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Information Brief

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Tax Exempt Property

An Overview of Minnesota Law

This information brief outlines the Minnesota law of real property tax exemptions—the constitution, statutes, and court decisions. It is written as a basic introduction to the legal rules for legislators. It is not intended to be a legal analysis for lawyers and property tax administrators, although the endnotes provide some additional discussion and legal citations.

This is one of three information briefs on tax exempt property in Minnesota. The other briefs are *Tax Exempt Property: Natural Resources In Lieu Payments* and *Tax Exempt Property: 1992 Market Values by County*.

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Types of Exempt Property

Minnesota law grants real property tax exemptions in three ways.

- ▶ **Constitutionally mandated exemptions**—The constitution requires these exemptions.
- ▶ **Constitutionally presumptive exemptions**—The constitution provides these exemptions, but the legislature could limit or completely eliminate them.
- ▶ **Statutory exemptions**—These exemptions are granted by legislation.

The legislature has no power to alter the constitutionally mandated exemptions.

Three types of property have a constitutionally guaranteed exemption from property taxation.

- ▶ churches and houses of worship
- ▶ private and public schools and higher education institutions¹
- ▶ property exempted by federal law, such as U.S. government property, Indian lands, and certain public housing

Limiting, restricting or repealing these exemptions would require a state constitutional amendment in the case of churches and schools or federal legislation for United States government property, Indian lands, and public housing.

The constitution prescribes additional property tax exemptions, but authorizes the legislature to limit or completely eliminate these exemptions.

These presumptive constitutional exemptions include the following.

- ▶ church property (other than houses of worship)
- ▶ institutions of purely public charity
- ▶ property owned by a governmental entity and used exclusively for a public purpose²
- ▶ public hospitals
- ▶ public burying grounds³

Some specific examples of these types of exempt property include parsonages, nonprofit art museums, nonprofit theaters, state and local government lands and buildings (other than schools), and school property not used solely for educational purposes.

The exemption for institutions of purely public charity has, perhaps, been the most heavily litigated issue involving exempt property. This exemption embraces properties as diverse as theaters, museums, concert halls, nursing homes, and chemical dependency treatment facilities. The Minnesota Supreme Court has developed a set of six factors as a guide to whether property qualifies as an institution of purely public charity.

- ▶ Is the purpose of the undertaking to help others without immediate expectation of material reward?
- ▶ Is the entity supported by gifts and donations?
- ▶ Is the "charitable" assistance provided without requiring recipients to pay?
- ▶ Is the income from the property, including gifts, used to advance the charitable purpose and not to produce a profit or surplus?
- ▶ Is the class of beneficiaries unrestricted or, if not, is the restricted class reasonably related to the charitable objective?
- ▶ Is income from the property or assets upon dissolution prohibited from becoming available to private interests?⁴

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The Minnesota Supreme Court has made it clear that these factors are only a guide. Failure to meet one or more of the factors does not disqualify a property; each case must be decided on its facts.⁵ Generally, it is very helpful if traditional charitable objectives, such as helping the poor or fostering cultural or artistic endeavors, are advanced. However, the court has not been limited by the classic definition of "charity" or "charitable"—i.e., helping the poor.

The exemption for "public hospitals" is not limited to governmentally owned hospitals, as implied by the use of the term "public." The Minnesota case law extends this exemption to private hospitals, if they provide "free access to the public without discrimination" and are not "operated for the benefit of a private individual, corporation or group of individuals."⁶ The Minnesota court has held explicitly that it is not necessary for the hospital to provide charity care to qualify for the exemption.⁷

A 1970 constitutional amendment authorized the legislature to modify or limit these presumptive constitutional exemptions, but it has rarely done so. In a couple of limited instances, the legislature limited these exemptions.⁸ All of the constitutionally presumptive exemptions and some of the constitutionally mandated exemptions are codified in statute as well.⁹ In some cases, these statutory codifications of the exemptions may actually broaden the constitutional exemptions.¹⁰

The legislature has granted a large number of purely statutory property tax exemptions.

In recent legislative sessions, it has become routine for the legislature to grant new property tax exemptions. The basic property tax exemption statute now consists of 29 separate clauses.¹¹ Most of the new exemptions are, however, very limited in scope and affect only a small amount of property. The following is a list of the pure statutory exemptions. Although not comprehensive, the list includes all of the important exemptions for real property.¹²

- pollution control property¹³
- wetlands¹⁴
- native prairie¹⁵
- emergency shelters for victims of domestic abuse, owned and sponsored by a charitable organization¹⁶
- senior citizens social centers, if approved by the city council or town board¹⁷
- hydropower facilities on publicly owned sites¹⁸
- certain satellite broadcasting facilities¹⁹
- hot water district heating facilities owned and operated by charitable organizations²⁰
- lands leased by the Department of Natural Resources for cottage and camp purposes²¹
- farm electric power distribution lines²²
- transitional housing facilities²³
- property of the Minnesota Supercomputer Center, Inc., a for profit corporation owned by the University of Minnesota and the University Foundation²⁴
- alternative energy systems²⁵
- nonprofit ice arenas and rinks²⁶

- private property leased by a school district for instructional facilities²⁷ or acquired by a local government under a lease purchase or installment sale contract and used for a public purpose.²⁸
- property of volunteer fire departments used for fire prevention and protection²⁹
- property managed and controlled by a housing and redevelopment authority³⁰

In recent years the legislature has increasingly granted property tax exemptions to advance specific, nontax related goals. The legislative practice of granting exemptions reflects an approach of using property tax exemptions to encourage investment in certain types of properties (e.g., satellite broadcasting and various alternative energy facilities), preservation of property (e.g., wetlands and native prairie), or to provide indirect subsidies for various types of private or public programs (e.g., transitional housing, senior citizens centers, and ice rinks). Many of the recently granted exemptions involve relatively minor amounts of property and, thus, shift few costs to the state or other property owners.

Federal and state programs provide in lieu payments for some types of exempt property—mainly natural resource lands—partially offsetting the lost property tax base.

By reducing local tax base, property tax exemptions shift the cost of local services to either the state or to local taxpayers. For example, the general education aid formula guarantees school districts a set amount of revenue will be raised by a specified tax rate. If the property tax base is lower, state aid increases to offset the loss. Other state formulas provide higher aid entitlements as property tax base declines. If state aid (and state taxpayers) do not compensate for property tax exemptions, local governments must shift the cost to other local taxpayers or reduce local government services.

State and federal programs make **in lieu** payments for some types of exempt property, mainly forest and other natural resource lands. These state and federal **in lieu** payments reduce or, in some cases, may actually eliminate the cost shifting effects of these property tax exemptions. For more information on these programs and the amounts of money distributed under them, see another information brief in this series, **Tax Exempt Property: Natural Resources In Lieu Payments.**

Some owners of exempt property make voluntary payments for local government services that they receive. These private **in lieu** payments tend to be isolated and involve relatively small amounts. In most instances, they compensate only for property related services, typically city services.

General Legal Rules

Exempt property must satisfy both ownership and use tests.

Most exempt property must meet both ownership and use tests. Take, for example, the exemption for governmental property. It is not sufficient for the property to be owned by a governmental entity; it also must be used for an appropriate public purpose. Thus, if governmental property is used by a private business or individual, it is taxable. Conversely, privately owned property that is leased by a governmental unit and used for a public purpose does not qualify for the exemption.³¹ These rules apply generally to any type of exempt property, such as that owned by an institution of purely public charity or other exempt entity.

Two statutes specify that property, owned by an exempt entity and used for nonexempt purposes, is taxable.

- ▶ **For profit business use rule.** If the property is used by an individual or firm in connection with a profit making business, the property is taxable as if the user owned the property.³² This tax applies regardless of the nature of the agreement (e.g., whether it is a lease or other arrangement or the duration of the permitted use). A number of special properties and circumstances are exempt from this tax, such as concessions at public parks and University of Minnesota property.³³
- ▶ **One year lease rule.** If the property is leased to an individual or entity for a term of one year or more, the property is taxed as if the lessee were the owner.³⁴

The tax imposed under these provisions is collected as provided for personal property taxes. The tax is an obligation of the lessee or user and does not become a lien on or obligation of the property which is owned by the tax exempt entity. Thus, the governmental unit or exempt entity is not at risk of losing its property for nonpayment of taxes, if the user or lessee of the property does not pay the tax.

Property tax exemptions are strictly construed by the courts.

A long established rule of statutory construction is that exemptions from tax, including property tax exemptions, are to be strictly construed.³⁵ Although the Minnesota Supreme Court frequently repeats this rule in deciding exempt property cases, the rule may be less important than one would think. The court, in many instances, has reached relatively expansive interpretations of both constitutional and statutory exemptions.

The rule of strict construction does not apply to the exemption for schools.³⁶ The rationale for this was that a broad construction of the school exemption would encourage private schools, relieving the state of public education costs.³⁷

Administrative Provisions

Owners of some types of exempt property must annually file statements of exemption with the assessor.³⁸ This requirement does not apply to properties that qualify for a constitutionally mandated exemption, property owned by governmental entities, and a number of the statutory only exemptions: shelters for victims of domestic abuse, pollution control property, leased DNR lands, hydropower facilities, transitional housing facilities, wind and solar power facilities, nonprofit ice arenas and rinks, and certain agricultural pollution control facilities.

Exempt property that is sold or otherwise converted to a taxable use before July 1 becomes taxable effective for the next taxes payable year.³⁹ Thus, if an exempt property is sold on May 1, 1994, it must pay taxes in 1995. By contrast, if the property is sold after August 1, 1994, it does not become taxable until taxes payable in 1996. The value is determined based on its value on January 2, the assessment date, and the purchaser's use or intended use of the property.

Property acquired by an exempt entity generally only qualifies for exemption effective for the next assessment year after the acquisition. An exception applies if the property is acquired by a governmental entity, an institution of purely public charity, a church, or educational institution before July 1 of the assessment year.⁴⁰

The law requires assessors to value exempt property every six years.⁴¹ The most recent assessment of exempt property was done in assessment year 1992 (the value as of January, 1992). These values do not directly affect taxes or state aid, but are primarily intended to provide information on the amount of exempt property.⁴² **Tax Exempt Property: 1992 Market Values by County**, another information brief in this series, provides an overview of the data from this assessment.

Endnotes

1. The specific constitutional language is "property used solely for educational purposes by academies, colleges, universities and seminaries of learning." Minn. Const. art X § 1. Private schools may be operated for profit and still qualify. *Ramsey County v. Stryker*, 52 Minn. 144, 53 N.W. 1133 (1892). The curricula of private elementary and secondary schools must follow that used in the public education system. See, e.g., *State v. Northwestern Preparatory School*, 249 Minn. 552, 83 N.W.2d 242 (1957)(prep school to help gain admission to military service academies did not qualify). In addition, for higher education institutions the type of education must be general in nature, not restricted to a specific or narrow subject matter. See, e.g., *American Assoc. of Cereal Chemists v. County of Dakota*, 454 N.W.2d 912 (Minn. 1990)(courses in cereal chemistry too narrow).
2. U.S. government property and Indian lands cannot be taxed under federal law.
3. Public burying grounds may be operated on a for profit basis and still be exempt. *Application of Grandview Park Cemetery Assoc. v. City of Edina*, 257 N.W.2d 339 (Minn. 1977). Public burying grounds and schools are the only types of for profit properties that qualify for exemption under the constitution.
4. See, e.g., *North Star Research Institute v. County of Hennepin*, 306 Minn. 1, 236 N.W.2d 754 (1975).
5. *Mayo Foundation v. Commissioner of Revenue*, 306 Minn. 25, 236 N.W.2d 767 (1973).
6. *State v. Browning*, 192 Minn. 25, 28, 29, 255 N.W. 254 (1934).
7. *Village of Hibbing v. Commissioner of Taxation*, 217 Minn. 529, 14 N.W.2d 923 (1944).
8. One instance in which the legislature restricted a constitutional presumptive exemption relates to nonprofit low income housing. The legislature essentially reversed a Supreme Court decision in *Rio Vista Non-Profit Housing Corp. v. County of Ramsey*, 277 N.W.2d 187 (Minn. 1979). It was not clear whether this decision construed the constitution or statutory codification of the constitutional exemption, since the language is identical. See Minn. Stat. § 272.02, subd. 1(6) (1992). In another instance, the legislature specifically excluded from the exemption hospital property used for a "recreational or rest area" for hospital employees or medical personnel. Minn. Stat. § 272.02, subd. 3 (1992).
9. Compare, e.g., Minn. Const. art X § 1 with Minn. Stat. § 272.02, subd. 1, clauses (1) to (7).
10. One instance where this may have occurred is with regard to Indian lands. The state statute simply provides that "Indian lands" are exempt. Minn. Stat. § 272.011, subd. 3(d) (1992). Under federal law, generally only trust lands are exempt. These lands are held in the name of the United States "in trust" for the Indian tribe. Other lands owned by tribes, tribal corporations, or individual tribal members, although in Indian country, need not be exempt under federal law. However, the state statute may, in fact, exempt some of this property. The issue has not been litigated. It is also possible that the constitution's presumptive exemption for public property used exclusively for a public purpose would exempt non-trust tribal lands in some instances, even though this may not be required by federal law.
11. Minn. Stat. § 272.02, subd. 1 (1993 Suppl.), as amended.
12. Most personal property is exempt from taxation, except certain utility property. See generally Minn. Stat. § 272.02, subd. 1(8) (1993 Suppl.).
13. Minn. Stat. § 272.02, subd. 1(9), (22), and (27) (1992).

14. Minn. Stat. § 272.02, subd. 1(10) (1992).
15. Minn. Stat. § 272.02, subd. 1(11) (1992).
16. Minn. Stat. § 272.02, subd. 1(12) (1992).
17. Minn. Stat. § 272.02, subd. 1(13) (1992).
18. Minn. Stat. § 272.02, subd. 1(14) (1992).
19. Minn. Stat. § 272.02, subd. 1(15) (1992).
20. Minn. Stat. § 272.02, subd. 1(16) (1992).
21. Minn. Stat. §§ 92.46, 272.02, subd. 1(17) (1992).
22. Minn. Stat. § 272.02, subd. 1(18) (1992).
23. Minn. Stat. § 272.02, subd. 1(19) (1992).
24. Minn. Stat. § 272.02, subd. 1(20) (1992). This exemption is now obsolete, since the University of Minnesota and the University Foundation have sold this corporation to a private corporation which will disqualify the Center from qualifying for a property tax exemption.
25. This includes wind energy and solar electric power systems. Minn. Stat. § 272.02, subd. 1(21) and (23) (1992).
26. Minn. Stat. § 272.02, subd. 1(24) (1992).
27. Minn. Stat. § 272.02, subd. 8 (1992).
28. 1994 Minn. Laws chapter 614 § 3, codified as Minn. Stat. § 272.02, subd. 1(28).
29. Minn. Stat. § 272.021 (1992).
30. Minn. Stat. § 272.026 (1992).
31. There are two exceptions to this rule: property leased to school districts for instructional facilities, Minn. Stat. § 272.02, subd. 8 (1992); property acquired by a city, county, town or school district under a lease purchase or installment sale contract and used for a public purpose. 1994 Minn. Laws chapter 614 § 3, codified in Minn. Stat. § 272.02, subd. 1(28).
32. Minn. Stat. § 272.01, subd. 2 (a) (1992).
33. Concessions at the following public facilities are exempt: public parks, markets, fairgrounds, port authorities, economic development authorities, municipal parking facilities, museums, stadiums, and various airport facilities. Use of these concessions by a for profit businesses does not result in property tax being imposed. Minn. Stat. § 272.01, subd. 2(b) (1992).

A number of other properties are exempt from this tax on business use of otherwise exempt property: (1) federal property on which in lieu payments equal to the taxes are made; (2) land used by utilities for transmission and distribution lines; (3) property owned by the University of Minnesota or Hamline University

(educational institutions chartered by the territorial legislature); (4) Indian lands and property owned by certain tribal corporations; (5) temporary leasing of excess highway property or leasing of highway easements; and (6) certain port properties of the Duluth Port Authority. Minn. Stat. § 272.01, subd. 3 (1992).

34. Minn. Stat. § 273.19 (1992). These one year lease rules do not apply to (1) airport property that is exempt from the business use rule; (2) Duluth port authority property exempt from the business use rule; and (3) hydropower facilities.

35. *See, e.g., United Power Assoc. v. Commissioner of Revenue*, 483 N.W.2d 74 (Minn. 1992).

36. *See the discussion in Camping & Education Foundation v. State*, 282 Minn 245, 164 N.W.2d 369, 374 fn 1 (1969)

37. *Id.*

38. Minn. Stat. § 272.025, subd. 1 (1993 Suppl.).

39. Minn. Stat. § 272.02, subd. 4(a) (1993 Suppl.).

40. *Minn. Stat. § 272.02, subd. 4(b) (1993 Suppl.)*.

41. Minn. Stat. § 273.18 (1992).

42. The value of exempt property is, however, used in the formula that distributes state aid to local fire relief associations. *See Minn. Stat. § 69.021, subd. 7 (1992)*.