

PT 04-23
Tax Type: Property Tax
Issue: Religious Ownership/Use

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

**NAPERVILLE CHURCH OF
THE BRETHREN,
APPLICANT**

v.

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

No. 03 PT 0059

Real Estate Exemption

**For 2003 Tax Year
P.I.N. 07-13-318-013**

DuPage County Parcel

**Kenneth J. Galvin
Administrative Law Judge**

RECOMMENDATION FOR DISPOSITION

APPEARANCES: Ms. Jamie Ryan, Keay & Costello, on behalf of Naperville Church of the Brethren; Mr. Robert G. Rybica, Assistant State's Attorney, on behalf of DuPage County; Mr. John Alshuler, Special Assistant Attorney General, on behalf of the Department of Revenue of the State of Illinois.

SYNOPSIS:

This proceeding raises the issue of whether a child care center located on DuPage County Parcel Index Number 07-13-318-013 (hereinafter the "subject property") qualifies for exemption from 2003 real estate taxes under 35 ILCS 200/15-40, wherein "[a]ll property used exclusively for religious purposes" is exempted from real estate taxation.

The controversy arises as follows: On March 28, 2003, Naperville Church of the Brethren (hereinafter “Naperville” or “church”) filed an Application for Property Tax Exemption for tax year 2003 with the DuPage County Board of Review (hereinafter the “Board”). Dept. Ex. No. 1. The Board reviewed the application and subsequently recommended to the Illinois Department of Revenue (hereinafter the “Department”) that Naperville be granted a full year exemption for 2003 “except for day care portion.” The Department accepted the Board’s recommendation in a determination dated June 26, 2003, finding that the “the sanctuary/balcony, library, pastor’s office, business office and the land on which they stand and a proportionate amount of the parking area is exempt.” “The remainder is taxable (property is not in exempt use).” Dept. Ex. No. 1. The “remainder” is the childcare center at issue in this case. On July 28, 2003, the applicant filed a timely request for a hearing as to the denial.

On June 9, 2004, Naperville presented evidence at a formal hearing with Ernie Thakor, Co-Chair of the Board, and Helen Hochstetter, manager of the childcare center, testifying. Following submission of all evidence and a careful review of the record, it is recommended that the childcare center located on the subject property not be exempt from real estate taxes for the 2003 tax year.

FINDINGS OF FACT:

1. Dept. Ex. No. 1 establishes the Department’s jurisdiction over this matter and its position that the childcare center was not in exempt use in 2003. Tr. p. 15; Dept Ex. No. 1.

2. Naperville started the childcare center in 1968. The center was outsourced to Jefferson Street Child Care LLC (hereinafter “Jefferson”) in 2001. Tr. pp. 18-21.
3. Jefferson is incorporated under the Illinois “Limited Liability Company Act.” Its purpose is the “[o]peration and management of one or more early learning or day care centers for children and any other lawful activity permitted within the State of Illinois.” Ms. Hochstetter, the manager of Jefferson, has owned childcare centers since 1962 and presently owns other centers in Naperville. Tr. pp. 61-64; Dept. Ex. No. 3.
4. The “Outsourcing Operating Agreement” (the “Agreement”) between Naperville and Jefferson required Jefferson to pay Naperville “fixed payments” of \$4,240/month for the first six months of 2003 and \$4,494/month for the last six months, or \$52,404 for the year 2003. Because of decreased enrollment, Jefferson was only able to pay \$48,000 in “fixed payments” for the year. The Agreement also requires Jefferson to pay quarterly, in addition to the fixed payments, “an amount equal to the positive difference (if any) between 10% of the total gross payments of cash actually received during such quarter and the sum of the fixed payments” paid for the quarter. No variable payments have yet been paid. Tr. pp. 22-24, 36-38, 46, 54; Dept. Ex. No. 2.
5. Paragraph 5 of the Agreement requires Jefferson to pay “in addition to all the other payments specified, \$1,250 per month until June 30, 2002 for the use of utilities to be supplied by the Church. These monthly payments shall then increase by 6% each year over the previous year’s required utility payments.” In 2003, Jefferson paid Naperville a total of \$15,000 for utilities. Tr. pp. 43-45; App. Ex. No. 1.

6. Paragraph 7 of the Agreement states that “[S]ubject to the reasonable approval of the Manager, the Church may include in the curriculum at its expense and with its personnel, teachings of the importance of religion and respecting religious beliefs as a part of the general curriculum.” Tr. pp. 59-60; Dept. Ex. No. 2.
7. Chapel services, conducted by Naperville’s pastor Dennis Webb, are held for children in the childcare center. Christian books are placed throughout the center. The children tell Bible stories. Tr. pp. 29, 32-33, 57.
8. No scholarships to the childcare center were given away during 2003. Tr. pp. 39-40.
9. There were 30 students enrolled in the childcare center in 2003. Tr. p. 65.

CONCLUSIONS OF LAW:

An examination of the record establishes that Naperville has not demonstrated, by the presentation of testimony, exhibits and argument, evidence sufficient to warrant an exemption of the childcare center for the 2003 tax year. In support thereof, I make the following conclusions.

Article IX, Section 6 of the Illinois Constitution of 1970 limits the General Assembly’s power to exempt property from taxation as follows:

The General Assembly by law may exempt from taxation only the property of the State, units of local government and school districts and property used exclusively for agricultural and horticultural societies, and for school, religious, cemetery and charitable purposes.

The General Assembly may not broaden or enlarge the tax exemptions permitted by the constitution or grant exemptions other than those authorized by the constitution. Board of Certified Safety Professionals v. Johnson, 112 Ill. 2d 542 (1986). Furthermore, Article

IX, Section 6 does not in and of itself, grant any exemptions. Rather, it merely authorizes the General Assembly to confer tax exemptions within the limits imposed by the constitution. Locust Grove Cemetery v. Rose, 16 Ill. 2d 132 (1959). Thus, the General Assembly is not constitutionally required to exempt any property from taxation and may place restrictions on those exemptions it chooses to grant. Village of Oak Park v. Rosewell, 115 Ill. App. 3d 497 (1st Dist. 1983).

In accordance with its constitutional authority, the General Assembly enacted section 15-40 of the Property Tax Code which exempts “[a]ll property used exclusively for religious purposes ... and not leased or otherwise used with a view to profit.” 35 ILCS 200/15-40 (1996). The Illinois Supreme Court defined the term “religious use” as follows:

As applied to the uses of property, a religious purpose means a use of such property by a religious society or persons as a stated place for public worship, Sunday schools and religious instruction.

People ex rel. McCullough v. Deutsche Evangelisch Lutherisch Jehova Gemeinde Ungeanderter Augsburgischer Confession, 249 Ill. 132, 136-137 (1911), (hereinafter “McCullough”). Property satisfies the exclusive-use requirement of the tax exemption statutes if it is primarily used for the exempted purpose, even though it may also be used for a secular or incidental purpose. McKenzie v. Johnson, 98 Ill. 2d 87, 98 (1983).

Based on the evidence and testimony presented at the evidentiary hearing, I conclude that the primary use of the property at issue in this case is as a childcare center and that this use does not further any exempt religious purpose of the Church. “Religious purpose” according to the Supreme Court’s definition in McCullough, includes the use of property for public worship, Sunday school, and religious instruction. Mr. Thakor

testified that Naperville's Pastor conducted chapel services for children at the childcare center. "There are also Christian books that are placed throughout the day care center [that] kids have access to." Tr. p. 29. Ms. Hochstetter testified that "there is definitely a daily Christian environment where even though they are only two, three, and four year olds, we do bring it down to their level through Bible stories, a prayer, the chapel by the Pastor..." Tr. p. 57.

Although the above activities seem to constitute "religious instruction" as in McCullough, the instruction is incidental to the operation of the childcare center. The Agreement between Naperville and Jefferson states that "subject to the reasonable approval of the manager, the Church may include in the curriculum at its expense and with its personnel, teachings of the importance of religion and respecting religious beliefs as a part of the general curriculum." Dept. Ex. No. 2. As the Agreement indicates, any incorporation of religious instruction into the curriculum is "subject to the reasonable approval of the manager." There was no testimony as to what constitutes "reasonable" approval. Conceivably, Ms. Hochstetter, the manager, could refuse to incorporate any religious instruction into the curriculum. I am unable to conclude that the property at issue furthers any religious purpose of the Church when the church does not have unilateral control over the curriculum. The primary use of the property at issue is for childcare. While fostering a "Christian environment" may be a worthy endeavor, it is incidental to the primary use of the property as a childcare center and therefore is not, in itself, a basis for a property tax exemption.

I also conclude from the evidentiary hearing that the property at issue is used with a view to profit and that the property does, in fact, generate a profit for Naperville. The

Church started the childcare center in 1968. Tr. p. 20. In 2001, the Church “outsourced” the day care center. Tr. p. 18. Mr. Thakor’s testimony with regard to why the childcare center was outsourced shows that the outsourcing was not done for any religious purpose, but for monetary reasons. “We were into financial difficulties... At the time that we went to outsourcing we had more than \$50,000 owed to us, that was owed to the Church at the time, and we just felt that we were getting to a situation where we had to decide to ... close it because we were unable to run it.” Tr. p. 19. Prior to outsourcing, the Church hired an administrator to oversee the childcare center “but they didn’t look after the Church’s interest and so we had at one time decided to close down the business.” Tr. pp. 19-20. “Many, many times we have had to use our own funds to keep the day school functioning, and obviously when it got to the point where we weren’t bringing in enough tuition to keep the thing, that is what led to the decision to close it down at one time.” Tr. pp. 21-22. “But then we found out about outsourcing...” Tr. p. 20.

Mr. Thakor testified repeatedly that the church did not make a profit from the center. “The Church has never made any money off of this.” Tr. p. 21. It must be noted that 35 ILCS 200/15-40 does not require that the church make a profit from the use of the property to destroy the exemption. Use of the property with a “view to profit” is sufficient to destroy the exemption. In Village of Oak Park v. Rosewell, 115 Ill. App. 3d 497 (1st Dist. 1983), the First Presbyterian Church leased its parking lot to the Village of Oak Park as a municipal parking lot. The use of the property in Oak Park was not to further any exempt religious purpose, but rather with a view to profit. The court in Oak Park stated that where property is leased with a view to profit, it is immaterial whether the income derived is used for religious purposes; in fact it is irrelevant whether the lease

actually generates a profit or a loss, or the revenues are totally offset by operational or maintenance costs. *Id.* at 500.

I conclude that the property at issue in this case was used with a “view to profit.” Mr. Thakor refers to the childcare center as a “business.” Tr. p. 20. The childcare center was outsourced because of “financial difficulties.” Tr. p. 19. It is certainly reasonable to conclude from this testimony that Naperville anticipated or “viewed” a profit from the childcare center, but because of financial difficulties, the Church was unable to make a profit. Mr. Thakor’s statement that \$50,000 was owed to the childcare center implies that if this \$50,000 had been collectible, the childcare center would have been profitable. His testimony also leads me to conclude that if there had been a sufficient number of students generating “enough tuition to keep the thing,” profit would have been anticipated. In fact, the Agreement between Jefferson and the Church calls for Jefferson to make quarterly “variable payments” equal to 10% of the gross tuition paid to Jefferson less the amounts paid as “fixed payments” to the Church.” Dept. Ex. No. 2. The “variable payments” obviously anticipate that a profit will be generated at some time. It is reasonable to conclude then that the childcare center was used with a “view to profit” in tax year 2003 when the factors negating a profit for the “business,” according to Mr. Thakor, were “financial difficulties,” the collectibility of accounts and decreasing enrollment.

35 ILCS 200/15-40 does not require that a profit be made to destroy a religious exemption. I conclude from the testimony and evidence however that the childcare center did, in fact, make a profit for Naperville and that this profit was material to Naperville’s operations. In 2001, Naperville outsourced the childcare center to Jefferson Street Child Care LLC, a limited liability company. Jefferson’s purpose, according to its Articles of

Organization, is the operation and management of childcare centers for children. Dept. Ex. No. 3. The Articles do not indicate that Jefferson has any religious purpose or association with any religion. Jefferson presently owns other childcare centers in Naperville. Tr. p. 64. It must be noted that Jefferson is a limited liability company and, unlike a not-for-profit company, anticipates a profit. When Ms. Hochstetter was asked if she knew the difference between a not-for-profit corporation and a corporation organized to make a profit, she responded that she “imagined” that Jefferson’s Articles of Organization were “filed under the possibility of making a profit.” Tr. p. 62. The Agreement between Naperville and Jefferson calls for Jefferson to “collect for its exclusive account all sums paid or payable for attendance in or use of the programs.” There were 30 students enrolled in the childcare center in 2003. Tr. p. 65. No scholarships to the childcare center were offered in 2003. Tr. pp. 39-40.

The tuition rates for students attending the childcare center are set by Jefferson. Tr. pp. 55-56, 73. Mrs. Hochstetter was not “exactly sure” as to the tuition paid by the students because of the different programs offered and the different tuition rates paid based on the age of the children. Tr. p. 65. No financial information for Jefferson was offered so I am unable to determine the gross amount of tuition revenue collected by Jefferson. No information was offered as to the salaries paid to Jefferson employees working at the childcare center. No financial information was offered as to whether Jefferson made a profit on the childcare center before remitting payments to the Church.

From the amounts Jefferson collects for tuition, Jefferson pays to the church “fixed payments” of approximately \$4,000/month. In tax year 2003, Jefferson paid the Church \$48,000 in fixed payments. Jefferson also paid the Church, as required by the

Agreement, an amount for utilities totaling \$15,000 for the year. Tr. pp. 24, 38; Dept. Ex. No. 2. In 2003, Naperville received a total of \$63,000 from the childcare center which the Church recorded in an account entitled “Income-Day School (Rent/Utilities).” App. Ex. No. 1. Naperville’s income statement for year-to-date November 2003, shows total income of \$150,778. The Church’s receipt of “rent/utilities” from Jefferson makes up 42% of its total income. The only other item of income that the Church receives that is comparable in amount to the income from the childcare center is “Income-Church Envelopes” of \$85,601 or 57% of total income.

Mr. Thakor testified repeatedly that the Church did not make a profit from the childcare center. Tr. pp. 21, 38. He also testified that maintenance of the building cost Naperville more than the \$48,000 it collected in “fixed payments” from Jefferson. Tr. p. 38. The income statement does not bear either of these contentions out. App. Ex. No. 1. “Total Church Expenses” on the income statement are \$145,314, leaving the Church with a “Net Church Profit” of \$5,464 (\$150,778 in income less \$145,314 in expenses). It must be noted that if the Church had not collected the \$63,000 from rental of the childcare center, the Church would not have had a profit, but rather a loss of approximately \$58,000.

Of the \$145,314 in Church expenses for the year, \$39,723 is for, *inter alia*, building repairs, maintenance, utilities including telephone, electric, gas and water, lawn care, disposal service and snow removal. This \$39,723 relates to the entire Church complex which consists of the sanctuary/balcony, library, pastor’s office and business office and land. Dept. Ex. No. 1. There was no testimony at the evidentiary hearing as to specifically how much of the subject property is occupied by the childcare center. If the

entire \$39,723 in expenses was attributable to the childcare center, which would seem to be a gross overestimate, then Naperville still earned a profit of \$23,277 (\$63,500 minus \$39,723) from the rental of the childcare center to Jefferson. It must be noted again that the childcare center paid \$15,000 toward the total expenses of \$39,723 in 2003. The only logical conclusion that can be drawn from the financial information admitted into evidence is that Naperville does, in fact, earn a profit from the rental and that this profit is not incidental to Naperville's operations.

Mr. Thakor testified that the rooms used for childcare are also used for Sunday school every Sunday morning, choir practice, storage, fellowship and deacon meetings and for dressing for weddings. A kitchen and furnace located in the area of the childcare center is used by both the church and the day care. Tr. pp. 27-28, 57. No evidence of square footage was offered either for the childcare area or for any of the other areas mentioned above. The childcare center operates from 7:00 a.m. to 6:00 p.m., Monday through Friday. Tr. p. 36. No testimony or evidence was offered as to the time the property at issue was used for the other church purposes. No testimony was offered as to what was stored in the area used by the childcare center. Without more detailed information as to the use of the childcare center for church purposes, I must conclude that these uses are incidental and are not the basis for an exemption of the property.

WHEREFORE, for the reasons stated above, I recommend that the Department's determination which denied an exemption to the childcare center on the grounds that it was not in exempt use should be affirmed and that the childcare center, located on DuPage County P.I.N. 07-13-318-013 should not be exempt from 2003 real estate taxes.

July 28, 2004

Kenneth J. Galvin