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## IMPORTANT COURT DECISION REGARDING COLORADO TAX EXEMPTION FOR RELIGIOUS AND CHARITABLE ORGANIZATIONS

Tax exemption comes in many different flavors – there’s the federal 501(c)(3), Colorado’s state property tax exemptions, and local sales and use taxes. Charitable senior service organizations need to be aware of changes in all of these tax exemption systems in order to continue to receive the benefits of tax exemption.

Colorado’s Supreme Court issued an important new local sales and use tax decision on June 1, 2009 in the case of *Catholic Health Initiatives Colorado v. City of Pueblo*. The case offered the first opportunity since 1968 (when the Court issued a decision called *United Presbyterian Association v. Board of County Commissioners of the County of Jefferson*) for the court to give its opinion about the tax exempt status of senior living facilities under local sales and use tax systems.

The City of Pueblo’s local tax ordinance, like many others around Colorado, uses the following definition of the charitable purposes that will support a local tax exemption:

[A] charitable organization is an organization which exclusively, and in a manner consistent with existing laws and for the benefit of an indefinite number of persons, freely and voluntarily ministers to the physical, mental or spiritual needs of persons, and which thereby lessens the burdens of government.

Villa Pueblo Towers, a continuing care retirement community operated by Catholic Health Initiatives Colorado (“CHI”), contended that it did not have to meet this definition of a charitable organization because all of the services provided at Villa Pueblo Towers were part of the religious mission of CHI. CHI claimed that it would violate the First Amendment of the US Constitution, and the state constitution as well, for the City of Pueblo to inquire into this religious mission to determine if the local property tax should be imposed.

In a change from existing law, the Supreme Court stated that a religious organization may not be undeniably entitled to a property tax exemption for its senior care services under the language used in Pueblo’s ordinance. The court stated that to obtain the local sales and use tax exemption, the religious organization must also show that it meets the standards for a *charitable* organization.



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This is where the case got extra interesting (at least for lawyers). In an initial decision issued March 30, 2009, the Court stated that unless a senior care provider was serving *only* people who did not have the financial means to provide for themselves, there was no right to obtain a sales and property tax exemption under Pueblo's ordinance. The court showed contempt for the argument that seniors have needs for charitable services even if they can afford to pay for middle class housing:

Put simply, government has no burden to provide 'retirement lifestyle' housing to elderly people who enjoy sufficient independent financial means to provide for themselves. . . . [T]here may be some residents for whom the provision of housing or nursing services does lessen the burdens of government. However, because many of Villa Pueblo's residents are financially independent, Catholic Health's provision of such services does not exclusively 'lessen the burdens of government,' and, therefore, does not fit the definition of 'charitable organization' utilized by the City of Pueblo.

The court further noted that CHI did not operate Villa Pueblo Manor entirely "freely and voluntarily" as required by the Pueblo ordinance.

Villa Pueblo does 'freely and voluntarily' minister to some residents. However, the City of Pueblo's definition requires an organization to 'exclusively' provide services in a free and voluntary manner in order to qualify for the charitable organization sales and use tax exemption. As long as Villa Pueblo provides housing or nursing services to residents on a transaction or *quid pro quo* basis, despite its charity to some residents, it will fail to satisfy the City of Pueblo's definition.

These highly critical statements were very dangerous to the future application of local sales and use tax exemptions for both secular and religious charitable senior services organizations in Colorado. On May 15, 2009, therefore, CHI submitted a brief and asked the Supreme Court to rehear the case. The court refused to rehear the case, but in an unusual move, it did issue a revised opinion.

Under the new opinion, issued June 1, 2009, the court removed its critical comments about "retirement lifestyle" housing, and backed off the notion that a senior services organization must provide only pure charity care to obtain a tax exemption. Rather, the court noted that "the furnishing of homes to older adults is not in itself a charitable purpose" – hardly a surprise concept in light of the many for-profit organizations that deliver senior services. The court's new opinion emphasizes that to be entitled to a tax exemption, a senior services organization should meet the definition of "charitable" adopted in the 1968 United Presbyterian Association decision:

A charity, in the legal sense, may be more fully defined as a Gift, to be applied consistently with existing laws, for the benefit of an indefinite number of persons, either by bringing their minds or hearts under the influence of education or religion, by relieving their bodies from disease, suffering or constraint, by assisting them to establish themselves in life, or by erecting or maintaining public buildings or works, or otherwise lessening the burdens of government.

In this revised context, charging fees for some services “would not necessarily remove” a senior services organization from obtaining a charitable tax exemption. The key to maintaining a sales and use tax exemption under the system used by Pueblo (and in many other municipalities around Colorado) will be to avoid having a “pricing and fee structure” that indicates the “transactional, rather than charitable, nature of the services provided to residents.” Indicators of the charitable nature of an organization are that services are provided at lower cost than the services offered by for-profit enterprises; that persons who receive charitable status receive equal levels of services (e.g. equivalent apartments and levels of nursing care) to those who pay more to the organization; and that some services are provided free.

While this case is important and instructive, it is not the only story in the book. Not all Colorado communities apply the sales and use tax in the same way that Pueblo does. Each municipality may apply its tax in its own fashion so long as it provides some real tax exemption for charitable service providers under the terms of its own ordinance. And so far, the State of Colorado does not apply this type of restrictive analysis to the state property tax.

Meanwhile, the federal government recognizes a much broader tax exemption for senior services. Since 1979, the Internal Revenue Service has recognized “that the elderly as a class are proper beneficiaries of charitable activity *regardless of their income or net worth.*”<sup>1</sup> In the key IRS Revenue Ruling on this issue (Rev. Rul. 72-124), the IRS stated:

it is now generally recognized that the aged, apart from considerations of financial distress alone, are also, as a class, highly susceptible to other forms of distress in [the] sense that they have special needs because of their advanced years.

The IRS then identified specific criteria to determine that an elder care facility would be eligible for federal tax exemption “if it operates in a manner designed to satisfy the three primary needs of aged persons. These are the need for housing, the need for health care, and the need for financial security.”

Senior services organizations receive many financial benefits from tax exemption. Losing these benefits might have a serious impact upon the ability of an organization to fulfill its purposes. Therefore, CEOs, CFOs and Boards of Directors should be sure that they understand the obligations imposed upon them under their local sales and use tax ordinances, under the state property tax statute, and under federal law. Some organizations may decide that they are not able to avoid a “transactional” pricing and fee structure to garner a local sales and use tax exemption. All organizations, however, should be fully aware of the decisions they are making now at all taxing levels, and should take stock of how these decisions may affect their ability to provide charitable services in the future.