

Allina Medical Clinics,  
Petitioner,

**FINDINGS OF FACT,  
CONCLUSIONS OF LAW and  
ORDER FOR JUDGMENT**

vs.

File No. C0-02-256  
C9-03-363  
C7-04-288

County of Meeker,  
Respondent.

Dated: February 18, 2005

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The Honorable George W. Perez, Chief Judge of the Minnesota Tax Court, heard this matter, on September 14, 15 and 16, 2004, at the Meeker County Courthouse, 325 North Sibley, Litchfield, Minnesota.

Douglas J. Carney, Attorney at Law, of the firm Hanbery, Neumeyer & Carney, PA, represented the Petitioner.

Michael J. Thompson, Meeker County Attorney, represented the Respondent.

Both parties filed post trial briefs. The matter was submitted to the Court for decision on November 18, 2004.

The issue in this case is whether the subject property, owned by Allina Medical Clinic, is exempt from real property taxation as a public hospital and/or as an institution of purely public charity.

The Court, having heard and considered the evidence adduced at the hearing, and upon all of the files, records and proceedings herein, now makes the following:

**FINDINGS OF FACT**

1. Petitioner, Allina Medical Clinic-Litchfield Clinic, (“Litchfield Clinic”) has sufficient interest in the property to maintain this petition; all statutory and jurisdictional requirements have been complied with, and the Court has jurisdiction over the subject property and the parties.
2. The Subject Property is located in the City of Litchfield, County of Meeker directly across the street from the Meeker County Memorial Hospital (“County Hospital”).<sup>1</sup> The nearest corresponding Allina Health System Hospital is in Buffalo, Minnesota, approximately 45 miles away.<sup>2</sup>
3. The Subject Property consists of physician offices; administrative offices; a waiting area; restrooms; exam rooms; three procedure rooms; two nurses’ stations; a laboratory area; and a conference room.<sup>3</sup>
4. The years at issue are for taxes payable in 2001, 2002 and 2003.
5. The number of physicians has fluctuated during the tax years at issue. Currently, there are five family physicians, an orthopedic surgeon, a general surgeon, and an internist for a total of eight.<sup>4</sup>

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<sup>1</sup> Tr. at 427-28

<sup>2</sup> Tr. at 68

<sup>3</sup> Petitioner’s Ex. 4; Tr. at 285-87

<sup>4</sup> Tr. at 326-27

6. Litchfield Clinic has general radiology equipment for basic X-rays and general routine lab equipment found in most medical offices.<sup>5</sup> There is no other diagnostic capability at the site.<sup>6</sup> The bulk of diagnostic work is done at the County Hospital.<sup>7</sup> The procedure rooms are used for minor procedures only; no general anesthesia is administered, and there are no operating rooms.<sup>8</sup> No invasive surgery is performed.<sup>9</sup> There are no overnight beds nor is any institutional care provided.<sup>10</sup>
7. Most emergency care goes to the emergency room at the County Hospital.<sup>11</sup>
8. The procedures performed in the Litchfield Clinic are basically the same procedures performed there during the last 20 years.<sup>12</sup> The Litchfield Clinic physicians perform most, if not all, of their hospital work, as discussed below, at the County Hospital.<sup>13</sup> The County Hospital provides the Litchfield Clinic physicians and their patients with the facility and nursing services required for outpatient, inpatient, and emergency care. All major functions that a hospital performs are performed at the County Hospital.<sup>14</sup>

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<sup>5</sup> Tr. at 234

<sup>6</sup> Tr. at 234; 284-85

<sup>7</sup> Tr. at 279

<sup>8</sup> Tr. at 286-88

<sup>9</sup> Tr. at 345

<sup>10</sup> Tr. at 72

<sup>11</sup> Tr. at 288

<sup>12</sup> Tr. at 290-91

<sup>13</sup> Tr. at 291

<sup>14</sup> Tr. at 344-46

9. Litchfield Clinic does not operate 24 hours a day, seven days a week; it operates on a limited schedule: Monday through Friday generally, from 8:00 a.m. to 6:00 p.m. and also on Saturday mornings.<sup>15</sup>
10. The County Hospital is a county-owned hospital. It is licensed for 38 beds. It employs 170 employees with a full-time equivalent of 120 employees. It is an acute-care hospital with 22 beds designated and staffed as follows: medical surgical beds; four critical-care beds; four birthing beds; and eight geriatric/ psychiatric beds. It is a 24 hour/7 day-a-week operation.<sup>16</sup>
11. The County Hospital provides surgical care, both inpatient and outpatient. It has a full-service laboratory (AKLEA certified);<sup>17</sup> full-service radiology department; rehabilitation services; physical-therapy services; occupational-therapy services; and cardiac-rehab services.<sup>18</sup> Diagnostic services include a full range of radiology services; low densitometry; mammography; ultrasound; an in-house CT scanner; and nuclear medicine and MRI services that come to the hospital in mobile units.<sup>19</sup>
12. The County Hospital provides a 24/7 emergency room (“ER”). The ER is staffed with RNs. The physician staff for the ER is provided by physicians from Litchfield Clinic, Affiliated Community Medical Centers (“Affiliated Clinic”), and a contract service paid for by the County

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<sup>15</sup> Tr. at 288-89

<sup>16</sup> Tr. at 424-25

<sup>17</sup> Tr. at 437

<sup>18</sup> Tr. at 425; Petitioner’s Ex. 18; Respondent’s Ex. 23

<sup>19</sup> Tr. at 438

Hospital. Since the middle of 2001, the contract physicians have staffed the ER every weeknight from 7:00 p.m. to 7:00 a.m., and weekends from Friday from 7:00 p.m. to Monday, 7:00 am.<sup>20</sup>

13. During the weekdays, the ER is staffed by physicians from both Litchfield Clinic and Affiliated Clinic on a split-call schedule.<sup>21</sup> The County Hospital compensates both clinics for the on-call availability in the total sum of \$42,000 per year. Additionally, each clinic bills patients separately for any actual ER services they perform.<sup>22</sup>
14. During the tax years at issue, the County Hospital has assisted both the Litchfield Clinic and Affiliated Clinic with physician recruitment. The same program is available to both clinics and involves splitting recruitment costs “50/50” with the clinics.<sup>23</sup>
15. Litchfield Clinic is not licensed by the Minnesota Department of Health as a hospital.<sup>24</sup>
16. Affiliated Clinic is a for-profit group entity that has clinics throughout West Central Minnesota.<sup>25</sup> The Affiliated Clinic is also located across the street from the County Hospital.<sup>26</sup>
17. Allina Medical Clinic (“AMC”) is structured as a non-profit corporation under Minn. Stat. § 317A; it has also obtained non-profit status for

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<sup>20</sup> Tr. at 425-26

<sup>21</sup> Tr. at 427

<sup>22</sup> Tr. at 428-29

<sup>23</sup> Tr. at 452

<sup>24</sup> Tr. at 207

<sup>25</sup> Tr. at 450; Respondent’s Ex. 16--21

<sup>26</sup> Tr. at 427-28

income tax purposes under 26 U.S.C. 501 (c) (3).<sup>27</sup> For the tax years at issue, AMC had its own Board Directors.

18. Litchfield Clinic is operated by AMC, which is a wholly owned subsidiary of Allina Health System (“AHS”). Both AMC and AHS are non-profit corporations under Section 501(c)(3) of the Internal Revenue Code.<sup>28</sup>

19. AMC owns and operates 42 community based clinic facilities which offer a broad array of healthcare services.<sup>29</sup> The 42 AMC facilities are not separate corporate entities, nor are they separate divisions within AMC. AMC is one entity that operates 42 clinics, including the Litchfield Clinic.

20. AMC does not maintain audited financial statements for each facility.

21. AMC receives funding through direct and indirect public support. AMC receives about \$35 million through indirect public support via its parent AHS.<sup>30</sup> This funding equals approximately 15% of AMC’s annual revenues.<sup>31</sup> AHS and its foundations receive direct public contributions, government grants and donations.<sup>32</sup>

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<sup>27</sup> Petitioner’s Ex. 11A, 11B

<sup>28</sup> Petitioner’s Ex. 1A, 5A (p.25, note #15)

<sup>29</sup> Petitioner’s Ex. 6B (Statement 22, p. 1 of 8).

<sup>30</sup> Reflects an average for the years 2001 and 2002 of Petitioner’s indirect public support, as contained within AMC’s respective Internal Revenue Service Form 990, line (b), page 1, identified as Petitioner’s Ex. 7A and 7B. The amount of indirect support for 2001 is \$31.6 million, and for 2002 is \$38.2 million.

<sup>31</sup> The percentage of annual revenues-15%- reflects Petitioner’s \$35 million of indirect public support divided by the average of the AMC 2001 and 2002 gross revenues contained with AMC’s respective Internal Revenue Service Form 990, line 2, page 1, identified as Petitioner’s Ex. 7A and 7B. The amount of gross revenues for 2001 is \$222.3 million and for 2002 is \$246.9million.

<sup>32</sup> Petitioner’s Ex. 1B, 1C.

22. AMC's annual cost of providing charity is about \$770,000.<sup>33</sup>
23. AMC offers qualifying patients a "sliding scale fee" payment option.
24. AMC provides healthcare services to public enrollees under Medicare/Medicaid.<sup>34</sup>
25. AMC develops and leads many community outreach programs in response to specific community needs. Many of the combined AHS/AMC community programs are jointly administered and funded. Allina's annual cost of providing programs and activities to build healthy communities is \$6.65 million for the years 2001, 2002 and 2003.<sup>35</sup>
26. AMC facilities generate losses. Excluding the public support from AHS, AMC annual generated losses of \$43 million for the years 2001, 2002 and 2003.<sup>36</sup> Similarly, including the indirect public support from AHS, AMC annually generated losses of \$9.7 million for 2001 and \$6.2 million for 2002.<sup>37</sup>
27. AMC as a stand-alone unit is budgeted to lose money.<sup>38</sup>

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<sup>33</sup> Tr. at 181-82. The annual estimated of \$770,000 is an average of the annual charity care data for 2003 which is \$842,000 and for 2002, which is \$698,000.

<sup>34</sup> Tr. at 440-41

<sup>35</sup> Petitioner's Ex 5A, p. 11 note 3. The cost of \$6.65 million reflects an average based on \$6.4 million for 2003 and \$6.9 million for 2002.

<sup>36</sup> The \$43 million loss reflects an average of Petitioner's losses for the years 2001 (\$47.8 million) and 2002 (\$37.8 million), which are contained within AMC's respective Internal Revenue Service Form 990's identified as Petitioner's Exhibits 7A and 7B. The AMC loss for 2001 was calculated by adding the indirect public support of \$38.1 million on line 1b on page one of Form 990 to the loss of \$9.7 million on line 18 on the same page of the Form 990. Similarly, the AMC loss for 2002 was calculated by adding the indirect public support of \$31.6 million on line 1b on page one of Form 990 to the loss of \$6.2 million on line 18 on the same page of the Form 990. The analysis demonstrates what the actual loss would have been if AHS had not made the cash infusion of indirect public support to AMC.

<sup>37</sup> Petitioner's Ex. 7A, page one, line 18; Petitioner's Ex. 7B, page one, line 18

<sup>38</sup> Tr. at 59

28. AMC has two policies for charity care: Senior Partners Care and Community Partners Care.<sup>39</sup> Under the two programs, the total dollar value of the charity care program for the Litchfield Clinic was \$4,393, covering 21 patients. The charity care program is not advertised in the local paper or radio. It is available through brochures within the Litchfield Clinic.<sup>40</sup>
29. For AMC, the total amount of charity care under these programs for year 2001 equaled a total of \$907,675<sup>41</sup> or only .4% of program service revenue.<sup>42</sup>
30. AMC is in competition with other health care providers, in fact offering discounts to prospective patients.<sup>43</sup> This policy, though written by AHS, applies to AMC.<sup>44</sup>
31. AMC is required to file its own, separate tax return from AHS.<sup>45</sup> These are the Forms 990.
32. AMC's 990 Form for 2000<sup>46</sup> showed Program Service revenue of \$203,874,148.00, Direct public support equaled only \$58,210,00, of which \$35,570,87 arose from "grants and allocations" from the public (Form 990 Statement 4). Expenses totaled \$254,099,751, of which \$157,034,309 constituted compensation (wage and benefits) to officers, directors, and employees (Form 990 Part I Lines 25, 26, 27

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<sup>39</sup> Petitioner's Ex.14A

<sup>40</sup> Tr. at 301--302

<sup>41</sup> Respondent's Ex 33

<sup>42</sup> Petitioner's Ex. 7A, line 2

<sup>43</sup> Petitioner's Ex. 14D, para. 8

<sup>44</sup> Tr. at 126-27

<sup>45</sup> Tr. at 183

<sup>46</sup> Respondent's Ex. 37



and 28). Part II Program Services expenses listed \$215,194,263 and referred to Statement 6 as the basis for these expenses. Statement 6 summarized the goal of Charity Care, Participation in Governmental Programs, Necessary Community Health Care Services and Programs to Build Healthy Communities.<sup>47</sup> Program Service expenses were not broken down as to the Litchfield Clinic.

33. AMC's 2001 Form 990<sup>48</sup> indicated that Program Service revenue equaled \$222,348,964. Direct public support was stated as \$105,638, of which only \$32,907 comprised grants and allocations (Statement 4). Indirect Public Support, consisting of contributions to AMC from AHS,<sup>49</sup> was listed as \$38,112,308. Total revenue for AMC equaled \$268,608,066. Total expenses were listed as \$278,360,596. Compensation was stated in total at 168,481,431 (Part II, Lines 25 — 28). Program Service expenses were not broken down as to the Litchfield Clinic.

34. AMC's 2002 Form 990<sup>50</sup> was the most recent tax return submitted by Litchfield Clinic. Program Service revenue was listed at \$246,947,996. Direct Public Support was listed at \$273,257. For Indirect Public Support, the AHS contribution<sup>51</sup> was \$31,612,251. Total expenses equaled \$295,420,699, of which \$176,907,168 was compensation

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<sup>47</sup> Id.

<sup>48</sup> Petitioner's Ex. 7A

<sup>49</sup> Tr. at 40- 41

<sup>50</sup> Petitioner's Ex. 7B

<sup>51</sup> Tr. at 41-42

related (Part II, Lines 25 — 26). Again, Program Service expenses were not broken down as to the Litchfield Clinic.

35. Most physicians, except for officers and managers, are compensated according to a “work relative value unit” (RVU).<sup>52</sup> Compensation is based on the productivity a physician generates.<sup>53</sup> They are compensated for the number of procedures they perform.<sup>54</sup> Additionally, physicians receive a flex allowance of 3% of their compensation.<sup>55</sup>
36. Physicians are not paid for their volunteer time to community activities.<sup>56</sup> There is no RVU established for volunteer services; it is performed by physicians “gratis.”<sup>57</sup> In establishing physician compensation, there is little consideration given to metro versus non-metro physicians; the conversion factor is the same.<sup>58</sup>
37. In addition to their salaries, managers and executives are eligible for bonuses through the Management Incentive Program.<sup>59</sup> It is based on two factors, that being whether AHS meets its financial goals and whether an employee meets their individual goals.<sup>60</sup> Bonus levels fluctuate between lower-level managers who can receive between 5% and 8% of salary, to a director level who is eligible for 12%, vice

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<sup>52</sup> Tr. at 19

<sup>53</sup> Tr. at 27

<sup>54</sup> Tr. at 80

<sup>55</sup> Tr. at 54-55

<sup>56</sup> Tr. at 292 -93

<sup>57</sup> Tr. at 334

<sup>58</sup> Tr. at 242

<sup>59</sup> Tr. at 55-56

<sup>60</sup> Tr. at 56, 58

president 25%, president at 30%, and CEO at 50%. The bonus does not depend on AMC reaching a profit, just its financial goals. Thus, for example, Ms. Condon, Vice President of Operations and Finance, received a bonus for 2002 of 25% despite AMC showing a loss.<sup>61</sup>

38. Litchfield Clinic Budget reflects the following facts:

- Gross income is reduced by “discounts” that reflect what contractual and government providers pay less than AMC’s gross fee schedule.
- AMC negotiates with insurance companies for procedural rates.
- Support Staff salaries include personnel at the Litchfield Clinic that are not a billing provider, such as managers.
- System Allocation is an expense that is assigned to the Litchfield Clinic by AHS for services it tenders. It is established solely by AHS. It is done for each of the AMC clinics.
- AMC Administration allocation is for services provided by AMC to the individual clinics.<sup>62</sup>

39. The for-profit Affiliated Clinic is listed as accepting Medicare payments.<sup>63</sup>

40. AHS is a 501(c)(3) not-for-profit corporation, exempt from federal income taxes.<sup>64</sup> Litchfield Clinic is a wholly-owned subsidiary of AHS.<sup>65</sup>

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<sup>61</sup> Tr. at 62-63

<sup>62</sup> Tr. at 75-79

<sup>63</sup> Respondent’s Ex. 35

<sup>64</sup> Petitioner’s Ex. 5A, p. 25, #15

<sup>65</sup> Petitioner’s Brief, p. 1

41. AHS provided approximately \$35 million (for 2001 \$31.6 million and for 2002 \$38.2 million) indirect public support to AMC.<sup>66</sup> Combined AHS/AMC community programs are jointly administered and funded at \$6.65 million (\$6.4 million for 2003 and \$6.9 million for 2002).<sup>67</sup>
42. Meeker County is not designated as a medically underserved area.<sup>68</sup> In 2002, it had a population of 22,644.<sup>69</sup> In 2000, 6.2%, or 1,403 persons, of Meeker County residents did not have any form of health insurance.<sup>70</sup> In 2001, the Litchfield Clinic administered a total of \$4,393 of charity care to 21 patients.<sup>71</sup>
43. Litchfield Clinic's Articles of Incorporation provide that it was formed "exclusively for charitable, scientific or educational purposes."<sup>72</sup>

### **CONCLUSIONS OF LAW**

1. Petitioner does not qualify for tax exempt status as a public hospital under Minn. Stat. § 272.02, subd. 4.
2. Petitioner does not qualify for tax exempt status as an institution of purely public charity under Minn. Stat. § 272.02, subd. 7.
3. The Meeker County Assessor's classification of the Subject Property for taxes payable in 2001, 2002 and 2003, is hereby affirmed.

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<sup>66</sup> Petitioner's Ex 7A, 7B, Petitioner's Brief p. 2

<sup>67</sup> Petitioner's Ex 5A, p. 11, #3

<sup>68</sup> Tr. at 64

<sup>69</sup> Respondent's Ex. 12

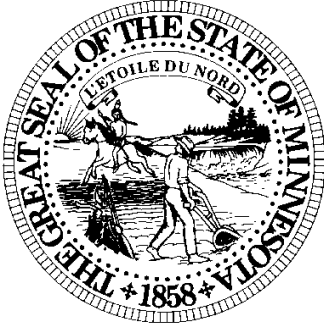
<sup>70</sup> Respondent's Ex. 11

<sup>71</sup> 2001 is the only year for which Petitioner provided these statistics.

<sup>72</sup> Petitioner's Ex. 1B

LET JUDGMENT BE ENTERED ACCORDINGLY. A STAY OF FIFTEEN DAYS IS HEREBY ORDERED. THIS IS A FINAL ORDER.

BY THE COURT,



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George W. Perez, Judge  
MINNESOTA TAX COURT

DATED: February 18, 2005

**MEMORANDUM**

The issue in this case is whether the Subject Property is exempt from real property taxes as a public hospital or as an institution of purely public charity under Minn. Stat. § 272.02, subs. 4 and 7. We find that the Subject Property is not exempt from real property taxes for the reasons set forth below.

**Facts**

Allina Medical Clinic (“AMC” or “Petitioner”) owns and operates 42 clinic facilities which offer a broad array of healthcare services.<sup>73</sup> The 42 AMC facilities are not separate corporate entities, nor are they separate divisions within AMC. AMC is one entity that operates 42 clinics, including the Litchfield Clinic (“Litchfield Clinic” or “Subject Property”).

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<sup>73</sup> Petitioner’s Ex. 6B (Statement 22, p. 1 of 8).

Petitioner's Articles of Incorporation provide that it was formed "exclusively for charitable, scientific and educational purposes."<sup>74</sup> The Litchfield Clinic is managed by a CEO, Vice President, Directors and Managers. All levels of management receive both salary and bonus compensation. The Litchfield Clinic is also under the management of the Allina Health System ("AHS") and receives grant money and management direction from AHS.

The Subject Property is located in Meeker County on parts of Block C Butler's Addition to the City of Litchfield, Meeker County, Minnesota.<sup>75</sup> The Subject Property is located directly across from the Meeker County Memorial Hospital ("County Hospital"), which is not a hospital affiliated with AHS.<sup>76</sup> The nearest hospital affiliated with AHS is located 45 miles away in Buffalo, Minnesota.<sup>77</sup>

The Subject Property is also located directly across the street from Affiliated Community Medical Center ("Affiliated Clinic") which is a for-profit clinic and part of a larger group of clinics located throughout West Central Minnesota.<sup>78</sup>

The Subject Property consists of physician offices, administrative offices, a waiting area, restrooms, exam rooms, three procedure rooms, two nurse's stations, laboratory and conference room.<sup>79</sup> The number of physicians in the Litchfield Clinic has varied; at the time of trial there were a total of eight

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<sup>74</sup> Petitioner's Ex. 1B

<sup>75</sup> Petitioner's Ex. 3A, 3B Meeker County Parcel Number 27-1241000

<sup>76</sup> MCMH is a county owned hospital managed by its own Board of Directors and reviewed by the Meeker County Board of Commissioners.

<sup>77</sup> Tr. at 34

<sup>78</sup> Tr. at 450, Respondent's Ex. 18

<sup>79</sup> Petitioner's Ex. 4

physicians.<sup>80</sup> The Litchfield Clinic has general radiology equipment for x-rays, but no other diagnostic capabilities. Almost all diagnostic work is completed at the County Hospital. There are no facilities at the Litchfield Clinic for invasive surgery or for overnight care. Therefore, all Litchfield Clinic patients requiring such care go to the County Hospital. Litchfield Clinic does not hold a hospital license, nor does it operate 24 hours a day. The Litchfield Clinic is open for general business hours Monday through Friday, with limited hours on Saturday mornings.<sup>81</sup>

The Litchfield Clinic is open to all patients and takes on urgent care matters if it has the appropriate facilities for the matter. Most extreme urgent care is admitted directly to County Hospital.<sup>82</sup> The physicians from Litchfield Clinic and from Affiliated Clinic are both scheduled to staff as on-call physicians at County Hospital. For these services County Hospital compensates both clinics a total of \$42,000<sup>83</sup> per year. All shared space and staff used by the Litchfield Clinic and by Affiliated Clinic are contracted and paid for by each clinic. County Hospital splits the cost of physician recruitment with the two neighboring clinics, Affiliated Clinic and the Litchfield Clinic.<sup>84</sup>

Litchfield Clinic operates a charitable program providing free or discounted healthcare to seniors and to persons willing but unable to pay for care. While charity care options do exist, there is little advertisement of the charity care

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<sup>80</sup> At trial, there were five family physicians, an orthopedic surgeon, a general surgeon, and an internist.

<sup>81</sup> Tr. at 288-89

<sup>82</sup> Tr. at 288

<sup>83</sup> Tr. at 428-29

<sup>84</sup> Tr. at 452

programs.<sup>85</sup> When a patient enters the clinic in a non-urgent fashion he/she will first be asked for insurance or methods of payment. If the patient is uninsured, the Litchfield Clinic will assess for government assistance. If the patient is ineligible, Litchfield Clinic will then consider providing discounted or free care.<sup>86</sup> In 2001, the Litchfield Clinic administered a total of \$4,393 of charity care to 21 patients.<sup>87</sup> In addition to free in-clinic care, Litchfield Clinic, through its association with AHS, provides free online medical information and referrals. The online service is a shared service funded by all of the Allina affiliated clinics and by AHS.

## **Analysis**

### **Qualifications for a Public Hospital Exemption**

Petitioner contends that Litchfield Clinic is tax exempt as a public hospital. For the reasons set forth below, we find that Litchfield Clinic is not exempt as a public hospital pursuant to Minn. Stat. § 272.02, subds. 1 and 4.

It is well established that since taxation is the rule and exemption is the exception, exemptions are to be strictly construed. Country Bible Church v. County of Grant, File No. C5-02- 65 (Minn. Tax Ct. June 9, 2003); Mayo Found. v. Commissioner of Revenue, 306 Minn. 25, 236 N.W.2d 767 (1975); Ideal Life Church of Lake Elmo v. County of Washington, 304 N.W.2d 308, 313 (1981); Camping & Educ. Found. v. State, 282 Minn. 245, 164 N.W.2d 369 (1969).

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<sup>85</sup> Tr. at 300-02

<sup>86</sup> Tr. at 118-19

<sup>87</sup> In 2000 approximately 1,403 persons or 6.2% of Meeker County's population of 22,644 was uninsured.



A statute creating exemption from taxation must be strictly construed and any doubt should be resolved in favor of the taxing authority. Care Inst. Inc.- Roseville v. County of Ramsey, 612 N.W 2d 443 (Minn. 2000). The burden to prove entitlement to the exemption rests with the party seeking the exemption. Id. at 372; Ideal Life Church, 304 N.W.2d at 313.

For purposes of exemption, public hospitals have been described as institutions that are “open to the public generally and . . . operated without private profit . . . it is not necessary that the hospital be owned by the public, that it dispense public charity, or render its services without charging for them.” Village of Hibbing v. Commissioner of Taxation, 217 Minn. 528, 532-33, 14 N.W.2d 923 (1944), citing State v. Browning 192 Minn. 25, 255 N.W.2d 254 (1934).

Petitioner argues that Litchfield Clinic provides services which were previously provided in hospitals, provides necessary services to the County Hospital, and has staff and patients shared with the County Hospital. Respondent argues that Petitioner does not meet the burden of proving that Litchfield Clinic is entitled to the public hospital exemption because it has not adequately demonstrated a necessary or integral relationship between AHS and the Litchfield Clinic, nor has it shown that the Litchfield Clinic, alone, can serve as a public hospital.

In the instant case, Litchfield Clinic is open to the public and renders some free services. However, Litchfield Clinic is limited in hours and in scope of services to that of a hospital. When a patient needs extreme or urgent care, Litchfield Clinic redirects the patient to the County Hospital. Litchfield Clinic also

depends on the County Hospital to provide some types of diagnostics, lab work and analysis.

In examining the evidence, it is clear that Litchfield Clinic does not perform the functions of a hospital. Petitioner contends that while it may not serve as a stand-alone hospital, it is an integral component of the AHS Hospitals.

Specifically, Petitioner argues for an application of the exemption as a property “devoted to and reasonably necessary for the accomplishment of public hospital purposes.” State v. Fairview Hosp. Ass’n, 62 Minn. 184, 187, 114 N.W.2d 568, 571 (1962). A functional interdependence test has been formulated to determine whether auxiliary facilities are reasonably necessary to what the AHS Hospital does. Chisago Health Services v. Commissioner of Revenue, 462 N.W.2d 386, 390 (Minn. 1990).<sup>88</sup>

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<sup>88</sup> In Chisago Health Services, the Supreme Court summarized the requirements for auxiliary facilities to qualify for the “hospital” exemption. They are:

- 1) The property must be devoted to and reasonably necessary for the accomplishment of public hospital purposes.
- 2) The term necessity is to be given a ‘reasonable, natural, and practical interpretation in light of modern conditions.’
- 3) The Court rejected a ‘reasonably necessary’ test based predominantly on economic necessity.
- 4) The Court applies a ‘reasonably necessary’ test in a functional sense.

Id. at 388-89.

To qualify as a “hospital,” Litchfield Clinic must either perform hospital functions or perform functions that are necessary for the AHS hospitals to function. In rejecting the economic necessity test, the court stated as follows:

The difficulty with granting tax exemption to auxiliary properties which help an exempt institution to survive or to prosper financially is two-fold. First it is difficult to know where to draw the line; almost any auxiliary facility can be found to improve the financial well being of a hospital. Secondly, these exemptions, because they are exceptions to the requirement of uniform taxation, tend to give an unfair competitive advantage to the exempted facility over similar facilities privately operated.

Moreover, if economic well-being were to be the test, the court would be required to weigh the competing economic interests of the currently

In Ridgeview Medical Center v. County of Carver, File No. C3-00-590 (Minn. Tax Ct. Oct. 25, 2001), we reviewed the services provided by an auxiliary location. These included: the existence of operating rooms, sports/ medicine rehabilitation, behavioral health facilities, and a business office that served the actual hospital. Id. at 6.

In the present case, none of these services are present. Litchfield Clinic performs essentially the same services it has for the last 20 years. There are no operating rooms, no overnight beds, no outpatient surgery, very basic and limited diagnostics. Litchfield Clinic is primarily an exam facility. Anything requiring traditional hospital services is referred to the County Hospital, a full-service, acute-care facility. Moreover, it has minimal contact with the nearest AHS Hospital, which is in Buffalo, Minnesota about 45 miles from the Litchfield Clinic.

Petitioner has presented no evidence that AHS Hospitals substantially rely on Litchfield Clinic, nor is the relationship between the County Hospital and Litchfield Clinic distinguished from its for-profit neighbor Affiliated Clinic. Both clinics contract space and rights of access at the County Hospital and are financially compensated when clinic-affiliated doctors log time at the County Hospital. The only service shared between Litchfield Clinic and the County

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volatile health care marketplace, thus placing the court in the position of legislating tax relief. . . . The legislature, with its ability to explore all issues with respect to these health care facilities, is the appropriate body to make such a determination.

Id. at 390-91.

Hospital is the cost of physician recruitment, which is also shared by Affiliated Clinic.

The Minnesota Supreme Court denied exemption to medical clinics in Chisago Health Services stating that a free standing auxiliary clinic providing little more than redistribution of the patients and practicing physicians was not exempt as a public hospital. Petitioner has failed to distinguish the Litchfield Clinic from Chisago Health Services. The Litchfield Clinic enjoys a positive business relationship with the County Hospital. However, Petitioner has failed to demonstrate that AHS Hospitals depend on Litchfield Clinic; neither has Petitioner shown that Litchfield Clinic is prepared to stand-alone or provide public hospital services.

### **Qualifications for a Purely Public Charity Exemption**

Petitioner next argues that Litchfield Clinic qualifies for an exemption from property taxation as an institution of purely public charity pursuant to Minn. Stat. § 272.02, subd. 7. For the reasons set forth below, we find that Litchfield Clinic is not exempt as an institution of purely public charity.

The Minnesota Supreme Court has articulated six factors to use in determining whether an organization's activities fall within the ambit of the purely public charity exemption:

- (1) Whether the stated purpose of the undertaking is to be helpful to others without immediate expectation of material reward;
- (2) Whether the entity involved is supported by donations and gifts in whole or in part;

- (3) Whether the recipients of the “charity” are required to pay for the assistance received in whole or in part;
- (4) Whether the income received from gifts and donations and charges to users produces a profit to the charitable institution;
- (5) Whether the beneficiaries of the “charity” are restricted or unrestricted and, if restricted, whether the class of persons to whom the charity is made available is one having a reasonable relationship to the charitable objectives;
- (6) Whether dividends, in form or substance, or assets upon dissolution are available to private interests.

North Star Research Inst. v. County of Hennepin, 236 N.W.2d 754, 757 (Minn. 1975)

Additionally, with respect to factor five, the Supreme Court has recognized a separate subfactor—whether or not the organization’s undertaking “lessens the burdens of government.” Skyline Preservation Found. v. County of Polk, 621 N.W.2d 727, 734 (Minn. 2001); White Earth Land Recovery Project v. County of Becker, 544 N.W.2d 778, 781 (Minn. 1996) (citations omitted); Worthington Dormitory, Inc. v. Commissioner of Revenue, 292 N.W.2d 276, 280 (Minn. 1980).

Finally, in applying the six-part factor North Star analysis, it is not necessary that every factor be present before an institution qualifies for the exemption. Care Inst. Inc.—Maplewood v. County of Ramsey, 576 N.W.2d 734, 738 (Minn. 1998); Mayo Found., 236 N.W.2d at 773. “Although [tax] exemptions are to be strictly construed, they should not be interpreted in a manner that frustrates the very purpose of exemption.” Skyline, 621 N.W.2d at 732. “The evident purpose of the [tax] exemption is to foster and facilitate delivery of charitable services by private institutions by exempting them from taxation.” Id.

Petitioner and Respondent disagree on all North Star factors. We, therefore, analyze each North Star factor in turn.

**Factor One: Whether the stated purpose of the undertaking is to be helpful to others without immediate expectation of material reward.**

The Court traditionally looks to Articles of Incorporation to describe the goals of the organization in determination of the stated purpose for North Star factor one. In Cook Area Health Service, Inc v. County of St. Louis, No. C6-00-100312 (Minn Tax Ct. Apr. 27, 2001), this Court stated that it “consistently interpret[s] Supreme Court decisions to mean that the first factor is satisfied if the organization has articles which state the organization’s purpose is to be helpful to others on a nonprofit basis.” Petitioner argues that its Articles of Incorporation demonstrate that it was formed “exclusively for charitable, scientific and educational purposes.” Petitioner’s Articles of Incorporation also go on to state that AMC “shall not afford pecuniary gain, incidentally or otherwise, to its members or directors, and no part of the net income or net earnings of the corporation shall inure to any member, director or individual.”<sup>89</sup>

Respondent asserts that while the Articles of Incorporation may be written to fall under factor one, in practice Petitioner fails to meet factor one. Respondent, however, provides no statute or case law to support the conclusion that North Star factor one is determined not by the stated objectives alone but also by the organization’s practice. Because Petitioner has sufficiently

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<sup>89</sup> Petitioner’s Ex. 1A

demonstrated that its Articles of Incorporation fall in line with factor one, we find Petitioner meets factor one of the North Star test.

**Factor Two: Whether the entity involved is supported by donations and gifts in whole or in part.**

To find North Star factor two, there is no amount or percentage of donations required. In Assembly Homes, Inc. v. Yellow Medicine County, 140 N.W.2d 336, 341 (Minn.1966) the Court held that even with minimal donations factor two could be met. Petitioner claims 35 million dollars over three years through indirect support from AHS. Respondent argues that the “indirect support” is akin to a write-off from a parent organization rather than a donation. At present, it is unnecessary to analyze the indirect support and eligibility as a donation because both Respondent and Petitioner agree that each year there had been some direct donation support. Respondent agrees that Petitioner received in 2000, \$58,210; in 2001, \$105, 638; and in 2002, \$273,257.<sup>90</sup> Consistent with Assembly Homes, we find Petitioner meets factor two of the North Star test.

**Factor Three: Whether the recipients of the “charity” are required to pay for the assistance received in whole or in part.**

To satisfy the third North Star factor, Petitioner must prove that Litchfield Clinic patients receive services free of charge or at considerably reduced rates. In Rio Vista Non-Profit Housing Corp. v. County of Ramsey, 277 N.W.2d 187 (Minn. 1979) and Community Memorial Home at Osakis v. County of Douglas,

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<sup>90</sup> Respondent’s Ex. 37, Petitioner’s Ex. 7A, 7B

573 N.W.2d 83, 87 (Minn. 1997) the Minnesota Supreme Court stated that the key determination is whether patients receive services at significantly less than market cost or value. Discounts that are merely good business decisions, however, do not satisfy factor three. Id. at 88 (it was more financially sound to offer a discounted rent than allow a room to be left vacant).

AMC has two policies for charity care: Senior Partners Care and Community Partners Care. Under these programs for the 2001 year, the total dollar value of charity care provided by Litchfield Clinic was \$4,393 covering 21 patients. There was no evidence submitted regarding the other two years at issue. In a county where 6.2% of its 22,644 residents do not have health insurance, a potential of 1,403 patients exists. Yet Litchfield Clinic was only able to serve 21 residents. Then we consider that AMC's total amount of charity care under these programs for the 2001 year was \$907,675 or only .4% of total program service revenue. Even when we focus only on Litchfield Clinic, \$4,393 in total charity care for one year is a fraction of its budget. Moreover, AMC is in competition with other health care providers and offers patient discounts in order to induce business.

The facts show that the majority of the patients that enter Litchfield Clinic pay for services and that all patients are first asked to pay. Charity care is not made available until all other avenues of payment are exhausted. We find that factor three of the North Star test is not met.



**Factor Four: Whether the income received from gifts and donations and charges to users produces a profit to the charitable institution.**

When examining the fourth factor of the North Star test, the question is whether an increase in net worth appears consistent with the organization's charitable goals or results from an effort to generate a profit. Volunteers of America Assisted Living v. County of Hennepin, File Nos. 24677 et al. (Minn. Tax Ct. Mar. 23, 1999) (citing Mayo Found.). Profit alone is not a bar to a finding of the fourth North Star factor. In American Ass'n of Cereal Chemists v. County of Dakota, 454 N.W.2d 912 (Minn. 1990), the Minnesota Supreme Court upheld the Tax Court's decision and found that although there were profits, the profits were used to further the charitable objectives of the association and not for private gain. Id. at 915. Also, non-profit tax IRS classification is not determinative of this issue. Id. at 914.

Litchfield Clinic is owned and operated by AMC.<sup>91</sup> AMC is its own separate corporation. AMC is required to file its own separate income tax returns.<sup>92</sup>

Petitioner argues that tax returns and budget statements show that it is consistently operating at a loss and, therefore, not profiting from revenue. Since AMC as a stand-alone business unit is budgeted to lose money, we need to look more closely at its expenses.<sup>93</sup> Also, while AMC may show a loss,<sup>94</sup> its parent

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<sup>91</sup> Petitioner's Ex. 1A

<sup>92</sup> Tr. at 183

<sup>93</sup> Tr. at 59

<sup>94</sup> See footnote 36

company AHS showed a profit of \$6,821,647 for 2001 and \$106,140,345 for 2002.<sup>95</sup>

Listed under expenses in addition to their salaries, managers and executives are eligible for bonuses through the Management Incentive Program.<sup>96</sup> It is based on two factors: whether AHS meets its financial goals and whether an employee meets their individual goals.<sup>97</sup> Bonus levels fluctuate between lower-level managers who can receive between 5% and 8% of salary, to a director level who is eligible for 12%, vice president at 25%, president at 30%, and CEO at 50%. The bonus does not depend on AMC reaching a profit, just its financial goals. Thus, for example, Ms. Condon, Vice President of Operations and Finance, received a bonus for 2002 of 25% despite AMC showing a loss.<sup>98</sup>

In addition, there are the top 100 salaries of AMC, which include both physicians and administration. For 2001, the range is from a high of \$602,742 to a low of \$204,338. For 2002, the range is from a high of \$608,272 to a low of \$201,560.<sup>99</sup>

Despite the accounting, Litchfield Clinic does receive enough revenue from paying patients to create its potential profit. Revenue is allocated to pay managers, directors and executives through extensive bonus options. The percentage of revenue allocated to salaries and bonuses far exceeds the minimal

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<sup>95</sup> Petitioner's Ex. 6A and 6B, Form 990, line 18

<sup>96</sup> Tr. at 55-56

<sup>97</sup> Tr. at 56, 58

<sup>98</sup> Tr. at 62-63

<sup>99</sup> Tr. at 129, Respondent's Ex. 10

percentage allocated to supplement charity programs and outreach. We find that Petitioner has not met North Star factor four.

**Factor Five: Whether the beneficiaries of the “charity” are restricted or unrestricted and, if restricted, whether the class of persons to whom the charity is made available is one having a reasonable relationship to the charitable objectives.**

North Star factor five examines whether the beneficiaries of the charity are restricted or unrestricted and if the charity lessens the burdens of government. The class of beneficiaries is restricted to those who are willing to pay but cannot pay. In this case, Litchfield Clinic provided charity care for 21 patients. Petitioner also contends that it provides charity care to the community through outreach programs and its Web site. However, this form of charity care is difficult to quantify. While Petitioner contends that it provides numerous educational and research programs, there is little data to show its effectiveness in reaching its intended population in Meeker County, nor is there any evidence to show how Petitioner’s programs differ from similar programs conducted by the for-profit Affiliated Clinic. Petitioner also contends that its Web site is a form of charity care to the community. While its Web site does provide free and helpful medical information, it is also a form of marketing. Increasingly, many businesses are providing Web sites, to both inform consumers and to market products. Again, there is no evidence to show that the target population has the resources to access and receive information from Petitioner’s Web site.

A sub-factor for this issue is whether Litchfield Clinic lessens the burden of government. Simply put, the charity care provided by Litchfield Clinic is available only after all governmental benefits have been procured, pursued or denied.<sup>100</sup> Petitioner's practice of first exhausting all government forms of payment before providing charity care does not lessen the burden of government. Also, Meeker County has not been identified as a medically underserved area. We find that Petitioner does not meet North Star factor five.

**Factor Six: Whether dividends, in form or substance, or assets upon dissolution are available to private interests.**

Petitioner's Articles of Incorporation restrict transfer of assets upon dissolution to charitable entities.<sup>101</sup> We find that Petitioner does meet North Star six.

**Conclusion**

We find that the Litchfield Clinic fails to sufficiently satisfy the factors under the North Star test and, therefore, does not qualify for exemption from real property taxation under Minn. Stat. § 272.02, subd. 7. We also find that the Litchfield Clinic is not exempt from real property taxes as a public hospital under Minn. Stat. § 272.02, subd. 4.

G. W. P.

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<sup>100</sup> Tr. at 118-119

<sup>101</sup> Petitioner's Ex. 1A