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The Wauwatosa Outpatient Center Decision Is Good News for Hospitals and Other Providers of Health Care and Senior/Retirement Housing Seeking or Defending Property Tax Exemptions

Synopsis

The City of Wauwatosa's challenge to a property tax exemption for Wheaton Franciscan Healthcare's outpatient facility has been widely followed as a test case affecting not only hospitals, but also other nonprofit providers of health care and senior housing. The issues raised in this lawsuit will have particular impact on off-campus hospital outpatient facilities, certain joint ventures, and any hospital that is part of a larger health care system. Recently, a Milwaukee County judge largely rebuffed Wauwatosa's challenge, sustaining the property tax exemption for the St. Joseph Hospital outpatient facility in Wauwatosa. Reinhart attorneys Don Millis and Kristina Somers represented Wheaton Franciscan Healthcare in this case.

Background

One of the hospitals owned by Wheaton Franciscan Healthcare—St. Joseph Regional Medical Center¹—developed a hospital outpatient facility in Wauwatosa. The outpatient facility provided outpatient services in the same manner as would be provided within the four walls of a hospital: (1) Services were provided by physicians credentialed to practice in the main hospital; (2) Services were subject to hospital-based billing; (3) The outpatient center shared the same records system, billing system and staff bylaws with the main hospital; and (4) The facility was built to hospital construction standards.

Private Benefit

Wauwatosa's most fundamental objection was to challenge the exempt status of Wheaton Franciscan Healthcare itself, essentially challenging the exempt status of all hospital property owned by the system. The hospital exemption statute provides that the net earnings of a nonprofit hospital may not inure to the benefit of a shareholder, director, officer or member. Wheaton Franciscan Healthcare is the parent corporation, technically a member of St. Joseph Hospital.

St. Joseph Hospital—the owner of the outpatient facility—never paid Wheaton Franciscan Healthcare a dividend. However, St. Joseph Hospital and other hospitals in the system paid for a disproportionate share of the services provided by Wheaton Franciscan Healthcare in order to subsidize other facilities in the system (*e.g.*, nursing homes) that could not cover their costs.

Wauwatosa argued that making disproportionately large payments for services constituted impermissible private benefit to a member, *i.e.*, Wheaton Franciscan Healthcare. The Court rejected this argument, concluding that the statute was not intended to apply to payments to a member that is a nonprofit corporation.

¹St. Joseph Regional Medical Center is now known as Wheaton Franciscan Healthcare—St. Joseph.

Commercial Purposes

The outpatient facility was designed to expand and improve the services provided by St. Joseph Hospital, including women's health services, urgent care and wound care. While acknowledging the expansion of services, the outpatient facility's business plan focused on economic considerations. Wauwatosa argued that the economic focus in planning for the facility indicated that it was built for a commercial purpose, and therefore was not exempt. The Court rejected this argument. The Court acknowledged that nonprofit hospitals operate in a competitive environment and that attention to these pressures does not mean the facility was designed for commercial purposes.

The Court's commercial purposes holding may help health care providers other than hospitals. While the exemption statute governing non-hospital providers does not explicitly preclude commercial purposes, courts often are influenced by the commercial nature of an enterprise. The court's recognition that nonprofit health care providers exist in a competitive environment runs counter to the assertion by many assessors who appear to argue that any attempt to be successful should preclude a tax exemption.

Doctor's Office

The hospital exemption does not apply to property used for doctor's offices. About two floors of the outpatient facility were used by physicians for their practices and no exemption was sought for this area. Wheaton Franciscan Healthcare sought an exemption for the balance of the facility that was dedicated to providing outpatient services in the same manner as outpatient services that are provided within any hospital.

Wauwatosa argued that an outpatient facility, regardless of the manner in which the services are provided, is a doctor's office and, therefore, is not exempt from the property tax. The Court rejected the City's argument, noting all of the ways in which the outpatient facility operated in the same manner as a hospital.

Leased Property

While Wheaton Franciscan Healthcare obtained a property tax exemption for that portion of the building containing the outpatient facility and all of the personal property used in the facility, the court denied an exemption for the land. In essence, the exemption for the land was lost because St. Joseph Hospital does not own the land, but leased it. The bar is higher for leased property than property that is owned when it comes to property tax exemptions. The lesson is that when it comes to joint ventures and partnerships, leasing property will increase the chances that the exemption will be lost. If possible, alternatives to leases should be considered.

Postscript

Wauwatosa may appeal, so this decision may not be the final word on these issues for a few years. Yet, no matter how this case ultimately plays out, it is clear that many local governments are stepping up their efforts to deny property tax exemptions to health care providers and senior living facilities. The statutes governing property tax exemptions contain a number of hurdles, each of which must be met to obtain the exemption. As health care providers enter into more novel and unconventional arrangements to provide services, they must remain cognizant of the effect these arrangements will have on their eligibility for property tax exemptions.

For more information about the taxability of leased property—as well as other property tax exemption issues—contact your Reinhart attorney or the authors:



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