HOUSE
RESEARCH
ORGANIZATION bill analysis | 5/4/2005 | HB 2080
Paxton, J. Keffer

SUBJECT: Tax status of resident license fees in tax-exempt retirement communities

COMMITTEE: Ways and Means — favorable, without amendment

VOTE: 6 ayes — J. Keffer, Edwards, Paxton, Ritter, Smithee, Woolley

0 nays

3 absent — Villarreal, Grusendorf, Luna

WITNESSES: For — George Linial, Texas Association of Homes and Services for the Aging; Keith Perry, Sears Methodist Retirement System, Inc.; David Thomason, Texas Association of Homes for the Aging.

Against — Richard Petree, Taylor County Commissioners Court and Wylie ISD.

BACKGROUND: Under Tax Code, sec. 11.18, qualified charitable organizations are entitled to an exemption from taxation of personal and real property owned by the organization. A qualified charitable organization includes a retirement community providing housing and related services to persons who are 62 years of age or older. To qualify, the retirement community must provide services without regard to the residents' ability to pay or provide a minimum of 4 percent of its net resident revenue in charitable care.

Residents of retirement communities must sign a license agreement setting out the resident's obligations, including the payment of certain entry and occupancy fees. Fees for resident units range from $80,000 to $200,000, with the average being around $150,000. These fees are used to assist in financing projects in the retirement community and to cover a portion of its operating costs, including charitable care. When a resident moves out of the community, 90 percent of the fees are refunded while the remaining 10 percent pay for ongoing operating costs. The Tax Code is silent on whether or not any or all portions of these license fees are exempt from taxation.

DIGEST: HB 2080 would stipulate that a resident's leasing agreement to occupy a residence in a tax-exempt retirement community would not be considered a taxable leasehold or other possessory interest in real property for taxable property value purposes. Any fees paid by a resident under the lease agreement would not be taxable. This would apply whether or not the resident was required to pay a refundable or nonrefundable deposit or a periodic service fee under the lease.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2005.

SUPPORTERS SAY:

HB 2080 would clarify the definition of eligible exempt property to include license fees paid by residents of tax-exempt properties in retirement communities. License fees are used to fund construction costs, provide equity and bond financing, and cover a portion of charitable care. These fees are not recorded as liabilities on the organizations' books due to the contingent nature of the agreement. The agreements note that the resident's ability to receive a refund clearly is contingent upon the community's ability to remarket the resident's unit, receive fees from a new resident, and repay the existing resident. These fees do not constitute a taxable leasehold or possessory interest because the residents do not retain any title to the units in which they live. Title remains with the organization.

Unlike a homeowner who has purchased property, individuals in retirement communities do not own the units they reside in. Although residents in these communities initially may pay deposits as a condition of moving in, they pay rental fees. Taxing a resident's license agreement and fees as a possessory interest would be comparable to taxing a renter's refundable security deposit.

The license granted to a resident to occupy a unit in a retirement community is narrowly defined. The resident is allowed to occupy a unit only so long as he or she meets the obligations spelled out in the contractual agreement. A resident cannot place a lien upon the contingent contracts, cannot borrow money against the contract, and cannot sublet the unit. Neither can residents unilaterally decide how long they will reside in their units. The organization maintains control of the unit and the resident's ability to live there according to very specific guidelines spelled out in the resident's license arrangement. The organization can move the resident at its discretion based on the contract terms.

HB 2080 would not create a new class of exemption, as these retirement communities are not currently on any tax rolls. There is only one county tax assessor in the state trying to tax license fees as a taxable leasehold or possessory interest. The bill would close that loophole so that elderly residents could not be taxed on property they did not own.

Even residents in good health who choose to live in a retirement community do so with the knowledge that at some point they will need to access the health care available in the community. If a property tax were assessed on individuals who did not own property, it could inhibit them from moving into the kind of communities that offered necessary health care they eventually would need.

Currently, there are roughly 13 of these residential communities within the state. It is unlikely that the number of such communities will increase significantly in Texas because they are multi-million dollar organizations and setting up a huge campus with assisted living and nursing facilities is a complicated undertaking that involves extensive licensing requirements and a tedious process to obtain status as a tax-exempt charitable organization.

OPPONENTS SAY:

HB 2080 would grant an exemption to individuals, not charitable organizations. This tax exemption would be unfair to similarly situated individuals. An individual who purchases a comparably priced home and ultimately sells it for 92 percent of its original cost after paying closing costs and realtor fees will pay thousands of dollars in property taxes each year the individual owns the home. An individual who lives in a retirement community unit, such as a duplex or single-family dwelling, will receive approximately the same amount of money after receiving a refund for paid license fees. Under this bill, that individual would not have to pay property taxes while residing in the property.

Some organizations would take advantage of this tax exemption to create property tax shelters by establishing and funding themselves as charitable organizations. Individuals likely would flock to these communities knowing that they would not have to pay any property taxes for the rest of their lives even though they would have a possessory interest in their retirement homes. Individuals in retirement communities enjoy all the benefits that other citizens have except that they cannot buy and sell a property whenever they want or to whomever they want because the only buyer is the retirement community.

Property taxes are the major source of revenue for school districts and other local governments. Under HB 2080, millions of dollars in property value that might be taxed by local governments would be ineligible to appear on the county appraisal rolls.