

REPRESENTATIVE FOR PETITIONER:  
Robert A. Anderson, Krieg DeVault, LLP;  
Lisa M. Glenn, Krieg DeVault, LLP

REPRESENTATIVE FOR RESPONDENT:  
Mark Thiros, Cohen & Thiros

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**BEFORE THE  
INDIANA BOARD OF TAX REVIEW**

St. Margaret Mercy Healthcare	)	Petition Nos:	45-034-00-2-8-00001
Centers, Inc.	)		45-036-00-2-8-00003
	)		
Petitioner,	)		
	)	Parcel Nos.:	12-14-0176-0011
v.	)		20-13-0294-0001
	)		
Lake County Property Tax	)		
Assessment Board of Appeals	)	County:	Lake
	)	Township:	St. John
Respondent.	)		
	)	Assessment Year:	2000
	)		

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Appeal from the Final Determination of  
Lake County Property Tax Assessment Board of Appeals

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**July 8, 2008**

The Board having reviewed the facts and evidence, and having considered the issues, now finds and concludes the following:

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

### Issues

1. The issues presented for consideration by the Board are whether the offices and personal property of physicians employed by St. Margaret Mercy are wholly or partially exempt under Ind. Code § 6-1.1-10-16(a), Ind. Code § 6-1.1-10-16(h) and Ind. Code § 6-1.1-10-18.5.

### Procedural History

2. St. Margaret Mercy Healthcare Centers, Inc., (St. Margaret Mercy), filed Form 136 Applications for Property Tax Exemption with the Lake County Property Tax Assessment Board of Appeals (PTABOA) on April 8, 2000. The Lake County PTABOA issued its determinations denying the exemptions on October 12, 2005.<sup>1</sup> On November 14, 2005, Krieg DeVault, LLP, on behalf of St. Margaret Mercy, filed Form 132 Petitions for Review of Exemption, petitioning the Board to conduct an administrative review of the above petitions.

### Hearing Facts and Other Matters of Record

3. Pursuant to Ind. Code § 6-1.1-15-4, the Board held a hearing on December 11, 2007, and December 12, 2007, in Crown Point, Indiana before Ellen Yuhan, the duly designated Administrative Law Judge authorized by the Board under Ind. Code § 6-1.5-5-2.<sup>2</sup>
4. The following persons were sworn in as witnesses and presented testimony:

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<sup>1</sup> St. Margaret Mercy filed Form 136 Applications for Property Tax Exemption for personal property located on three additional parcels. St. Margaret Mercy has not yet received a Form 120 Notice of Action on Exemption from Lake County so those parcels are not at issue.

<sup>2</sup> Due to the similarity in issues, Petition Nos. 45-027-00-2-8-00003, 45-008-00-2-8-00001, 45-023-00-2-8-00010, 45-023-00-2-8-00011, 45-023-00-2-8-00012, 45-023-00-2-8-00013, 45-034-00-2-8-00001, and 45-034-00-2-8-00001 were consolidated for purposes of the hearing.

For the Petitioner:

Scott A. Bonnar, Director, Managed Service Organization, St. Margaret Mercy

Gene Diamond, Regional CEO of Sisters of St. Francis Health Services, Inc.<sup>3</sup>

Arthur W. Saunders, Partner, Witsli, LLC

Edwin Udani, D.O., Physician, St. Margaret Mercy

Kurt J. Giricz, Physician, St. Margaret Mercy

Barbara Greene, President, Franciscan Physicians Hospital

Jon. C. Peterson, President, Jon Peterson & Associates, Inc.

For the Respondent:

Sharon Fleming, Director, Non-Profit Department, Lake County Assessor's Office

Betty Wilusz, Deputy Assessor, St. John Township

5. The following exhibits were presented by the Petitioner:

Petitioner Exhibit 1 – Articles of Incorporation for St. Margaret Mercy,

Petitioner Exhibit 2 – By-laws of St. Margaret Mercy,

Petitioner Exhibit 3 – St. Margaret Mercy's 2000 Mission Statement,

Petitioner Exhibit 4 – Sisters of St. Francis Health Services, Inc., 2000 Mission Statement,

Petitioner Exhibit 5 – U. S. Conference of Catholic Bishops' Ethical and Religious Directives,

Petitioner Exhibit 6 – Sample Physician Employment Agreement,

Petitioner Exhibit 7 – Physician Employment Agreement of Dr. Edwin Udani,

Petitioner Exhibit 8 – St. Margaret Mercy Physician Practice Charity Care Policy,

Petitioner Exhibit 9 – Application for Hospital Financial Assistance,

Petitioner Exhibit 10 – 2000 Federal Poverty Guidelines,

Petitioner Exhibit 11 – Charity Review Form,

Petitioner Exhibit 12 – Charity Care Approval Letter,

Petitioner Exhibit 13 – Charity Care Denial Letter,

Petitioner Exhibit 14 – Social Accountability and Community Benefit Report,

Petitioner Exhibit 15 – Indiana State Board decision in *In The Matter of The Petition for Review of Exemption for Sisters of St. Francis Health Services, Inc d/b/a St. Francis Hospital and Health Centers*, Cause No. 95-492-41, dated September 9, 1998,

Petitioner Exhibit 16R – St. Margaret Mercy Management Services Organization, Preliminary Business Plan Draft August 1996 with attached Exhibits (Redacted),

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<sup>3</sup> Sisters of St. Francis Health Care Services, Inc. owned an interest in St. Margaret Mercy. In 2001, they merged St. Margaret Mercy into the Sisters of St. Francis Health Services, Inc.

- Petitioner Exhibit 17 – Verified Memorandum in Support of Property Tax Exemption for Calendar Year 2000 for St. Margaret Mercy Healthcare Centers, Inc., Physician Practices with attached Exhibits filed with the Lake County PTABOA on September 28, 2005,
- Petitioner Exhibit 18 – Articles of Amendment for the Catholic Health Care Continuum, Inc., dated September 30, 1991,
- Petitioner Exhibit 19 – Articles of Amendment for Catholic Health Care Continuum, Inc., effective as of October 10, 1991,
- Petitioner Exhibit 20 – Internal Revenue Service 501(c)(3) Determination Letter dated October 18, 1991, issued to Catholic Health Care Continuum, Inc.,
- Petitioner Exhibit 21 – Internal Revenue Service, Response to Request for Copy of Determination Letter dated April 28, 1992, issued to St. Margaret Mercy Healthcare Centers, Inc.,
- Petitioner Exhibit 22 – Internal Revenue Service, 501(c)(3) Annual Group Ruling on Exemption for Catholic-sponsored organizations dated June 5, 2000, and attached Official Catholic Directory,
- Petitioner Exhibit 27R – Summary of Information regarding St. Margaret Mercy Hospitals and physician practices (including admissions, revenues, payor mix, gross charges, and gross collections) (Redacted),
- Petitioner Exhibit 29BR – List of physicians (Redacted),
- Petitioner Exhibit 30 – St. Margaret Mercy Healthcare Centers, facility information,
- Petitioner Exhibit 31 – *Curriculum Vitae* of Jon C. Peterson (expert witness),
- Petitioner Exhibit 32R – Report of Jon Peterson & Associates, Inc., (Redacted),<sup>4</sup>
- Petitioner Exhibit 37 – Property Tax Record, 1995 assessment year, Parcel No. 20-13-0294-00001,
- Petitioner Exhibit 38 – Real Property Maintenance Report, 2000 Pay 2001,
- Petitioner Exhibit 39 – Business Tangible Personal Property Return – Form 103,
- Petitioner Exhibit 40 – Asset worksheet related to Form 103,
- Petitioner Exhibit 41 – Business Tangible Personal Property Return – Form 104,
- Petitioner Exhibit 42 – Application for Property Tax Exemption – Form 136 for March 1, 2000,
- Petitioner Exhibit 43 – Application for Property Tax Exemption marked “Denied”,
- Petitioner Exhibit 44 – Request for site inspection,
- Petitioner Exhibit 45 – Letter recommending denial of application,
- Petitioner Exhibit 46 – Notice of Action on Exemption Application,
- Petitioner Exhibit 47 – Petition to the Indiana Board of Tax Review for Review of Exemption – Form 132,

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<sup>4</sup> Mr. Thiros objected to the submission of Exhibit 32 because it contained exhibits that arguably could be hearsay. In addition, Mr. Thiros argued, it was duplicitous and emphasized the written evidence over the oral testimony. The ALJ over-ruled the objection.

Petitioner Exhibit 96 – Property Tax Record, 1995 assessment year, Parcel No. 12-14-0176-011,  
Petitioner Exhibit 97 – Real Property Maintenance Report – 2000 pay 2001,  
Petitioner Exhibit 98 – Personal Property Maintenance Report – 2000 pay 2001,  
Petitioner Exhibit 99 – Business Tangible Personal Property Return – Form 103,  
Petitioner Exhibit 100 – Asset worksheet related to Form 103,  
Petitioner Exhibit 101 – Business Tangible Personal Property Return – Form 104,  
Petitioner Exhibit 102 – Application for Property Tax Exemption – Form 136 for March 1, 2000,  
Petitioner Exhibit 103 – Application for Property Tax Exemption marked “Denied”,  
Petitioner Exhibit 104 – Request for site inspection,  
Petitioner Exhibit 105 – Letter recommending denial of application,  
Petitioner Exhibit 106 – Notice of Action on Exemption Application,  
Petitioner Exhibit 107 – Petition to the Indiana Board of Tax Review for Review of Exemption – Form 132,  
Petitioner Exhibit 108 – Sandy Ridge Professional Building – square footage information.

6. The following exhibit was presented by the Respondent:

Respondent Exhibit 3 – Square footage calculation for parcel 12-14-0176-011.

7. The following additional items are officially recognized as part of the record of proceedings:

Board Exhibit A – Form 132 with attachments,  
Board Exhibit B – Notice of Hearing dated June 20, 2007,  
Board Exhibit C – Notice Scheduling Preliminary Conference dated July 16, 2007,  
Board Exhibit D – Order Regarding Conduct of Exemption Hearing dated August 27, 2007,  
Board Exhibit E – Order for Pre-Hearing Briefs dated August 27, 2007,  
Board Exhibit F – Notice of Hearing dated September 28, 2007,  
Board Exhibit G – Hearing Sign-in Sheets,  
Board Exhibit H – Order for Post-Hearing Briefs dated December 14, 2007.

8. The subject properties are physicians’ offices and personal property located in Schererville and Dyer. Parcel No. 20-13-0294-0001 (Petition No. 45-036-00-2-8-00003) is the Schererville Family Medical Services office (the Schererville office) located at 13 West Lincoln Highway, Schererville, in St. John Township. Parcel No. 12-14-0176-0011 (Petition No. 45-034-00-2-8-00001) is the Dyer Family Practice office (the Dyer office) located at 840 Richard Road, Dyer, in St. John Township.

9. For 2000, the PTABOA determined the real and personal property on the parcels to be 100% taxable.
10. For 2000, the Petitioner contends the land and improvements at the Schererville office, Parcel No. 20-13-0294-0001, should be 70% exempt, while the personal property is 100% exempt; and the land and improvements at the Dyer office, Parcel No. 12-14-0176-0011, should be 65% exempt, while the personal property should be 100% exempt.

### **JURISDICTIONAL FRAMEWORK**

11. The Indiana Board is charged with conducting an impartial review of all appeals concerning: (1) the assessed valuation of tangible property; (2) property tax deductions; and (3) property tax exemptions; that are made from a determination by an assessing official or a county property tax assessment board of appeals to the Indiana board under any law. Ind. Code § 6-1.5-4-1(a). All such appeals are conducted under Ind. Code § 6-1.1-15. *See* Ind. Code § 6-1.5-4-1(b); Ind. Code § 6-1.1-15-4.

### **ADMINISTRATIVE REVIEW AND THE PETITIONER'S BURDEN**

12. A Petitioner seeking review of a determination of an assessing official has the burden to establish a prima facie case proving that the current assessment is incorrect, and specifically what the correct assessment would be. *See Meridian Towers East & West v. Washington Twp. Assessor*, 805 N.E.2d 475, 478 (Ind. Tax Ct. 2003); *see also, Clark v. State Bd. of Tax Comm'rs*, 694 N.E.2d 1230 (Ind. Tax Ct. 1998).
13. In making its case, the taxpayer must explain how each piece of evidence is relevant to the requested assessment. *See Indianapolis Racquet Club, Inc. v. Wash. Twp. Assessor*, 802 N.E.2d 1018, 1022 (Ind. Tax Ct. 2004) (“[I]t is the taxpayer's duty to walk the Indiana Board . . . through every element of the analysis”).

14. Once the Petitioner establishes a prima facie case, the burden shifts to the assessing official to rebut the Petitioner's evidence. *See American United Life Ins. Co. v. Maley*, 803 N.E.2d 276 (Ind. Tax Ct. 2004). The assessing official must offer evidence that impeaches or rebuts the Petitioner's evidence. *Id*; *Meridian Towers*, 805 N.E.2d at 479.

#### **BASIS OF EXEMPTION AND BURDEN**

15. The general rule is that all property is subject to taxation. Ind. Code § 6-1-1-2-1. The General Assembly may exempt any property used for municipal, educational, literary, scientific, religious, or charitable purposes from property taxation. Article 10, § 1 of the Constitution of Indiana. This provision is not self-enacting. The General Assembly must enact legislation granting the exemption.
16. All property receives protection, security, and services from the government, e.g., fire and police protection and public schools. These government services carry with them a corresponding obligation of pecuniary support in the form of taxation. When property is exempt from taxation, the effect is to shift the amount of taxes it would have paid to other parcels that are not exempt. *See generally, Nat'l Assoc. of Miniature Enthusiasts v. State Bd. of Tax Comm'rs*, 671 N.E. 2d 218 (Ind. Tax Ct.1996).
17. Worthwhile activity or noble purpose alone is not enough. An exemption is justified because it helps accomplish some public purpose. *Miniature Enthusiasts*, 671 N.E.2d 220 (citing *Foursquare Tabernacle Church of God in Christ v. State Board of Tax Commissioners*, 550 N.E.2d 850, 854 (Ind. Tax Ct. 1990)).
18. The taxpayer seeking exemption bears the burden of proving that the property is entitled to the exemption by showing that the property falls specifically within the statutory authority for the exemption. *Indianapolis Osteopathic Hospital, Inc. v. Dep't of Local Gov't Fin.*, 818 N.E.2d 1009 (Ind. Tax Ct. 2004); *Monarch Steel, v. State Bd. of Tax Comm'rs*, 611 N.E. 2d at 714 (Ind. Tax Ct. 1993); *Indiana Association of Seventh Day Adventists v. State Bd. of Tax Comm'rs*, 512 N.E. 2d 936, 938 (Ind. Tax Ct.1987).

## PETITIONER'S CONTENTIONS

19. The Petitioner contends the physician's offices and personal property should be exempt under Ind. Code § 6-1.1-10-16(a), Ind. Code § 6-1.1-10-16(h), and Ind. Code § 6-1.1-10-18.5, because the practices are substantially related to and supportive of the inpatient facilities and provide and support the provision of charity care and community benefits.
20. The Petitioner argues that St. Margaret Mercy operates two acute-care hospitals in Lake County, Indiana. *Pet. Pre-hearing Brief at 5*. One of the hospitals is located in Hammond (the North Campus) and the other in Dyer (the South Campus). *Id.* St. Margaret Mercy is owned by the Sisters of St. Francis Health Services, Inc., an Indiana not-for-profit corporation and exempt under 501(c)(3) of the Internal Revenue Code. *Id.* The members of Sisters of St. Francis Health Services, Inc., are sisters in the Sisters of St. Francis of Perpetual Adoration. *Id. at 5-6*. St. Margaret Mercy's mission is:

Dedicated to continuing Christ's mission, Saint Margaret Mercy Healthcare Centers is a Catholic healing community that exemplifies Gospel values by respecting life, promoting the dignity and wholeness of all those we serve, and responding to community needs within the limits of our resources through provision of a comprehensive range of quality healthcare services.

*Pet. Pre-hearing Brief at 17.*

21. In response to the Balanced Budget Act of 1997, an increasingly competitive market, and a movement toward risk reimbursement systems, St. Margaret Mercy developed a strategic plan to establish an integrated healthcare delivery system with primary care and specialty physicians. *Diamond testimony; Saunders testimony; Pet. Ex. 16R*. The focus of the strategic plan was to form a geographically broad network of employed and independent physicians so St. Margaret Mercy could provide access to care in as many communities as possible.<sup>5</sup> *Id at 1*.

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<sup>5</sup> St. Margaret Mercy identified the objectives of the strategic plan as (1) improving Lake County's community health status, with special concern for those without access to care; (2) establishing a full continuum of care in St. Margaret Mercy Healthcare Centers, Inc.  
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22. The Petitioner argues that the cost of care continues to rise and much of that cost is fixed costs, such as heating, electricity, air conditioning, cleaning and maintenance. *Diamond testimony; Saunders testimony*. Despite rising costs, the Petitioner argues, reimbursement levels are actually decreasing on a per unit of service basis. *Saunders testimony*. To make up for slimmer margins, St. Margaret Mercy had to increase volumes or go out of business. *Id.* According to Mr. Saunders, the South Campus was at risk of going out of business because its volume of patients was so low. *Id.*
  
23. By implementing the strategic plan, St. Margaret Mercy hoped to further its religious mission, establish St. Margaret Mercy as the provider of choice in its service area, establish the expertise and operating systems necessary to successfully manage care in a rapidly changing environment, and enable St. Margaret Mercy and the affiliated physicians to meet the requirements of payers and purchasers. *Diamond testimony; Saunders testimony; Pet. Ex. 16R*. In order to accomplish these goals, St. Margaret Mercy determined it must increase its market share to 40%. *Saunders testimony; Pet. Ex. 16R at 26*.
  
24. To increase its market share, the Petitioner argues, St. Margaret Mercy sought to expand its physician network to at least 40 employed primary care physicians and create a Management Services Organization (MSO) that would be capable of providing business services to employed physicians and other physicians that would be affiliated with the hospital. *Saunders testimony; Pet. Ex. 16R at 1 and 26*. In employing physicians and acquiring physician practices, St. Margaret Mercy negotiated employment contracts that required these physicians to see all patients regardless of their financial resources. *Diamond testimony; Greene testimony; Pet. Ex. 6*. In addition, the employment contracts required physicians to follow the hospital's Ethical and Religious Directives. *Id.* Finally, physicians were to refer all patients needing inpatient facilities to St. Margaret Mercy's hospitals, subject to patient and payer preference. *Id.*

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strategic alliances and joint ventures with other providers; and (3) improving Lake County residents' geographic access to care by developing a broad network of primary care physicians. *Pet. Pre-hearing Brief at 19*.

25. The major benefit to St. Margaret Mercy in acquiring the physician practices, the Petitioner argues, is the requirement that all patients seen by the employed physician needing hospital care, be referred to St. Margaret Mercy unless the hospital did not have the appropriate medical facilities, the patient objected, or an insurer did not recognize St. Margaret Mercy as a participating provider. *Diamond testimony; Pet. Ex. 6 at 7.* According to the Petitioner, St. Margaret Mercy needed these referrals to increase its inpatient volumes to fund its mission and to support the hospitals' inpatient facilities. *Diamond testimony; Saunders testimony.* In 2000, employed physicians accounted for 9.2% of all inpatient admissions at the North Campus and 21.8% at the South Campus. *Greene testimony; Pet. Ex. 27R.* In the same year, employed physicians accounted for 15.8% of all outpatient ancillary services revenues at the North Campus and 43.7% of all outpatient ancillary services revenues at the South Campus.<sup>6</sup> *Id.*
26. The Petitioner argues that it engaged Jon C. Peterson to prepare an independent economic analysis of whether the real and personal property related to certain acquired physician practices provided considerable aid to, or promoted to a considerable degree, the interests of St. Margaret Mercy's inpatient facilities. *Peterson testimony; Pet. Ex. 32R.* Mr. Peterson testified that he considered a time frame from January 1, 1998, through December 31, 2000, for his analysis. *Id.* According to Mr. Peterson, he determined the additional inpatient revenues, cost, and net profit that St. Margaret Mercy captured by rendering inpatient services to physician practice patients who were admitted to its facility. *Pet. Ex. 32R at 3.* Mr. Peterson also analyzed the outpatient laboratory revenues, costs, and net profit captured from St. Margaret Mercy's physician practice patients. *Id.* Mr. Peterson testified that this "contribution margin analysis" provides a clear picture of how much the physician practices contribute to support the high fixed costs of the inpatient facility. *Peterson testimony; Pet. Ex. 32R at 4.*
27. Mr. Peterson testified that the physician practices are financially unprofitable as stand-alone businesses and make no direct financial contribution to the hospitals. *Peterson*

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<sup>6</sup> Ancillary services consist of services such as laboratory tests, x-rays, MRIs, and physical therapy.

*testimony; Pet. Ex. 32R at 6.* According to Mr. Peterson, however, the physician practices make indirect financial contributions in the form of additional inpatient admissions and outpatient lab tests that more than offset the negative financial performance. *Id.* Mr. Peterson determined that the physician practices contributed net inpatient revenues of approximately \$14 million to \$16 million for 1998 through 2000. *Peterson testimony; Pet. Ex. 32R at 12.* This is slightly over 7% of St. Margaret Mercy's total revenues. *Id.* Mr. Peterson testified that the percentage of inpatient operating expenses covered by the contributed net inpatient margin, which in 1998, 1999, and 2000 was 38%, 27% and 5% respectively is even more compelling evidence that the physician practices support St. Margaret Mercy's inpatient facilities. *Peterson testimony; Pet. Ex. 32R at 14.*

28. Mr. Peterson also calculated the physician practices' contribution margin associated with outpatient services to be between \$1.4 and \$1.8 million per year for 1998, 1999 and 2000. *Peterson testimony; Pet. Ex. 32R at 16.* Combined with the inpatient revenues, Mr. Peterson testified, the net coverage of inpatient facility related expenses associated with the physician practices was 46.03% for 1998, 37.49% for 1999, and 15.45% for 2000. *Id.* According to Mr. Peterson, this demonstrates that the physician practices provided considerable aid to, and promoted to a considerable degree, the interests of St. Margaret Mercy's inpatient facilities. *Id.*
  
29. The Petitioner also argues that the physician practices provide and support the provision of charity care. *Diamond testimony.* According to Mr. Diamond, St. Margaret Mercy's mission is to provide care to the needy. *Diamond testimony; Pet. Ex. 8.* St. Margaret Mercy provides care at reduced cost or no cost to those who qualify in accordance with its charity care policy. *Id.* The charity care policy applies at both the inpatient institutions and at the physicians' office level. *Id.* Thus, the Petitioner argues, St. Margaret Mercy's employed physicians are required to see all patients, including those who might not otherwise have access to medical care due to their financial status. *Id.*

30. To ensure that St. Margaret Mercy's employed physicians conform to its charity care policy, St. Margaret Mercy bases the physicians' compensation on relative value units which measure productivity related to the time spent with a patient or the complexity of the case. *Diamond testimony; Udani testimony; Giricz testimony; Pet. Ex. 6.* Because the physician's compensation is based on productivity and not revenue generated, the Petitioner argues, the patient's ability or inability to pay is not relevant to the physician's income. *Id.* In fact, if a physician establishes a pattern of failure to provide such services, the physician may be terminated. *Pet. Ex. 6.*
31. As a result of its policy, the Petitioner argues, St. Margaret Mercy's physician practices see more patients on government assistance than the average physician sees. *Pet. Ex. 17 at 16.* According to the Petitioner, 21.5% of its patients were on Medicaid in 2000. *Pet. Pre-hearing Brief at 26.* The national average is 8.0%. *Id.* Further, St. Margaret Mercy's employed physicians saw fewer private pay patients than physicians in private practice. *Id.* According to the Petitioner, this shows that St. Margaret Mercy was "proving valuable and needed services to the low-income residents and the working poor of Lake County." *Id.* According to Dr. Udani, in private practice, a physician would have to be careful regarding providing medical services to patients that could not pay because of the overhead costs of practice. *Udani testimony.* As a physician employed by St. Margaret Mercy, however, he is committed to caring for indigent patients. *Id.* Dr. Giricz, likewise, testified that he provided healthcare to uninsured patients. *Giricz testimony.*
32. The Petitioner argues that the hospitals provided \$13,380,869 in benefits to the poor. *Greene testimony; Pet. Ex. 14.* According to Ms. Greene, the hospitals accepted 287 applications for charity care in 2000 and incurred \$4,781,003 in costs to deliver charity care. *Id.* St. Margaret Mercy also incurred \$8,472,810 in unreimbursed cost to provide Medicaid services. *Id.* Dr. Giricz testified regarding two specific cases wherein he treated complex cases at the Schererville office for patients without insurance or the ability to pay for their care. *Giricz testimony.* In addition, he testified that he sees

patients without insurance at his office between one and three times a week on average. *Id.*

33. In response to questioning, the Petitioner's witness admitted that St. Margaret Mercy attempts to collect all of its billing. *Greene testimony.* The Petitioner argues, however, that its unreimbursed cost for charity care is not simply bad debt. *Id.* In fact, Ms. Green testified that a tax-exempt entity cannot write off an account because a patient does not respond to attempts to collect payment for services. *Greene testimony.* Ms. Greene contends the hospital would lose its tax-exempt status if it wrote off accounts to charity without income information because it is a federal requirement to go through that process. *Id.*
34. In addition, the Petitioner argues, the hospitals provided \$12,642,618 in community benefits. *Greene testimony; Pet. Ex. 14.* Ms. Greene testified that the benefits to the community include the unpaid cost of Medicare and non-billed services such as health screenings. *Id.* Community benefits also include low or negative margin services, such as the neo-natal and the pediatric intensive care units. *Id.* The hospitals also provide education and research benefits to the community. *Id.* This includes the salaries and malpractice insurance for residents. *Id.* According to Ms. Greene, the community benefits that St. Margaret Mercy provided in 2000 totaled 11.63% of its expenses. *Id.*
35. The employed physicians also provide benefits by serving communities that had been underserved. *Greene testimony.* In implementing its strategic plan, Ms. Greene testified, St. Margaret Mercy identified its market area and put physicians in locations that needed primary care. *Id.* As an example, prior to its acquisition by the Petitioner, the Woodmar Clinic did not accept Medicaid patients, despite the clinic's location in an area that has historically been underserved by pediatricians and primary care physicians. *Pet. Ex. 17 at 11.* Presently, the clinic not only accepts Medicaid patients, but it has a pediatrician who almost exclusively sees children on the Medicaid system. *Id.*

36. The Petitioner contends the Schererville office's land and improvements should be 70% exempt. *Pet. Pre-hearing Brief*. In support of this request, the Petitioner's witness testified that approximately 30% of the building is rented to a third party. *Udani testimony*. In addition, the Petitioner contends that the personal property located at the Schererville office should be 100% exempt. *Id.* The Petitioner argues that the property is used for charitable purposes under Ind. Code § 6-1.1-10-16 to provide family practice medical treatment for patients. *Id.* Further, the Petitioner argues, a substantial number of patients from this clinic were admitted to the hospitals generating significant revenues at the hospital. *Id.*
37. The Petitioner also contends the Dyer office's land and improvements should be 65% exempt. *Pet. Pre-hearing Brief*. In addition, the Petitioner contends that its personal property located at the Dyer office should be 100% exempt. *Id.* The Petitioner argues the properties are used for charitable purposes under Ind. Code § 6-1.1-10-16 to provide family practice medical treatment for patients. *Id.* Further, a substantial number of patients from this clinic were admitted to the hospitals generating significant revenues at the hospitals. *Id.* In support of this contention, the Petitioner presented a break down of the building's usage. *Pet. Ex. 108*. The Petitioner's exhibit showed 4,176 square feet of leased area, 800 square feet of space identified as "Common/Vacant Space," and 7,920 square feet of space used by St. Margaret Mercy. *Id.* In response to the Respondent's argument, the Petitioner contends that a percentage of the common and vacant area that relates to the percentage of use by St. Margaret Mercy should be considered exempt. *Anderson argument*.

#### RESPONDENT'S CONTENTIONS

38. The Respondent contends that Ind. Code § 6-1.1-10-16(h) "does not exempt from property tax an office or a practice of a physician or group of physicians that is owned by a hospital." *Resp. Pre-hearing Brief at 2*. Thus, the Respondent argues, the physician practices at issue are excluded from exemption. *Id.* In addition, Ind. Code § 6-1.1-10-18.5(a) did not become effective until January 1, 2001. *Resp. Post-hearing Brief at 7*.

Thus, the Respondent argues, St. Margaret Mercy's petitions for exemption should be denied. *Id.*

39. The Respondent argues that the burden of proof is on the Petitioner to present substantial and reliable evidence to support its claim for exemption. *Thiros argument.* According to the Respondent, St. Margaret Mercy must show that the physician practices are either substantially related to or supportive of its inpatient facility; or, that the physician practices provide or support the provision of charity care or community benefits for the physician practices to be exempt. *Resp. Pre-hearing Brief at 2.*
40. The Respondent argues that the Indiana Tax Court, in *Methodist Hospitals, Inc. v. Lake County Property Tax Assessment Board of Appeals*, 862 N.E.2d 335 (Ind. Tax Ct. 2007), defined "inpatient facility" as the part of a hospital where patients are provided overnight accommodations, meals and medical treatment. *Resp. Pre-hearing Brief at 2.* Further, the Court found that "substantially related to or supportive of" means that the physician practices are "associated, to a considerable degree, to a hospital's inpatient facility." *Id.*
41. The Respondent argues that the physician practices at issue in this appeal must be associated "to a considerable degree, to a hospital's inpatient facility" for the properties to be exempt. *Id.* According to the Respondent, "substantially related to or supportive of" the inpatient facility requires some relationship "more substantial and meaningful" than merely referring patients to the hospitals. *Resp. Pre-hearing Brief at 3.* The Respondent contends that the Petitioner's "strategic plan" was intended to increase the inpatient and outpatient income for St. Margaret Mercy. *Resp. Post-hearing Brief at 4.* "Thus, the Strategic Plan of acquiring family practitioners' practices was only for pecuniary profit." *Id.*
42. The Respondent argues that the facts at issue here are identical to the facts in the *Methodist Hospitals* case where the Board's denial of exemption was upheld by the Indiana Tax Court. *Resp. Post-hearing Brief at 5.* According to the Respondent, Methodist's doctors were also required to refer their patients to the hospital. *Id.* The Tax

Court, however, held that “substantially related to or supportive of” the inpatient facility requires that the physicians be “substantially used to provide medical care to Methodist inpatients.” *Id.* Here, the Petitioner’s family doctors “only provided an avenue for patients to receive and pay for services at St. Margaret [Mercy] instead of some other competing facility.” *Id.* In addition, even if the referral requirement were sufficient to relate to or support St. Margaret Mercy’s hospitals, the Petitioner “provided no specific evidence of the number of referrals from any particular location for which it seeks exemption.” *Id.*

43. The Respondent also contends that St. Margaret Mercy’s “charity care policy” is insufficient to show that the physician practices provide and support charity care and community benefits. *Resp. Pre-hearing Brief at 3.* According to the Respondent, the physician practices in *Methodist Hospitals* had a similar requirement and the Board denied exemption to those facilities. *Id.*
44. Here, the Respondent argues, the employment contract between St. Margaret Mercy and the employed physicians “does not mandate that the physician provide or support the provision of charity care or community benefits.” *Resp. Post-hearing Brief at 6.* In fact, the Respondent contends, the Petitioner’s witness, Ms. Greene, admitted that St. Margaret Mercy requires all patients to sign a financial responsibility form prior to treatment and any balance owed is billed to the individual patient. *Id.*
45. While St. Margaret Mercy may have provided over \$4.7 million in charity care, the Respondent argues, that figure reflects the entire hospital system. *Resp. Post-hearing Brief at 6.* The Petitioner presented no direct evidence that any of physician practices “provides or supports the provision of charity care or provides or supports the provision of community benefits.” *Resp. Post-hearing Brief at 4.* The Respondent contends that the “family doctors employed by St. Margaret [Mercy] do not see patients knowing that they may be unable to pay for their services.” *Id. at 7.* Rather, they “see all patients that come into their office because they are required to do so by their contract.” *Id.*

Similarly, they do not refer patients to St. Margaret Mercy's inpatient facilities to receive charity medical care, "but because they must do so." *Id.*

46. The Respondent argues that even the St. Margaret Mercy hospitals failed to show that its predominant use is charitable. *Resp. Post-hearing Brief at 7.* According to the Respondent, the Petitioner's own documents "indicate that it operated at a handsome net profit for the years 1999 and 2000." *Id.*
47. Further, assuming St. Margaret Mercy met its 40% market share goal, the Respondent contends, of the 240,000 patients St. Margaret Mercy would have seen in 2000, only 315 applications for charity care were received and only 287 applications for partial or full payment were approved. *Id. at 8.* According to the Respondent, "[t]hese patients were not offered charity care up front but were given 'charity' only after they asked for it and after it was determined later that they were unable to pay their bill." *Id.* Thus, the Respondent concludes, "[t]o the extent that charity care was provided, it seems rather to have resulted indirectly from St. Margaret [Mercy]'s strategy of 'putting as many people into the funnel as possible' and simply ending up with a very small percentage of those who could not afford to pay for the services afterwards." *Id.*
48. Finally, the Respondent argues, if the Petitioner is entitled to an exemption for the physician's practice properties, St. Margaret Mercy incorrectly calculated the percentage of exempt use. *Fleming testimony; Resp. Ex. 3.* Ms. Fleming testified that the Petitioner's calculation of a 65% exemption, for land and improvements at the Dyer office is incorrect because it includes all the vacant area, which is not entitled to exemption. *Fleming testimony.* According to the Respondent, it calculated that the Dyer office would only be entitled to a 59% exemption on the land and improvements. *Resp. Ex. 3.*

## ANALYSIS OF THE ISSUES

49. Generally, non-profit hospitals maintained to “relieve the destitute and deserving” are charitable. *Indianapolis Osteopathic Hospital, Inc. v. Dep’t of Local Gov. Finance*, 818 N.E.2d 1009, 1015 (Ind. Tax Ct. 2004). Other property owned by a non-profit hospital, however, “does not automatically receive a charitable purpose exemption.” *Id.* Such properties, like the physician’s offices at issue here, must be “substantially related to or supportive of the in-patient facility of the hospital.” Ind. Code § 6-1.1-10-16(h).
50. The Indiana Tax Court in *Methodist Hospitals, Inc. v. Lake County Property Tax Assessment Board of Appeals*, 862 N.E.2d 335 (Ind. Tax Ct. 2007), determined that the “inpatient facility” in Ind. Code § 6-1.1-10-16(h) is not the “entire hospital,” but that part of a hospital where “admitted patients are provided overnight accommodations, meals and medical treatment.” 862 N.E.2d at 339. Further, the Court found that “substantially related to or supportive of” means that the physician practices are “associated, to a considerable degree, to a hospital’s inpatient facility *or* that the other property provides considerable aid to, or promotes to a considerable degree, the interests of a hospital’s inpatient facility.” *Id.* (*emphasis in original*).
51. Here, the Petitioner argues that the doctors in the physician practices are employees of the hospital, the offices are staffed by the hospital, and the billing is done by the hospital. St. Margaret Mercy considers the physician practices to be part of their integrated health care system, just like any other hospital department. They are not considered separate entities.
52. Moreover, St. Margaret Mercy acquired the physician practices as part of a strategic plan to remain competitive in the market. *Diamond testimony. Saunders testimony; Pet. Ex. 16R*. Increased costs were leading to slimmer margins. *Saunders testimony*. St. Margaret Mercy had to increase volumes or go out of business. *Id.* According to the Petitioner, St. Margaret Mercy’s south campus was actually at risk for going out of business because its volume of patients was so low. *Id.* As part of its strategic plan, the

Petitioner sought to offer a full spectrum of care in a way that guaranteed high clinical quality and affordability and provided a wide primary care physician base that preferentially used St. Margaret Mercy. *Id.* In order to ensure the preferential use of St. Margaret Mercy's facilities, the hospital negotiated employment contracts that required the employed physicians to refer their patients to St. Margaret Mercy for any necessary hospital services. *Diamond testimony; Greene testimony; Pet. Ex. 6.*

53. According to the Petitioner, employed physicians accounted for 9.2% of all inpatient admissions at St. Margaret Mercy in Hammond and 21.8% at St. Margaret Mercy in Dyer in 2000. *Greene testimony; Pet. Ex. 27R.* In addition, employed physicians accounted for 15.8% of all outpatient ancillary services revenues at St. Margaret Mercy in Hammond and 43.7% of all outpatient ancillary services revenues at St. Margaret Mercy in Dyer. *Id.*
54. In an effort to quantify the impact of the physician practices' referrals, St. Margaret Mercy submitted a contribution analysis prepared by Mr. Peterson. *Pet. Ex. 32R.* Mr. Peterson determined that the individual physician practices operate at a loss. *Id. at 6.* However, the indirect contribution of the practices was between approximately \$14 million and \$16 million for 1998 through 2000. *Peterson testimony; Pet. Ex. 32R at 12.* According to Mr. Peterson, this is slightly over 7% of St. Margaret Mercy's total revenues. *Id.* In addition, the physician practices' contributed between \$1.4 and \$1.8 million per year for 1998, 1999 and 2000 through their outpatient services. *Peterson testimony; Pet. Ex. 32R at 16.* Together, the physician practices covered between 15.45% and 46.03% of the inpatient facility related expenses for 1998, 1999 and 2000. *Id.*
55. The Petitioner submitted sufficient evidence to show that the physician practices provided considerable aid to, and promoted to a considerable degree, the interests of St. Margaret Mercy's inpatient facilities. The Petitioner showed that physician practices' referrals constituted a significant percentage of St. Margaret Mercy's inpatient patients. Further, the inpatient and outpatient contribution related to the physician's practices covered a substantial portion of the hospitals' fixed costs. Moreover, the Petitioner

showed that the ownership and use of such physician practices was necessary to the hospitals' continued viability.

56. Indiana Code § 6-1.1-10-16(h) also allows an exemption for physicians' practices if the property provides or supports the provision of charity care or community benefits. Pursuant to Indiana Code § 16-18-2-52.5 defines charity care as the "unreimbursed cost to a hospital of providing, funding, or otherwise financially supporting health care services." Similarly, community benefits are "the unreimbursed cost to a hospital of providing charity care, government sponsored indigent health care, donations, education, government sponsored program services, research, and subsidized health services." Ind. Code § 16-21-9-1.
57. Here, in accordance with its mission of providing care to the needy, St. Margaret Mercy has a charity care policy that requires the physician practices to provide care at a reduced cost or at no cost to those who qualify. *Diamond testimony; Pet. Ex. 8*. In support of this policy, St. Margaret Mercy presented the testimony of two physicians and a form employment contract showing that St. Margaret Mercy's employed physicians are required to see any and all patients who present without regard to their financial ability to pay. *Diamond testimony; Udani testimony; Giricz testimony; Pet. Ex. 6*. The employed physicians' compensation is not impacted by a patient's inability to pay and, in fact, doctors risk termination if they fail to provide patient services without regard to the patient's ability to pay or payor classification. *Id.* As a result of this policy, the physician practices provide more care to Medicaid patients than the national average and its employed physicians did not see as many privately-insured patients as their peers. *Pet. Ex. 27R*.
58. St. Margaret Mercy also submitted a Consolidated Summary of Social Accountability Expenditures that quantified the benefits to the poor and the benefits to the community provided by St. Margaret Mercy. *Pet. Ex. 14*. The Summary showed that the cost for the total benefits for the year 2000 was in excess of \$26 million. *Id.* St. Margaret Mercy calculated the cost of those benefits to be 11.65% of its total expenses. *Id.* The

Petitioner, however, did not present any information regarding the community benefits provided by the individual physician practices.

59. The statute does not specify a minimum amount of charity care and community benefit necessary to qualify for exemption. But there must be some meaningful contribution, if the purpose of tax-exempt status is to be served. The taxpayer must demonstrate that it provides “a present benefit to the general public...sufficient to justify the loss of tax revenue.” *St. Mary’s Medical Center of Evansville, Inc. v. State Board of Tax Commissioners*, 534 N.E. 2d 277, 279 (Ind. Tax Ct. 1989), *aff’d*. 571 N.E. 2d (Ind. Tax 1991) (in order to reach the conclusion that the office buildings are reasonably necessary for the maintenance of St. Mary's charitable purposes the resulting benefit from the use of the buildings must inure to the public).
60. Here, the Petitioner presented evidence that its employed physicians must accept any patients. Further, the Petitioner provided evidence of the financial contribution that the physicians’ practices make to the hospitals which would support St. Margaret Mercy’s provision of charity care and community benefits.
61. The Board therefore finds that the Petitioner presented sufficient evidence that the physicians’ practices support St. Margaret Mercy’s inpatient facility and support the hospitals’ provision of charity care financially and through patient referrals. Thus, the Board finds that the Petitioner raised a prima facie case that the Schererville office and the Dyer office are exempt under Indiana Code 6-1.1-10-16(h).
62. Once the Petitioner establishes a prima facie case, the burden shifts to the Respondent to rebut the Petitioner’s evidence. *See American United Life Ins. Co. v. Maley*, 803 N.E.2d 276 (Ind. Tax Ct. 2004).
63. The Respondent argued that the burden of proof is on the party claiming the exemption and the exemption is to be strictly construed against the Petitioner. *Thiros argument*. According to the Respondent, the facts of St. Margaret Mercy’s case are very similar to

the case presented in *Methodist Hospitals, Inc. v. Lake County Property Tax Assessment Board of Appeals*, 862 N.E.2d 335 (Ind. Tax Ct. 2007). *Resp. Post-hearing Brief at 5.* The Respondent claims that in the *Methodist* case Judge Fisher interpreted “substantially related to or supportive of the inpatient facilities” to mean substantially used to provide medical care to Methodist’s inpatients. *Id.* The Respondent argues that St. Margaret Mercy did not present any evidence that the physician practices aided, or supported, or promoted to a considerable degree the medical treatment or accommodations of any of St. Margaret’s inpatients. *Id.* The Respondent further contends that even if St. Margaret Mercy proved that the physician practices were related to or supportive of its hospitals, St. Margaret Mercy provided no specific number of referrals from any particular location. *Id.*

64. The Respondent is correct that St. Margaret Mercy shares many facts with the *Methodist* case. First, in *Methodist*, the physician practices were owned by the hospital and the physicians were employees of the hospital. Further, the employment agreements with those physicians required the physicians to provide medical care without regard to a patient’s ability to pay. The hospital also provided millions of dollars in charity care and had a community benefit program. In upholding the Board’s denial of exemption, the Tax Court held that Methodist did not present evidence showing the relationship between Methodist’s physician practices and Methodist’s inpatient facility or how those physician practices promoted the overall interests of Methodist’s inpatient facilities. 862 N.E. 2d at 339. The Tax Court found that merely providing medical services and admitting patients into Methodist’s hospitals, “without more” does not show how the physician’s practices “are substantially related to or supportive of Methodist’s inpatient facilities.” *Id.*

65. The Board does not interpret the ruling in *Methodist Hospitals* to require that the physician practices only treat patients seen in St. Margaret Mercy’s inpatient facilities, or that St. Margaret Mercy’s physician practices must predominantly treat patients that are seen in its inpatient facilities for such facilities to be exempt. A Petitioner, however, must show more than that its physician practices are employed by the hospital and are

required to admit patients to the hospital. Here, St. Margaret Mercy established that the physician practices generated significant referrals to its inpatient facilities in 2000. Moreover, the physician practices contributed substantial revenue that supported the inpatient facilities. In fact, the evidence suggests that without the patient referrals and financial contribution of the physician's practices, St. Margaret Mercy's inpatient facilities may not have remained financially viable and may not have continued to exist. Similarly, the Petitioner's evidence showed that the physician's practices lost money on their own. Therefore the primary purpose of those practices, if not the only purpose, must be to support the hospitals.

66. In addition to the physician practices' support of St. Margaret Mercy's inpatient facilities, the Petitioner also presented direct evidence that quantified the financial contribution the offices make to support St. Margaret Mercy's provision of charity care. Further, the evidence showed that those physician practices serve previously un-met or underserved needs in the community. The hospital in *Methodist* chose not to present any evidence regarding charity care or community benefits for its physician's offices. 862 N.E. 2d at 337, fn. 6.
67. Thus, while the case at bar and the *Methodist* case may be facially similar, St. Margaret Mercy presented sufficient evidence to show that the Schererville office and the Dyer office are entitled to an exemption under Indiana Code § 6-1.1-10-16(h).<sup>7</sup>
68. The Board having determined that the physician practices are substantially related to, and supportive of, the inpatient facilities and the hospital's provision of charity care, must now determine the percentage of exemption for each individual properties.
69. St. Margaret Mercy contends that 70% of the Schererville office, located at 13 West Lincoln Hwy. in Schererville (Petition No. 45-036-00-2-8-00003) is used by St. Margaret

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<sup>7</sup> The Respondent correctly observed that St. Margaret Mercy could not be considered exempt under Ind. Code § 6-1.1-10-18.5 because the statute did not take effect until January 1, 2001. *Resp. Post-hearing brief at 7*. This issue moot, however, because the Petitioner established its claim for exemption under Indiana Code § 6-1.1-10-16(h).

Mercy's employed physicians. The Respondent presented no evidence to dispute this fact. Thus, the Board finds the Schererville office's land and improvements are 70% exempt. The personal property, however, is used exclusively for St. Margaret Mercy's purposes. The Board, therefore, finds the personal property used at the Schererville office to be 100% tax exempt.

70. St. Margaret Mercy also contends that the Dyer office located at 840 Richard Road in Dyer (Petition No. 45-034-00-2-8-00001) should be 65% tax exempt. The Respondent argues that only 59% of the real property can be exempt.
71. The Petitioner argues that the Dyer office building is 12,096 square feet in area. *Pet. Ex. 108*. The Petitioner's evidence showed that 4,176 square feet of the building is leased space. The Petitioner, however, identified 800 square feet of the building as "Common/Vacant space." The Respondent argues that this common or vacant area is taxable. *Resp. Ex. 2*. The Indiana Tax Court in *Indianapolis Osteopathic Hospital* found that vacant space in the hospital's medical pavilion was not exempt. 818 N.E.2d at 1019. According to the Court, an exemption only applies to the part of a building that is "owned, occupied, and used" for charitable purposes." *Id. (emphasis in original)*. "An exempt use will not be imputed to vacant space." *Id.* Thus, the vacant space at the Schererville office is not exempt.
72. In response, the Petitioner argues that common area should be tax exempt in proportion to the percentage of the building that St. Margaret occupies and uses. The Board need not determine whether "common area" is exempt, partially exempt based on the proportion of exempt use of the building, or fully taxable, however, because the Petitioner failed to show what portion of the 800 square feet of "Common/Vacant space" was common area. Thus, the Board finds that the Dyer office is 59% exempt for the land and improvements for the 2000 assessment year. The personal property, however, is used exclusively for St. Margaret Mercy's purposes. The Board, therefore, finds the personal property used at the Dyer office to be 100% tax exempt.

## Summary of Final Determination

73. The Board determines that the real and personal property of the Schererville office, located at 13 West Lincoln Hwy. in Schererville (Petition No. 45-036-00-2-8-00003) is 70% exempt and the personal property used at the Schererville office is 100% tax exempt. Similarly, the Board finds that the real and personal property of the Dyer office located at 840 Richard Road in Dyer (Petition No. 45-034-00-2-8-00001) is 59% tax exempt and the personal property at the Dyer office is 100% exempt.

This Final Determination of the above captioned matter is issued this by the Indiana Board of Tax Review on the date first written above.

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Chairman, Indiana Board of Tax Review

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Commissioner, Indiana Board of Tax Review

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Commissioner, Indiana Board of Tax Review

### Appeal Rights -

You may petition for judicial review of this final determination under the provisions of Indiana Code § 6-1.1-15-5, as amended effective July 1, 2007, by P.L. 219-2007, and the Indiana Tax Court's rules. To initiate a proceeding for judicial review you must take the action required within forty-five (45) days of the

date of this notice. The Indiana Tax Court Rules are available on the Internet at <http://www.in.gov/judiciary/rules/tax/index.html>>. The Indiana Code is available on the Internet at <<http://www.in.gov/legislative/ic/code>>. P.L. 219-2007 (SEA 287) is available on the Internet at <<http://www.in.gov/legislative/bills/2007/SE/SE0287.1.html>>