day was higher, .6 per patient day, in nonprofit nursing homes than in for-profit homes, .2 per patient day. This difference in the number of hours of skilled RN care has been fairly consistent over the past four years. The total number of hours of all types of nursing providers (RN, LPN and nursing assistants) per patient day is higher in nonprofit nursing homes by .5 hours per patient day than in for-profit nursing homes in 2005.

Past nursing facility studies (e.g., Luksetich et al., 2000; Vitaliano, 2003) often assume that if costs are higher, number of nursing care hours and salaries, then the quality of care goes up. Unfortunately cost is a poor proxy for quality of care; and when independent measures of quality of care exist, they are only weakly correlated with measures of nursing inputs.²² One would expect that the higher the number of hours of nursing care, the better the care will be for the patient. That expectation assumes that the nursing staff will be the same in one home versus another when there could be very distinct quality difference in staff, like years of experience and retention rate of staff, which would make the quality of care different between homes. Those additional characteristics of the nursing care employees are lacking from the comparison of the number of nursing care hours alone.

Based on this assessment of different financial indicators based on ownership type, it is not clear if the federal requirements for nonprofit charitable nursing homes currently receiving this property tax exemption are meeting the expectations that the Legislature had intended for nursing homes when they narrowed this tax preference to nonprofit organizations.

Beneficiaries

Who are the entities whose state tax liabilities are directly affected by the tax preference?

Forty-two nonprofit nursing homes received a property tax exemption on a total of 87 parcels statewide in property tax year 2006-07. As was illustrated in Figure 1, the majority of the nonprofit nursing homes are in heavily populated urban counties like King, Snohomish, Spokane, Pierce and Thurston. There are eight nonprofit nursing homes in rural counties like Whatcom, Walla Walla, Kitsap and Yakima.

To what extent is the tax preference providing unintended tax benefits to entities other than those the Legislature intended?

No nursing homes other than nonprofit nursing homes are receiving this tax preference. The question of whether all nonprofit nursing homes are meeting the expectations of nursing homes that the Legislature had envisioned when limiting this tax exemption to nonprofit nursing homes is a more difficult question to answer. The current property tax exemption for nursing homes run by nonprofit organizations provides these homes with the same tax benefit as government

²² Comparative Performance and Quality Among Nonprofit Nursing Facilities in Texas, Kris Joseph Knox and Eric Blankmeyer and J.R. Stutzman, *Nonprofit and Voluntary Sector Quarterly*, vol. 35 no. 4, December 2006.

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owned nursing homes. There is now unequal tax treatment among long term care facilities and nursing homes due to the divergence between the nursing home having a complete property tax exemption and homes for aged property being subject to a threshold test depending on the number of low income residents living within the facility.

Revenue and Economic Impacts

What are the past and future tax revenue impacts of the tax preference to the taxpayer and to the government if it is continued?

Prior to 1990, this nursing home tax preference also included a property tax exemption for the homes for the aged which included a variety of long-term care residential living facilities. Prior years' reports of the Department of Revenue Tax Exemption Report revealed that 75 nursing homes were benefiting from this tax particular preference in 1990. The value of the tax preference grew in the mid-1990s due to growth in property values statewide. The number of nursing facilities was constant between 1990 and 1994 but six years later the number of nonprofit nursing homes had declined to less than 50 homes in the state. Since 2000, the number of nonprofit nursing homes has not changed significantly. In 2000, the number of nonprofit nursing homes was 45 homes and in the 2004 Tax Exemption Report, there were 41 nonprofit homes reported. In 2007, the number of nonprofit nursing homes claiming a property tax exemption is 42.

Table 7 provides the forecast for the local and state property tax savings for nonprofit nursing homes and this estimate is based on the merging of the sampled counties assessed value with the DOR nonprofit exemption database for 2007. The property tax saving for property tax year 2006-07 is estimated to be \$2.8 million which is based on \$252 million in exempt nursing home property. The forecast of the property tax exemption is estimated to be \$2.9 million in property tax year 2007-08 and grow to \$3 million by 2009-10.

Table 7: Forecast of Local and State Property Tax Savings for Nonprofit Nursing Homes

Year	Exempt Value (\$ millions)	State Property Tax Savings	Local Property Tax Savings	Total Property Tax Savings
2006-07	\$252	\$510,000	\$2,320,000	\$2,830,000
2007-08	\$262	\$530,000	\$2,370,000	\$2,900,000
2008-09	\$272	\$550,000	\$2,440,000	\$2,990,000
2009-10	\$283	\$570,000	\$2,520,000	\$3,090,000

If this tax preference is continued and the exempt property value was not added to the tax roll, then nonprofit nursing homes would continue to not pay property taxes and other local taxpayers would pay slightly higher property taxes annually. It is estimated that in the counties with nonprofit nursing homes, on average the local property tax rate is higher by .08 percent with the largest difference in Thurston County's overall property tax rate of .48 percent. There would be a shift in the tax burden in specific locations where the nonprofit nursing homes are found statewide but the increase in the overall tax rate would be minimal to most taxpayers. The net

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revenue impact to local governments would depend on whether the taxing districts, where the nonprofit nursing homes are located, are at their maximum property tax rate limit or not. Governments will not see a change in their overall property tax revenue due to the continuation of this tax preference because of the shifting of tax liability among taxpayers if taxing districts are not at their maximum tax rate limit.

What impact do the beneficiaries of the tax preference have on the economy at a state and regional level?

To assess the economic impacts, this study first looked at that states' nursing home and residential care industry. According to 2004 data from IMPLAN on Washington's nursing home and residential care industry, the industry output was \$2.66 billion in services. This industry represents .6 percent of total statewide industry output of goods and services of \$460 billion in 2004. According to the Washington Employment Security Department data on the nursing home and residential care, in the third quarter of 2006, which is the most recent data available, there are 54,499 employees in this sector with 1,601 firms. This industry represents 1.9 percent of all employees statewide for the third quarter of 2006. Within the nursing home and residential care industry, the nursing facilities alone represent 46 percent of the entire nursing and residential care facilities industry sector employment. Table 8 reveals the number of firms, employees and total wages in the nursing home sector from 2002 through 2006 of which the data for 2006 only includes 3 quarters of data. Of the total nursing facilities statewide, this tax preference only benefits nonprofit nursing facilities. From the DSHS annual cost report data for nursing homes, there is information on the number of full-time and part-time employees. From that cost report data for 2005, the nonprofit organizations' portion of total full-time employees is 22 percent of total employees in all nursing homes statewide. It is estimated that nonprofit employees in 2005 totaled 4,680 full-time and part-time 2,373 employees for a total of 7,053 employees.

Table 8: Number of Firms, Employees and Wages in the Nursing Home Facilities Industry Sector

Year	Number of Firms	Total Employees	Total Wages (\$ millions)
2002	192	24,906	\$588.64
2003	191	24,789	\$600.68
2004	189	24,175	\$608.82
2005	183	24,074	\$622.69
2006*	190	24,998	\$506.96

Source: Washington Employment Security Department Covered Employment Data.

*2006 reflects 3 quarters of data.

Other States

Do other states have a similar tax preference?

According to the JLARC CCH state survey on other states' property tax exemptions for nursing homes, the results show that 23 states, including Washington, have a specific property tax exemption for property used by homes for the sick or infirm. All other states have property tax

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exemption provisions for charitable institutions of which a nursing home may qualify given the specific statutes in each state. Twelve states have restrictions on the charitable institutions in a variety of ways. For example, Colorado has adopted a gross revenue threshold test for nonprofit health care facilities to meet. Idaho has its own nonprofit status that must be met to qualify on the basis of charitable use. New Hampshire, Texas, Pennsylvania and Utah all require nonprofit nursing facilities to meet the charitable purpose tests, before it can be classified as exempt property. North Carolina requires a charitable purpose to have “human and philanthropic objectives.” Oregon requires the facility to be an “essential community provider.”

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