

## **Indiana Government Officials and Nonprofit Property Taxes**

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Briefing Number 2, Spring 2013

### **Indiana Intergovernmental Issues Study**

The Indiana Advisory Commission on Intergovernmental Relations (IACIR) periodically collects information on current issues affecting local governments in Indiana and services for state residents. In 2010, the IACIR surveyed nearly 1,150 local government officials including mayors, county auditors, county commissioners, county and town council members, school board members, and township trustees. The response rate was 35 percent. A summary of findings from the full 2010 survey can be found at the IACIR website: [www.iacir.spea.iu-pui.edu](http://www.iacir.spea.iu-pui.edu).<sup>1</sup>

This briefing assesses local government officials' opinions on nonprofit property tax policies, PILOTs (payments in lieu of taxes), and SILOTs (services in lieu of taxes). It is the second in a series of briefings from the *Indiana Nonprofits: Scope and Community Dimensions* project that focuses on nonprofit-government relations in Indiana. The first explored local government officials' attitudes toward 2-1-1 services. Subsequent briefings will examine relationships between local government and nonprofits, reliance on nonprofits to deliver government services, and nonprofit volunteer activities of local government officials. These briefings are available at the project website: [www.indiana.edu/~nonprof](http://www.indiana.edu/~nonprof).

### **What are PILOTs and SILOTs?**

In Indiana, most charities are exempt from property taxes. The Indiana State Constitution states that the General Assembly may provide property tax exemptions for "property being used for municipal, educational, literary, scientific, religious or charitable purposes" (Article 10, Section 1).

These policies benefit charitable nonprofits and are thought to acknowledge the public value that they create. Governmental buildings (e.g., court houses,

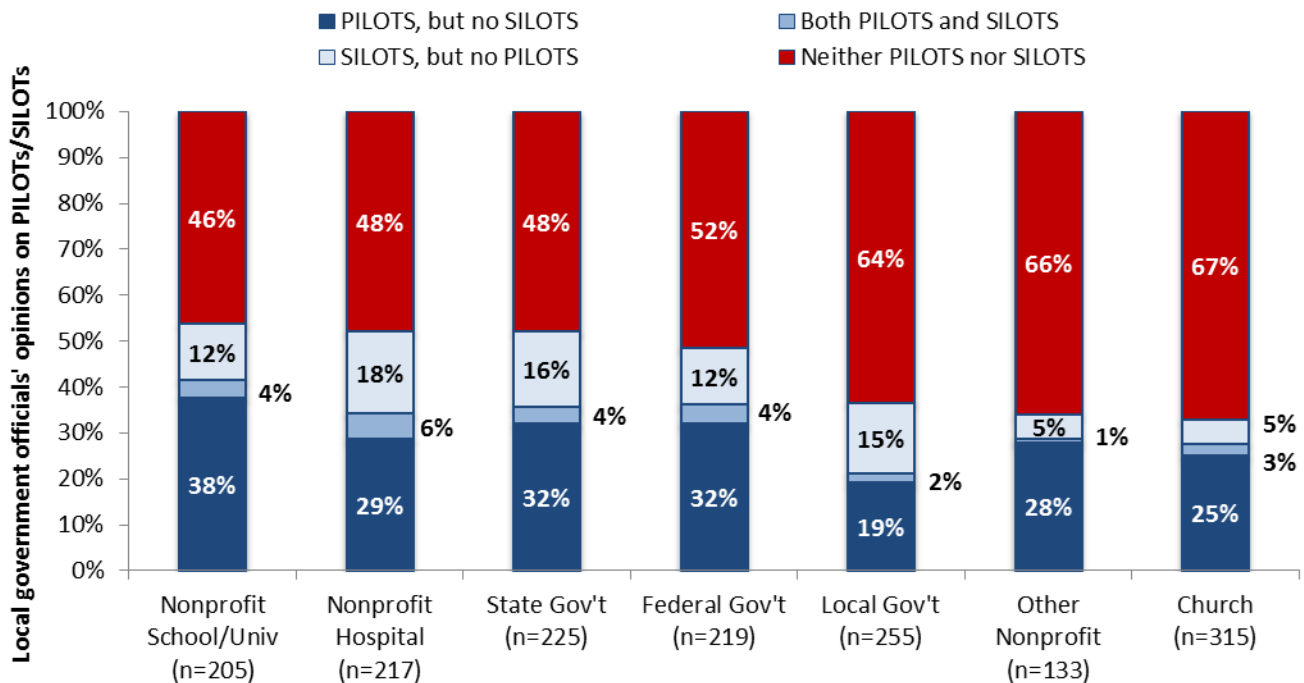
#### **Quick Facts**

- PILOTs or "payments in lieu of taxes" are non-voluntary payments (e.g., fees) that organizations make to local governments in lieu of taxes. SILOTs are "services in lieu of taxes."
- Local government officials prefer PILOTs over SILOTs, according to our survey.
- Over 50 percent of respondents think that nonprofit schools, universities, and hospitals should be obligated to provide PILOT and/or SILOT benefits to local communities.
- Over 30 percent think churches should provide PILOT and/or SILOT benefits.

public schools, city community centers) also are excluded from property taxes.

PILOTs are mandatory fees for municipal services that are paid by land-owning organizations that are

**Figure 1: Local government officials' opinions on what types of organizations should provide payments or services in lieu of property taxes**



Source: 2010 IACIR Survey

Faced with decreasing revenues and growing budgetary pressures, however, some municipalities are reconsidering nonprofit property tax exemptions. In the wake of the recent “great recession,” nearly nine out of ten cities reported that they were having more trouble meeting their fiscal needs.<sup>2</sup> Furthermore, Indiana began phasing in property tax caps in 2009, as well as other reforms which affected local government revenues.<sup>3</sup>

Over 40 percent of property taxes support local public schools.<sup>4</sup> Additionally, cities and counties rely heavily on property taxes to fund essential services like police and fire departments, garbage collection and snow removal, road construction and maintenance, public libraries, etc. Some local governments have instituted PILOTs and SILOTs to recover a portion of the revenue they would receive if nonprofit and public properties were taxed.

exempt from property taxes. Similarly, SILOTs require community programs or services from organizations with tax-exempt property.

These policies have been highly polarizing. Many nonprofits, which have also found themselves cash strapped after the recent recession, oppose such policies. Diana Aviv, Executive Director of the Independent Sector, told *The New York Times*, “Our members are beyond upset, they’re fearful. They know that state elected officials are short of cash and are looking for every opportunity — and, frankly, excuse — to raid pots of money to pay for other pressing needs.”<sup>5</sup>

In contrast, Matt Greller, executive director of the Indiana Association of Cities and Towns, commented, “We’re having to look at the public services nonprofits use and how we can adequately

cover those costs...We can't give them away for free any longer."<sup>6</sup>

## What organizations should be subject to PILOTs and SILOTs?

**Generally local government officials were more in favor of PILOTs than SILOTs for property tax-exempt nonprofit and public organizations** (Figure 1).<sup>7</sup> This could be because cash payments have a more quantifiable impact on local government revenues. It may also be more difficult to decide which specific services each organization could or should provide. Additionally, PILOTs feature more prominently than SILOTs in the news media and trade publications.

Opinions on PILOTs and SILOTs appear to vary based on the local government official's job. For example, county auditors are not particularly in favor of these programs (perhaps because they would be directly involved in implementing these decisions), while school board members are interested in using these programs to obtain tax payments from hospitals in their districts. Overall, however, local government officials were more in favor of PILOTs and SILOTs for hospitals and private schools than they were for churches or other types of nonprofits.

### *Hospitals and educational institutions*

**Over half of local government officials think that hospitals and privately operated nonprofit educational institutions should be required to make payments or provide services in lieu of taxes.** Over 35 percent think PILOTs are appropriate for nonprofit schools, universities, and colleges. Over 25 percent are in favor of PILOTs for nonprofit hospitals. Slightly more officials mentioned wanting SILOT arrangements from hospitals than educational institutions. This may reflect a growing opinion that nonprofit hospitals should provide more community health services, as well as the fact that hospital "charity care" has a long history in the United States.

"Meds and eds" are often the target of PILOTs. Some of these reasons are logistical. For example,

these are large organizations that use local services (e.g., water, sewers, fire protection, and police services) more heavily than smaller organizations. Additionally, with their large property holdings, they are more of a drain on tax revenue than churches or nonprofits with smaller property sizes. Being large also means they appear to have the resources to afford PILOTs, by either absorbing the cost or covering it through increased fees for services.

Often hospitals and colleges provide services to numerous clients that reside outside the local tax district. Some individuals question the equity of providing tax exemptions to nonprofits that do not primarily serve their community. Furthermore, nonprofit hospitals provide services similar to their non-exempt for-profit counterparts; giving a tax break to one hospital may be an unfair competitive advantage.

Even with these rationales, taxing hospitals and educational institutions remains controversial. For example, Fort Wayne Mayor Tom Henry faced considerable public backlash when he noted that the Urban Mayors Caucus was considering negotiating PILOTs with large universities and hospitals.<sup>8</sup> Illinois, however, recently enacted legislation that property tax exemptions would only be granted to hospitals engaged in "qualified service or activities," such as charity care or health programs to low-income families.

### *Churches and other nonprofits*

**Over 30 percent of government officials said that churches should provide payments or services in lieu of taxes, including more than 25 percent who favor PILOTs.** Not surprisingly, taxing churches and religious property is highly controversial. The *Indianapolis Star* noted in 2007 that there were over 1,600 tax-exempt churches in Marion County alone.<sup>9</sup> In the same year, the state legislature considered an amendment to the state constitution that would explicitly prohibit taxing properties used for "religious worship."<sup>10</sup> State Representative Tom Saunders, R-Lewisville, has pushed for PILOTs in the past but reported that concerns over taxing churches has made such proposals unviable.<sup>11</sup>

**Nearly one-third of government officials are also in favor of PILOTs and/or SILOTs from other types of nonprofit organizations.** In particular, one respondent noted that other nonprofits (including service groups like Lions Club International) should offer lower-cost services to the community.

### *Government property*

Property tax exemptions for government land are rooted in the Supremacy Clause of the Constitution and traditional notions of sovereign immunity. Some researchers and public officials, however, question the legitimacy of this logic in the face of modern federalism.<sup>12</sup>

**Around 50 percent of local government officials believe state and federal government properties should be subject to PILOTs and/or SILOTs. Only about one-third feel this way about local government facilities.** If officials are interested in supplementing local government revenue, it follows that they would not want to increase taxes on their own land holdings.

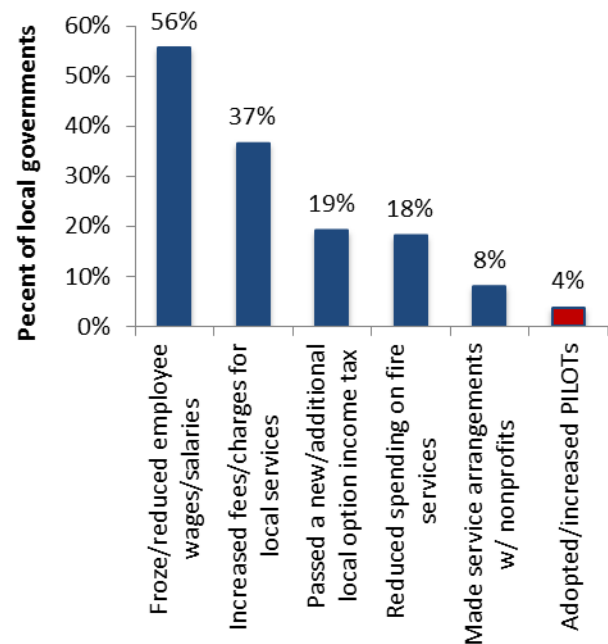
### **Where have PILOTs and SILOTs been implemented in Indiana?**

One problem with PILOTs and SILOTs is that they are rarely transparent to the public; government records do not provide clear information about which organizations are subject to these policies and how much they pay the local governments. Detailed research found indications that six Indiana localities have PILOT programs, but only three nonprofits are affected by these policies.<sup>13</sup> Most notably, in 2009, the University of Notre Dame announced it planned to pay a total of \$5.5 million (according to a PILOT agreement) over 10 years to three towns/cities (South Bend, Mishawaka, and Roseland), as well as St. Joseph County. Additionally, KCARC, a nonprofit in Knox County that provides services for individuals with disabilities, implemented a PILOT program in Vincennes. The Mayor of Vincennes has also asked for PILOT arrangements from Vincennes University and Good Samaritan

Hospital, but it is unclear if these were implemented. Finally, Indianapolis has a PILOT arrangement with an undisclosed nonprofit organization and a public wastewater treatment facility.<sup>14</sup>

**While many local officials appear to be in favor of PILOTs in this study, few (only 4 percent) said their governments had recently enacted such policies in response to tax revenue shortfalls.** In contrast, nearly half report having frozen or reduced wages for government employees, and over one-third report increased fees for local services (Figure 2).

**Figure 2: Local government actions in response to decreased tax revenue (n=405)**



With limited data, it is unclear whether government officials may believe the costs of implementing PILOTs and SILOTs might outweigh the benefits; furthermore, information on how local governments calculate the costs and benefits of such policies is extremely limited.<sup>15</sup> In addition, broad public support is essential for implementing such policies. Charities affected by these policies can mobilize effective and vocal opposition.<sup>16</sup> In some cases, politicians may find that the potential revenue gained from PILOTs might not outweigh the associated political backlash.<sup>17</sup>

Finally, PILOTs account for less than 1 percent of local government revenue nationwide. Notre Dame's payments account for less than 2 percent of local government budgets in the relevant regions.<sup>18</sup>

Simply put, the revenue gains from PILOTs (and perhaps SILOTs) might simply be not worth the administrative efforts and political costs.

Even so, other governments have tried to recoup lost property tax revenue by instituting fees instead of official PILOTs. For example, Muncie requires Ball State University to pay a small fee for fire protection. Indiana University has a similar agreement with the City of Bloomington.

## Conclusions

Contention surrounds nonprofit property taxes. Nonprofit property tax exemptions are thought to enable and support charitable organizations. Nonprofits provide services that alleviate the burdens of local governments and improve the quality of our communities. Yet the impact of these exemptions has raised concerns regarding equity among community members:

- Nonprofit property tax exemptions result in a loss of local government revenue – funds that go toward public schools, road maintenance, street lights, police, and other public services.
- When a large nonprofit receives an exemption, other property owners may pay higher taxes to offset the lost revenue.
- Some tax-exempt nonprofits (e.g., universities) provide services to people outside the community. This means that nearby residents pay higher taxes for services that may not directly benefit their community.

Additionally, property tax exemptions can create inequities among nonprofits and other businesses:

- Only nonprofits owning and using real estate receive this tax exemption. Nonprofits that rent facilities do not benefit from the exemption, even if they provide identical services. Standard

property tax fees are built into their rent payments.

- Additionally, for-profit businesses that provide similar types of services as nonprofits (e.g., day-care, health care, etc.) do not benefit from the exemption.

Local governments have tried to implement PILOTs and SILOTs to offset these revenue and equity issues. However, these efforts have at times led to contradicting two fundamental taxation principles:

- Equity – Local government PILOTs are not implemented fairly. They tend to target large, visible nonprofits like hospitals and universities while overlooking other exempt properties.
- Transparency – The details of PILOT agreements often are not transparent to other community taxpayers. It is often unclear which nonprofits make PILOTs and SILOTs, let alone the details of these arrangements.

In the face of so many problems, removing nonprofit property tax exemptions entirely may be a solution; however, many state constitutions (including Indiana - see Article 10, Section 1) provide for the exemption, which limits this option.

The financial pressure on cities and counties is not likely to dissipate in the near future. The stricter property tax caps implemented at the end of 2010 mean local governments in Indiana will continue to look for additional revenue sources. Furthermore, charities struggling to recover from the recession will still depend on local government to support their public service activities.

Nonprofit property tax exemptions, PILOTs, and SILOTs are therefore likely to be an ongoing debate. Communities should engage in open and fair discussions about the benefits and repercussions of these exemptions to find solutions that best serve the interests of all parties.



## Acknowledgements

This analysis of local government and nonprofit sector relations is a joint effort with the Indiana University Public Policy Institute, the School of Philanthropy, and the School of Public and Environmental Affairs at Indiana University. We seek to help community leaders develop effective and collaborative solutions to community needs and to inform public policy decisions by providing baseline information about the Indiana nonprofit sector.

This briefing is made possible by support for the Efroymsen Chair in Philanthropy from the Efroymsen Fund at the Central Indiana Community Foundation, the Indiana University Center on Philanthropy's Indiana Research Fund (supported in part by Lilly Endowment Inc.), and the School of Public and Environmental Affairs at Indiana University, Bloomington.

We thank members of the Advisory Board of the Indiana Nonprofit Sector: Scope and Community Dimensions project for helpful comments and suggestions. We are particularly grateful to Tom Rugh and Lucinda Nord of the Indiana Association of United Ways and Bob Cross of United Way of Central Indiana for helpful comments on our original analysis plan, and to Leslie Lenkowsky for his support in developing these and other nonprofit-related questions for the IACIR survey.

## Suggested Citation

*Indiana Government Officials and Nonprofit Property Taxes*, by Kirsten A. Grønberg and Kellie L. McGiverin-Bohan, with Lauren Dula, Weston Merrick, Deb Oonk and Katherine Zilvinskis. (Bloomington, IN: Indiana University School of Public and Environmental Affairs, 3/2013.)

<sup>1</sup> Palmer, J., Wyeth, D., with Chang, J. (2010). Intergovernmental Issues in Indiana: 2010 IACIR Survey. Indiana Advisory Commission on Intergovernmental Relations.

<sup>2</sup> Hoene, Christopher W. & Michael A. Pagano, 2010. "City Fiscal Conditions in 2010." *Research Briefs on America's Cities*. 2010. Washington, D.C.: National League of Cities.

<sup>3</sup> DeBoer, Larry. (2010). *Indiana's Property Tax Reforms, 2008-2010 and Beyond*. West Lafayette, IN: Purdue University – Farm Policy Study Group.

<sup>4</sup> State of Indiana. (2012). *Citizen's Guide to Property Taxes in Indiana*.

<sup>5</sup> Strom, Stephanie. (Feb 27, 2010). States Move to Revoke Charities' Tax Exemptions. *New York Times*.

<sup>6</sup> *ibid.*

<sup>7</sup> This briefing accounts for officials that indicated interest in both PILOTs and SILOTs, and adds additional categories to the analysis. Therefore, the calculations in this briefing are slightly different than those used in the IACIR report

<sup>8</sup> Francisco, Karen (Feb 14, 2010). Taxing nonprofits: Should high revenue groups pay for services? *The Journal-Gazette*.

<sup>9</sup> King, R and Nichols, M. (Aug 19, 2007). More than 1600 churches tax-exempt. *Indianapolis-Star*.

<sup>10</sup> Associated Press. (Dec 13, 2007) Proposal would amend constitution to keep churches tax exempt. *The Journal Gazette*.

<sup>11</sup> Francisco, K. (Feb 14, 2010). Taxing nonprofits: Should high revenue groups pay for services? *The Journal Gazette*.

<sup>12</sup> Bowman, W. (July 2003). Reexamining the property tax exemption. *Land Lines*, 15(3).

<sup>13</sup> Langley, A. H., Kenyon D. A., Bailin, P. C. (2012). Payments in Lieu of Taxes by Nonprofits: Which Nonprofits Make PILOTs and Which Localities Receive Them. Cambridge, MA: Lincoln Institute of Land Policy.

<sup>14</sup> *Ibid.*

<sup>15</sup> Longoria, T. (2012). Predicting Use and Solicitation of Payments in Lieu of Taxes. *Nonprofit and Voluntary Sector Quarterly*. (Published online only).

<sup>16</sup> *Ibid.*

<sup>17</sup> Russ, H. (Sep 28, 2012). U.S. cities' revenue boost from nonprofits meager. *Reuters*.

<sup>18</sup> *Ibid.*