

**PT 11-18**  
**Tax Type: Property Tax**  
**Issue: Government Ownership/Use**

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

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**SCOTT AIR FORCE BASE  
PROPERTIES, LLC,  
APPLICANT**

v.

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

**Docket No: 08 PT 0033  
Real Estate Tax Exemption**

**For 2007 Tax Year**

**P.I.N. 09-15.4-200-005  
09-10.4-400-003  
St Clair County Parcels**

**Kenneth J. Galvin  
Administrative Law Judge**

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**RECOMMENDATION FOR DISPOSITION**

**APPEARANCES:** Mr. Michael J. Wynn and Mr. Timothy Wieher, Reed Smith, LLP, on behalf of Scott Air Force Base Properties, LLC; Mr. Gregory J. Lafakis and Ms. Ellen Berkshire, Verros, Lafakis & Berkshire, on behalf of St. Clair 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 St. Clair County Parcels, identified by P.I.N.S 09-15.4-200-005 and 09-10.4-400-003 (hereinafter the “subject property”) should be exempt from 2007 property taxes. This controversy arose as follows:

On February 25, 2008, Applicant, Scott Air Force Base Properties, (hereinafter “SAFBP”) filed Property Tax Exemption Complaints with the St. Clair County Board of Review seeking exemption from 2007 real estate taxes for the subject property, stating

that the subject property was used “for housing of [United States Air Force] military personnel and their dependents under the terms of the Lease provided herewith and as provided by federal law (Military Housing [Privatization] Initiative Act), 10 U.S.C. § 2878, *et seq.*” SAFBP applied for exemption under 35 ILCS 200/15-50 of the Property Tax Code, in which all property of the United States is exempt, “except such property as the United States has permitted or may permit to be taxed.” 35 ILCS 200/15-50.

The Board reviewed the Complaints and then assessed SAFBP’s Leasehold Interest in the two P.I.N.S under 35 ILCS 200/9-195, “Leasing of Exempt Property.” On July 10, 2008, the Department of Revenue of the State of Illinois (hereinafter the “Department”) affirmed the County’s assessment on the Leasehold Interest and denied SAFBP’s exemption request for the P.I.N.S, finding that the subject property was not in exempt ownership or exempt use in 2007. Dept. Ex. No. 1. On September 4, 2008, SAFBP filed an appeal of the Department’s decision and requested a hearing in this matter. On October 28, 2008, Mr. Lafakis and Ms. Berkshire, Special Assistant State’s Attorneys, intervened on behalf of Mr. Robert Haida, State’s Attorney of St. Clair County.

On January 13, 2010, a formal administrative hearing was held with testimony from Mr. Gary Mueller, a Licensed Surveyor in the State of Illinois, Mr. Robin Vaughn, Executive Vice President, and Ms. Paula Baker, Community Director and Asset Manager for SAFBP, testifying on behalf of SAFBP. Following a review of the testimony and evidence at the hearing, and SAFBP’s Post-Hearing Memorandum of Law (“SAFBP Memo.”), Intervenor’s Post-Hearing Brief of St. Clair County<sup>1</sup> (“Int. Response”) and SAFBP’s Post-Hearing Reply Memorandum (“SAFBP Reply”), it is recommended that

the Department's determination be reversed, and that the Leasehold Interests not be assessed in the 2007 assessment year.

**FINDINGS OF FACT:**

1. Dept. Ex. No. 1 establishes the Department's jurisdiction over this matter and its position that St. Clair County P.I.N.S 09-15.4-200-005 and 09-10.4-400-003 were not in exempt ownership or use during 2007. Tr. pp. 17-18; Dept. Ex. No. 1.
2. P.I.N. 09-15.4-200-005 consists of individual parcels described as Georgian, Maintenance Facility (a/k/a Georgian Garage), Colonial, Colonial Annex and Galaxy. P.I.N. 09-10.4-400-003 consists of individual parcels described as Shiloh West, Shiloh East and Patriots Landing. Tr. pp. 28-37; App. Ex. Nos. 1, 2 and 5.
3. In 2004, the Air Force issued a "Request for Proposal" ("RFP") which solicited proposals "from qualified entities interested in entering into a business arrangement with the Government" pursuant to the National Defense Authorization Act, subtitled The Military Housing Privatization Initiative ("MHPI"), 10 U.S.C. § 2871-2885. According to the RFP, the goal of this privatization initiative for Scott Air Force Base ("Scott AFB") was to provide military families access to safe, secure, quality, affordable, well-maintained housing in a military community where they chose to live. "Privatization will accelerate housing improvements, alleviate housing shortages, and reduce waiting times for adequate housing, ultimately improving morale of Air Force personnel." The RFP noted that "[S]ince traditional military construction

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<sup>1</sup> On April 1, 2010, the Department filed a document agreeing with and adopting the legal arguments and

[MILCON] funds are unavailable to meet this goal in a timely manner, Government officials have determined that the best solution is to use privatization to leverage available resources.” Tr. pp. 96-99, 159-162; App. Ex. No. 10.

4. Paragraph 3.2.4 of the RFP entitled “Property Taxes,” states that the Successful Offeror (“SO”) shall be responsible for the payment of any property taxes assessed on the Project. “Offeror’s proposal shall assume that property taxes will be assessed on the Project and include such costs in its financial projections.” Should tax consequences for the Project change, “the SO acknowledges that the Government will not be held responsible for the results of such changes and the SO remains responsible for any property taxes assessed.” Paragraph 3.2.4 also states that “any savings during the Project realized from an exemption from or abatement of property taxes on the Project shall be distributed pursuant to the terms of the Lockbox Agreement.” SAFBP was the SO on this Project. Tr. pp. 122-124, 133, 166-167, 214-215; App. Ex. No. 10.
5. SAFBP is a member managed LLC, the manager of which is Scott Family Housing, LLC, organized for profit, which is itself wholly owned by Hunt ELP, a Texas limited partnership, organized for profit, the managing general partner of which is HBGP, LLC, a Nevada limited liability company, organized for profit. Tr. pp. 107, 153, 155.
6. On January 1, 2006, the United States, through the Secretary of the Air Force and SAFBP executed the “Lockbox Agreement,” which controls the revenues

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position set out in the Intervenor’s “Post-Hearing Brief of St. Clair County.”

and expenditures from the Project. “Any changes in Lockbox priorities require prior written Government consent.” The Lockbox Agreement sets up several different accounts, which are funded according to an order of priority. There are two funding schedules, entitled “Transfers from Lockbox Revenue Account Prior to Completion Date [of the Project]” and “Transfers from Lockbox Revenue Account After the Completion Date.” In both of these schedules, the “Imposition Reserve Account” is the third account funded. This account covers applicable property taxes and insurance premiums. In the funding schedule for “prior to completion date” of the Project, there is no provision in the schedule for distribution of excess funds to either SAFBP or the Government. In the funding schedule for “after the completion date” of the Project, the last funding priority states that the residual balance, if any, of the Lockbox Revenue Account shall be deposited for each year of the Lease as follows: 70% to the Reinvestment Account and the remaining 30% to SAFBP. The Reinvestment Account is controlled by an “Authorized Officer of the Government.” Tr. pp. 128-132, 167-169, 210-214; App. Ex. Nos. 10 and 12.

7. Article IV of the Lockbox Agreement requires that disbursements from the Project Operating Account, Impositions Reserve Account, Replacement Reserve Account, Performance Incentive Account and Tenant Security Deposit Account shall be made pursuant to a disbursement request from an authorized officer of SAFBP. Disbursement from the Operating Reserve Account and the Insurance and Condemnation Account shall be made pursuant to a disbursement request from an authorized officer of SAFBP, approved by the construction lender, the senior lender and the Government. App. Ex. No. 12.

8. Article V of the Lockbox Agreement requires that the Government, the construction lender, the senior lender and the lockbox agent, shall be provided such access to the property and the books and records of SAFBP, as shall be reasonably necessary to permit the parties to take all necessary action to assure compliance by SAFBP with the Lockbox Agreement. App. Ex. No. 12.
9. The Lockbox Agent is GMAC Commercial Mortgage Corporation. Tr. p. 128.
10. The RFP required that at the closing of the transaction, the SO will provide “new land” for the construction of privatized housing units. The SO had to construct housing units on the new land within 10 years after the closing of the transaction. “The land will consist of no more than three parcels, all within a 10 mile radius of [Scott AFB] proper.” As part of SAFBP’s proposal, it had to put an option on a piece of land as evidence that it had control of a suitable parcel to construct 381 units. SAFBP acquired suitable property from the Heberer Brothers. This new land is owned in fee simple by SAFBP, and SAFBP has not applied for an exemption on it. Tr. pp. 114-117, 222-224; App. Ex. No. 10.
11. On January 1, 2006, the United States, through the Secretary of the Air Force and SAFBP executed a “Declaration of Restrictive Covenants and Use Agreement for Military Housing Project,” (the “Use Agreement”) which governs operation of the new land. “Recitals” at the beginning of the Use Agreement, state that the Government has agreed to provide a portion of the permanent financing, lease certain real property on Scott AFB and convey certain improvements located on such leased real property to SAFBP. “In consideration of the Government’s undertakings set out above,” SAFBP has agreed to execute and deliver this Use Agreement, for the purpose of setting

forth terms and conditions relating to SAFBP's responsibility for the demolition, design, construction, renovation, operation and maintenance of the new land. App. Ex. No. 11.

12. Paragraph 2.1 of the Use Agreement states that SAFBP declares that the Government is the intended beneficiary of this Use Agreement, and it is the intent of both parties that this Use Agreement shall constitute a covenant in favor of or for the benefit of the Government. App. Ex. No. 11.

13. Article 17 of the Use Agreement restricts and targets the tenants who may rent housing on the new land. Within 10 days following the end of each month, SAFBP must inform the Scott AFB Housing Management Office of all actual and projected vacancies. The Housing Management Office will then provide a list to SAFBP identifying any target tenants, their pay grade and the number of dependents. A target tenant is "an active duty service member and his or her family authorized to reside at Scott AFB's family housing units" or "an individual designated by the Commander as 'key and essential' and his or her family." All housing units on the new land shall be designated by pay grade and entitlement and shall be made available to target tenants and other eligible tenants. Tr. pp. 117-118, 184-187; App. Ex. No. 11.

14. SAFBP financed the Project's required construction of new housing and renovation and demolition of old housing by borrowing \$173 million senior loan from GMAC for a 40 year period. SAFBP also borrowed \$24 million from GMAC as a bridge loan. The Government then gave Scott a commitment for \$24 million to pay off GMAC's bridge loan when construction was completed. SAFBP contributed \$11 million in equity. Tr. pp. 104-106.

15. On January 1, 2006, the United States, acting by and through the Secretary of the Air Force, transferred to SAFBP, by quitclaim deed, all right, title and interest of the Government in and to certain family housing units and ancillary improvements and all personal property contained therein now existing and located at Scott AFB. The transfer is made subject to the terms and conditions of a Lease. The Quitclaim Deed states that the deed neither quitclaims nor conveys any interest in the land underlying the improvements. The Quitclaim Deed states that “Future Tax Bills” [should be sent to] SAFBP, El Paso, Texas. The Quit Claim Deed was filed and recorded with the St. Clair County Recorder of Deeds. Tr. pp. 22-28, 61-62; App. Ex. Nos. 1 and 2.
16. On January 1, 2006, the United States, acting by and through the Secretary of the Air Force, entered into a “Lease of Property” (hereinafter “Lease”) with SAFBP for land situated within the boundaries of Scott AFB. The Lease states that the Secretary, under the authority contained in The Military Housing Privatization Initiative Act, 28 U.S.C. § 2878, determined that the leasing of certain property will be advantageous to the United States and in the public interest. App. Ex. No. 3.
17. The term “Project” as used in the Lease refers to the Leased Premises, the Leased Premises Improvements (both located on Scott AFB), the new land and the improvements constructed or to be constructed on the new land. Condition 6.1 of the Lease states that the sole purpose for which the Leased Premises and the Leased Premises Improvements that are now or will be erected, in the absence of prior written approval of the Government, is for design, demolition, construction, renovation, operation and maintenance of a rental housing

development containing 1,430 units prior to completion date, and 1,593 units after completion date, primarily for use by military personnel and their dependents, authorized to live on Scott AFB. Up to 465 of the required units may be located on the new land. Condition 4.1 of the Lease requires SAFBP to pay the Government for the entire term of the Lease “nominal cash rent in the amount of \$1.” Condition 4.2 requires SAFBP to pay “additional rent” to the Government in the form of reimbursement for police and fire protection services provided by the Government. Tr. pp. 40-41, 108-110, 121-122, 144-145, 175-179; App. Ex. No. 3.

18. Condition 2.1 of the Lease states that the Government shall have the right to reserve unto itself or to grant to third parties additional easements, rights of way, licenses or other property interests with respect to the Leased Premises. Condition 6.2 of the Lease states that in no event shall the Leased Premises be used by SAFBP for any retail sales or services or commercial recreational operations or activities. Condition 13.1 of the Lease states that any agency of the United States, its officers, agents, employees and contractors may enter upon the Leased Premises and Leased Premises Improvements, at all times for any purposes not inconsistent with SAFBP’s quiet use and enjoyment under the Lease. Tr. pp. 9, 13; App. Ex. No. 3.

19. Condition 8.1 of the Lease states that the lessee shall pay to the proper authority, when due, all taxes, assessments and other charges which, during the term of the Lease, may be imposed on lessee or the Project. Each party to the Lease shall have the right to contest such taxes, assessments or other charges, and to take any action as may be necessary to contest the validity of the taxes, to

minimize such taxes, or to assert any exemption which may be available. Condition 9.1 of the Lease states that upon termination of the Lease, SAFBP shall remove all of the Leased Premises Improvements and its other property from the Leased Premises and restore the Leased Premises to the reasonable satisfaction of the Government. Condition 9.5 of the Lease states that after any demolition of the Leased Premises Improvements requested by the Government, SAFBP shall “peaceably surrender possession” of the Leased Premises to the Government upon termination of the Lease. Funds to pay for such demolition and restoration shall be obtained from the “Replacement Reserve Account,” as defined in the Lockbox Agreement. Tr. pp. 176-180, 182-184; App. Ex. No. 3.

20. Condition 15.6.1 of the Lease requires SAFBP to offer renter’s insurance, at the sole cost and expense of SAFBP, to each target tenant and other eligible tenant as part of the tenant lease application process. App. Ex. No. 3.

21. Condition 17.1.2 of the Lease requires that all housing design plans and site design plans be submitted by SAFBP to the Government for review. Condition 17.6 of the Lease states that the Government and its representatives shall have access to the Leased Premises and Leased Premises Improvements before, during and after construction of the improvements for purposes of monitoring, observing, making inquiries, and taking samples of materials for testing as may be necessary to evaluate the physical characteristics of the Leased Premises Improvements. Condition 17.9 of the Lease requires that any Leased Premises Improvements that will be demolished by SAFBP shall be demolished in accordance with a demolition plan prepared by SAFBP and approved by the Government. Condition 17.10 of the Lease requires that all matters of ingress,

gress, contractor haul routes, construction activity and disposition of excavated material shall be approved by the Government. Condition 17.12 of the Lease requires that SAFBP shall not construct any permanent structure on the Leased Premises and shall not construct any temporary structure or advertising sign on the Leased Premises or make structural modifications, alterations or additions to the Leased Premises without the prior written consent of the Government. Condition 17.18 of the Lease requires that no housing unit shall be occupied by a tenant until the Government has provided written notice to SAFBP that such housing unit may be so occupied. App. Ex. No. 3.

22. Condition 19.2 of the Lease requires that the name used by SAFBP for any portion of the Project is subject to the prior written approval of the Government. Condition 19.4 requires SAFBP to first offer to rent units to target tenants at the rates specified for those target tenants pursuant to the Rental Rate Management Plan, included in the Operating Agreement, or at a lesser amount. Condition 19.6 requires that each tenant shall be required to sign a tenant lease, in a form approved by the Government, as included in the Operating Agreement. SAFBP shall not make any “material revision” to the tenant lease without the prior written approval of the Government. Condition 19.7 requires that if the occupancy rate of the Project falls below 95%, SAFBP shall have the right to offer vacant housing to other eligible tenants at rates that are not lower or more favorable than the target rate charged to target tenants. Condition 19.9 requires that all units shall be designated by pay grade and entitlement and shall be made available to target tenants and other eligible tenants in accordance with the Unit Occupancy Plan, included in the Operating Agreement. App. Ex. No. 3.

23. Condition 21.1 of the Lease states that SAFBP shall neither transfer nor assign the Lease or any interest therein or any property on the Leased Premises, nor sublet the Leased Premises, Leased Premises Improvements or any part or any property, nor grant any license, privilege or interest, without prior written consent of the Government. Condition 26.1 of the Lease provides that, at all times during the Lease Term, the Government may inspect and request copies of any of SAFBP's records, files, reports and related material pertaining to the assets and to its performance under the Lease. Condition 26.2 requires SAFBP, at its sole expense, to create, administer and comment upon the results of an annual customer satisfaction survey comprised of content and format to be provided by the Government. SAFBP is required to use the Government's surveying company of choice to complete this task. App. Ex. No. 3.
24. Condition 27.1 of the Lease states that nothing in the Lease shall be construed to diminish limit or restrict any right, prerogative, or authority of the Commander of Scott AFB over the Leased Premises, relating to the security or mission of the Installation, the health, welfare, safety or security of persons on the Installation or the maintenance of good order and discipline on the Installation, as established in law, regulation or military custom. Condition 27.2 states that the Commander has the right at all times to order the permanent removal and "barment" of anyone from the Installation, including but not limited to tenants, if he or she believes, in his or her sole discretion, that the continued presence on the Installation of that person represents a threat to the security or mission of the Installation, poses a threat to the health, welfare, safety or security of persons

occupying the Installation or compromises good order and/or discipline on the Installation. Tr. pp. 146-147; App. Ex. No. 3.

25. The Lease specifically “incorporated into and made a part of the Lease” the Operating Agreement. The Lease provides that SAFBP shall operate the Project in accordance with each of the following plans included as attachments to the Operating Agreement: Construction Management Plan; Rental Rate Management Plan; Unit Occupancy Plan; Property Operations and Management Plan; Facilities Maintenance Plan; Capital Repair and Replacement Plan; Reinvestment Plan; Utility Services Plan; Scott AFB Housing Leases for Military/Non-Military Tenants; Community Development Plan; Fee Management Plan; Unit Design Plan; Transition Plan; Severability Plan; Quality Control Plan. App. Ex. No. 3.

26. On January 1, 2006, the United States, through the Secretary of the Air Force and SAFBP executed the “Operating Agreement,” which had been incorporated into and made a part of the Lease. The Operating Agreement controls the operational aspects of the Project from initial construction and development to who can occupy the units, the rates to be charged and maintenance of the facilities. Section 3(a) of the Operating Agreement requires that SAFBP cannot enter into any “property management agreement” or agreement with a “management company” without the prior written approval of the Government. Tr. pp. 135-136; App. Ex. No. 13.

27. On January 1, 2006, SAFBP entered into a “Management Agreement” with American Management Services Central and HBC Property Managers Limited Partnership (hereinafter the “Property Manager”) to manage the Project,

including the Leased Premises and the new land. American Management Services Central is no longer part of the management team. HBC is the sole Property Manager. Government approval was required for this change. Tr. pp. 137-138; App. Ex. No. 14.

28. Section 5(a) of the Operating Agreement states that the Leased Premises and the Leased Premises Improvements are subject to periodic inspection by Scott AFB security personnel. SAFBP will cooperate with these inspections ... to ensure that law enforcement activities are not hindered and that Scott AFB security requirements are met. Paragraph 5(b) of the Lease requires that SAFBP's officers, agents, employees, independent contractors and subcontractors, must obtain identification passes from Scott AFB police before admission to Scott AFB. Vehicles of such personnel must also be registered with and issued temporary passes by Scott AFB before they may be driven onto Scott AFB. The vehicles are subject to inspection by Scott AFB security police before temporary passes will be issued. Section 5(c) of the Operating Agreement states that the Government retains the right to refuse access to Scott AFB, including the Leased Premises, by SAFBP, its officers, agents, employees, independent contractors and subcontractors, during a national emergency, or other compelling reasons as determined by the Commander in his sole discretion. App. Ex. No. 13.

29. Attachment B of the Operating Agreement is entitled the "Rental Rate Management Plan." This Plan details how rent is going to be charged on each individual unit for various service members depending on their pay grade and housing allowance. Certain units are called "designated quarters" and only

certain people who fill essential positions are allowed to live there. “The local Air Force Commander determines those positions considered as key and essential.” Tr. pp. 146-147; App. Ex. No. 13.

30. The Rental Rate Management Plan states that if a service member is promoted and wishes to move to a new house, then the service member’s new housing allowance will apply and a new one-year lease will be signed. Resident lease agreements with tenants other than referred military members will be limited to one-year duration. In the event that the general public is offered a home in the community, the Property Manager shall first locate the resident in the most severable location in the community. The Property Manager will accept all referrals from Scott AFB’s Military Housing Office and will make available any vacant home to the appropriate grade individual at the top of the waiting list. Acceptance or rejection of the available home will be at the sole discretion of the referred military member. The Air Force reserves the right to refuse occupancy to other eligible tenants based on the result of a background check of available criminal files to determine any evidence of sex offense convictions, probation or parole for serious offenses or other credible evidence of current or past criminal misconduct. App. Ex. No. 13.

31. The Rental Rate Management Plan states that the Air Force will have unrestricted access, through use of a web-based software program, to produce reports independently, or request reports on an as-needed basis. This capability includes the ability to view receivables, payables, property data, performance records and any other functions related to property operations. The Project

Manager will hold quarterly property review meetings attended by personnel from the Air Force, *inter alia*. App. Ex. No. 13.

32. The Facilities Maintenance Plan, included in the Operating Agreement, requires that all proposed major landscape work on the Leased Premises, other than routine pruning, trimming, mowing and maintenance, be approved by the Wing Commander. App. Ex. No. 13.
33. A Wing Commander, holding the position of Colonel, is in charge of Scott AFB. Wing Commanders serve for two years. Tr. pp. 235-237.
34. On January 1, 2006 the United States, through the Secretary of the Air Force, and SAFBP executed a “Mortgage Security Agreement and Agreement to Share Proceeds,” (hereinafter “Security Agreement”) which was recorded with St Clair County. Recital B of the Security Agreement states that SAFBP and the Government have entered into one or more project documents including the Lease and the Use Agreement. Recital D states that SAFBP has agreed to execute and deliver the Security Agreement “in order to evidence and secure its agreement to share certain sale or refinancing proceeds with the Government by placing a [Government] lien upon its leasehold interest in the land which is subject to the Lease and its fee simple interest in the [new] land which is subject to the Use Agreement... together with the improvements and personalty which are or will be located on the land.” Paragraph 2 states that SAFBP is obligated to pay to the Government 60% of the “capital event gross proceeds” paid to SAFBP from the sale or refinancing of the Project. Paragraph 7 states that SAFBP grants to the Government a lien on and security interest in the property and a security interest in the UCC Collateral to secure the performance of its

obligations under this Agreement.” Paragraph 7(b) states that the lien and the security interest granted to the Government shall be subordinated to the lien of any financing secured by the property that has been approved by the Government. Tr. pp. 54-58, 67-68, 112-114, 215-216; App. Ex. No. 8.

35. In the event that Scott sells its interest in the property, the Government would get 60% of the proceeds after Scott pays off its outstanding debt obligations.

Scott can only sell its interest with Government approval. Tr. pp. 112-113.

36. To get visitors on the base, residents must call a visitor’s center, and tell them who is coming, for how long and where they will be staying. This puts the visitor on an access list. The visitor then needs to go to the visitor’s center, produce proof of identity and have their social security number checked for outstanding warrants before they are allowed on Scott AFB. Tr. pp. 229-234.

### **CONCLUSIONS OF LAW:**

An examination of the record establishes that SAFBP has demonstrated, by the presentation of testimony and through exhibits and argument, evidence sufficient to warrant exempting the Leasehold Interest from taxation for the 2007 assessment 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 limitations 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 or limitations on those exemptions it chooses to grant. Village of Oak Park v. Rosewell, 115 Ill. App. 3d 497 (1<sup>st</sup> Dist. 1983).

In accordance with its constitutional authority, the General Assembly enacted section 15-50 of the Property Tax Code, which exempts all property of the United States, “except such property as the United States has permitted or may permit to be taxed.” 35 ILCS 200/15-50. Intervenors stated in their Post-Hearing Brief that the land that is leased to SAFBP is owned by the U.S. Government. “Due to that ownership, the land is undeniably exempt under Section 15-50 of the Illinois Property Tax Code.” Int. Response, p. 4. Accordingly, it is not in controversy here that the land that is leased to SAFBP is owned by the U.S. Government and is exempt under Section 15-50 of the Property Tax Code.

The United States Government leased the subject property to SAFBP in a Lease dated January 1, 2006 between the United States, acting by and through the Secretary of the Air Force, and SAFBP. The St. Clair County Assessor assessed the property as a leasehold interest under the provisions of Section 9-195 of the Property Tax Code which provides that when property which is exempt from taxation is leased to another whose property is not exempt, and the leasing of which does not make the property taxable, the

leasehold estate and the appurtenances shall be listed as the property of the lessee thereof, or his or her assignee. Taxes on that property shall be collected in the same manner as on property that is not exempt, and the lessee shall be liable for those taxes. 35 ILCS 200/9-195.

35 ILCS 200/15-50 and 35 ILCS 200/9-195 are the only two statutes at issue in this proceeding. Nonetheless, St Clair County, in its Post- Hearing Brief, addresses 35 ILCS 200/10-365 *et seq.*, “which deals specifically with U.S. Military Public/Private Residential Developments.” “That section of the Code concerns the classification and valuation of the leasehold interest in United State Property that is exempt from taxation but is leased to a non-exempt entity for a development of housing on a military compound for use by military personnel.” “For guidance” in determining how the Department should “uniformly” consider SAFBP’s application for exemption, St. Clair County suggests that this tribunal look at 35 ILCS 200/10-365 *et seq.*, “which indicates the intention of the legislature.” Int. Response p. 29. According to St. Clair County, “[I]t would be discriminatory not to tax and assess [Scott AFB] as other like property, with no distinguishing characteristics, is taxed and assessed in the State of Illinois.” Int. Response, p. 33.

There are several problems with St Clair County’s argument. First, 35 ILCS 200/10-370 covers “rental housing units and associated improvements at naval training and related naval support facilities in the State of Illinois.” 35 ILCS 200/10-370. Scott AFB is not a naval training or naval support facility. Second, St. Clair County states that “[T]hroughout the passage of this legislation there was never any doubt voiced by any party involved with the property or the legislature that the leasehold it created was taxable.” Int. Response, p. 30. However, the “leasehold it created” was never introduced

into evidence in the instant proceeding and I have no way of determining that there were “no distinguishing characteristics” between the leasehold involved in the legislation and the Leasehold at Scott AFB.

In the legislative debate on 35 ILCS 200/10-365 *et seq.*, which St. Clair County included in its Post-Hearing Brief, Representative Molaro stated that “[the legislation] gives us a platform if we ever wanna [sic] do it down south by the air base down there.” Int. Response, p. 30. I assume that Representative Molaro was referring to Scott AFB, “down south.” Whatever “platform” was given to the legislature was not acted upon because there is no statute on how to classify and value leasehold interests at air force bases and related air force support facilities in the State of Illinois. I cannot infer from Representative Molaro’s comments that other legislators agreed that the legislation provided a “platform” to tax leaseholds “down south.”

Much of the legislative debate concerns the effect that the naval base had on schools in the area. For example, Representative Molaro stated, “for the first time,” “when these Navy personnel who live there, who go to schools in that area, we are now taxing from the property taxes of the leasehold.” Int. Response, p. 30. In the instant matter, no evidence was presented by St. Clair County as to the effect that Scott AFB had on the schools in the area.

In the legislative debates, Representative May stated that “[T]his is an agreed bill, agreed by all parties; the Navy, the developer of the public private venture, and the four communities...” Int. Response, p. 31. It is difficult for me to infer legislative intent to tax leaseholds down south based on an “agreed bill” that covers naval training and support facilities in a county, which apparently needed the tax levy for its schools. Thus,

St. Clair County's arguments about this agreed bill do not provide guidance for deciding on the taxability of SAFBP's Lease in the instant matter.

The St. Clair County Assessor assessed the property at issue as a leasehold interest under 35 ILCS 200/9-195 of the Property Tax Code, finding that the Lease created a leasehold interest that is owned by SAFBP. Int. Response, p. 4. SAFBP's argument as to why the Lease is not taxable can be stated as follows: The Government gave to SAFBP nothing more than a contractual license to use the Leased Premises as directed by the Government for the purpose and benefit of the Government, and such license is not a taxable interest under Illinois law. SAFBP Memo., p. 2.

Whether an agreement is a license or a lease is not determined by the language used, but by the legal effect of the provisions and the intent of the parties. Stevens v. Rosewell, 170 Ill. App. 3d 58 (1<sup>st</sup> Dist. 1988). No particular words are required to create a lease. Rather the existence of a lease depends upon the intention of the parties and this intention must generally be inferred from the circumstances of the particular case. Generally, however, the question of possession will determine the matter. People v. Chicago Metro Car Rentals, 72 Ill. App. 3d 626 (1<sup>st</sup> Dist. 1979). Exclusive possession is essential to the character of a lease. Holladay v. Chicago Arc Light & Power Co., 55 Ill. App. 463 (1<sup>st</sup> Dist. 1894). The essential requirements of a lease include a definite agreement as to the extent and bounds of the property, a definite and agreed term, a definite and agreed rental price and manner of payment. Jackson Pk. Yacht Club v. Dept. of Gov't Affairs, 93 Ill. App. 3d 542 (1<sup>st</sup> Dist. 1981).

In contrast, a license is a limited right to use the licensor's premises for a specific purpose, subject to management and control retained by the licensor. In Re Application of Rosewell v. City of Chicago, 69 Ill. App. 3d 996 (1<sup>st</sup> Dist. 1979). A license is not

assignable, and merely gives another the right to use the premises for a specific purpose with the owner retaining possession and control. An instrument that merely gives to another the right to use premises for a specific purpose, the owner of the premises retaining the possession and control of the premises, confers no interest in the land and is not a lease, but a mere license. A license is an authority to do some act or series of acts on the land of another, without passing an interest in the land. Holladay v. Chicago Arc Light & Power, 55 Ill. App. 463 (1<sup>st</sup> Dist. 1894). Unlike leases, licenses for the use of exempt property are not taxable interests under the Property Tax Code. Jackson Park Yacht Club v. Dept. of Gov't Affairs, 93 Ill. App. 3d 542 (1<sup>st</sup> Dist. 1981).

The Lease at issue in the instant proceeding possesses some characteristics of a “lease” and some characteristics of a “license.” Additionally, as discussed more fully below, it appears from the numerous documents involved in this Project that the Government understood that the Lease might be taxed. However, after careful consideration of the evidence and testimony presented at the hearing, including the Parties’ Post-Hearing Briefs and the relevant case law and statutes, I conclude, because of the Government’s pervasive and all-encompassing control over the Leased Premises, that the Government gave SAFBP a license, rather than a lease, and that this license is not a taxable interest under the Property Tax Code.

**The Military Housing and Privatization Initiative:** The “Recital” in SAFBP’s Lease states that the Secretary of the Air Force has determined, under the authority contained in 10 U.S.C. § 2878, that the leasing of certain property within the boundaries of Scott AFB “will be advantageous to the United States and in the public interest.” App. Ex. No. 3. The Military Housing and Privatization Initiative (“MHPI”) is found in chapter 169 of Title 10 of the United States Code, which is captioned “Military Construction and

Military Family Housing,” and specifically in subchapter IV, captioned “Alternative Authority for Acquisition and Improvement of Military Housing.” 10 U.S.C. § 2871, *et seq.* Section 2878 of the MHPI states that the Secretary may convey or lease property or facilities to eligible entities for purposes of using the proceeds of such conveyance or lease to carry out activities under this subchapter. 10 U.S.C. § 2878(a). As part of the consideration for a conveyance or a lease under Section 2878, the lessor shall enter into an agreement with the Secretary to ensure that a “suitable preference” will be afforded members of the armed forces and their dependents in the lease or sublease of a reasonable number of the housing units covered by the conveyance or lease, or in the lease of other suitable housing units made available by the purchaser or lessee. 10 U.S.C. § 2878(d)(2).

Section 2878(e)(1) of the MHPI states that the lease of properties under this section shall not be subject to “Section 2667 of this title.” 10 U.S.C. § 2878(e)(1). Section 2667 is found in chapter 159 of Title 10 of the United States Code, which is captioned “Real Property; Related Personal Property and Lease of Non-Excess Property.” Section 2667 does not specifically address military construction and military family housing. Section 2667, titled “Leases: non-excess property of military departments,” states that whenever the Secretary of a military department considers it advantageous to the United States, he may lease to a lessee and upon such terms as he considers will promote the national defense or be in the public interest, real or personal property that is under the control of the department and not excess property. 10 U.S.C. § 2667(a)(1)(2). Mr. Vaughn testified at the evidentiary hearing that Section 2667 is the “enhanced use lease authority.” “Enhanced use leasing is a program of the government really to utilize – to monetize under-utilized assets on military installations.” Tr. p. 98. Section 2667 states that “the interest of a lease of property under this section may be taxed by State and local

governments.” 10 U.S.C. § 2667(f). Note that the MHPI is “not subject” to Section 2667.

There was testimony at the hearing that the RFP and the Project documents in the instant matter do, and are required to, identify the authority of the Government in entering into this transaction. Tr. pp. 97-98. SAFBP’s Lease, in the instant matter, is not an interest in property under 10 U.S.C. § 2667 because the Lease expressly states that the Lease is authorized under the MHPI, 10 U.S.C. § 2878. And Section 2878 of the MHPI, unlike 10 U.S.C. § 2667, does not expressly include language that allows taxation by State and local governments. In fairness, it must also be noted that Section 2878 does not expressly include language that would disallow taxation by State and local governments.

However, more than one court has read Section 2878’s omission of language that allows taxation by State and local government as evidence that Congress did not consent to state and local taxation of interests conveyed pursuant to Section 2878 of the MHPI. In Atlantic Marine Corps Communities LLC v. Onslow County, N.C., 497 F. Supp. 2d 743 (E. D. N.C. 2007), a Federal district court rejected local efforts to tax property in a MHPI arrangement involving a private party developer, similar to SAFBP, and military housing located at Marine Corps Base Camp Lejeune.<sup>2</sup> The Atlantic Marine Corps court noted that Congress may permit certain state actions, including the use of the state’s taxing authority, citing Offhut Housing Co. v. County of Sarpy, 351 U.S. 253 (1956), but the court concluded that that notion “has no application where, as here, Congress has actively withheld its consent to state property taxation, [citing] 10 U.S.C. § 2878(d)(1).” *Id.* at 756. Section 2878(d)(1) states that the conveyance of a lease or facilities under this

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<sup>2</sup> Atlantic Marine Corps, discussed extensively in SAFBP’s Post-Hearing Memorandum of Law, was not mentioned in St. Clair County’s Post-Hearing (Response) Brief.

section shall be for such consideration and upon such terms and conditions as the Secretary considers appropriate for the purpose of this subchapter and to protect the interests of the United States. 28 U.S.C. § 2878(d)(1).

The areas at issue in Atlantic Marine Corps were under exclusive federal jurisdiction. At Scott AFB, the Government exercises exclusive federal jurisdiction over the Colonial, Georgian, and Colonial Annex Parcels within the Leased Premises and proprietary federal jurisdiction over all other Parcels.<sup>3</sup> “Proprietary jurisdiction covers those instances in which the Federal Government has acquired some degree of ownership to a land area in a State but has not obtained any measure of the State’s legislative authority over the area.” United States v. Martin, 3 M.J. 744, 747 (1977). In an article entitled “Federal Immunity from State Taxation and the Contract Management of Military Commissaries,” the author notes that some commissaries on military installations are located on proprietary jurisdiction land. “Contractors operating such stores would have no protection under state taxing jurisdiction.” 37 Naval L. Rev. 157 (Winter, 1988). Therefore, it must be presumed that the Government recognized that the State might have the right to tax the Parcels held in proprietary jurisdiction.

The Atlantic Marine Corps court concluded that the MHPI “does not grant any power or authority to Onslow or Craven County to enforce the property tax laws on the

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<sup>3</sup> Condition 12.5 of the Lease entered into by the Government and SAFBP on January 1, 2006 states that “[T]he United States presently exercises proprietary jurisdiction over the leased premises.” App. Ex. No. 3. On January 7, 2010, (after the assessment year at issue in these proceedings) the United States, through the Secretary of the Air Force and SAFBP executed a “Seventh Amendment to Lease of Property on Scott AFB, Belleville, Illinois.” The Amendment states that the Government and the Lessee have determined that there is an error in Condition 12.5 of the Lease and Condition 12.5 of the Lease is modified as follows: “The United States presently exercises exclusive federal jurisdiction over Parcel A (Colonial), Parcel C (Georgian), and Parcel G (Colonial Annex) within the leased premises, and proprietary federal jurisdiction over Parcel B (Galaxy), Parcel D (Patriots Landing), Parcel E (Shiloh East) and Parcel F (Shiloh West) within the leased premises.” “The Lease, as modified by this Amendment, shall continue in full force and effect.” Tr. pp. 47-52, 121-122, 180-182; App. Ex. No. 7.

Marine Corps Lands” and that “[a]ll real and personal property related to plaintiff’s management, construction and renovation of privatized military housing pursuant to the [MHPI]... is not subject to property taxation by Onslow or Craven County.” *Id.* at 759-760. The court enjoined the Counties from “listing, appraising, or taxing any real or personal property related to plaintiff’s construction and renovation of military base housing pursuant to the [MHPI]. *Id.* at 760.

For the Parcels held in exclusive federal jurisdiction at Scott AFB, Atlantic Marine Corps cannot be distinguished. The court’s holding in Atlantic Marine Corps and Section 2878(d)(1) of the MHPI make it reasonable to conclude that the interests of the United States would similarly be “protected” by not enforcing State property tax laws on Parcels over which the Government exercises exclusive federal jurisdiction at Scott AFB.

St. Clair County did not introduce any testimony or evidence to support a partial exemption of the Leased Premises, based on the Government’s jurisdiction over the individual Parcels. All of the Leased Premises are within Scott AFB. All of the Parcels are governed by the Operating Agreement. There is nothing in the “Project” documents to distinguish the activities on any one Parcel in the Leased Premises from any other. All of the Parcels in the Leased Premises are equally under the control of the Government and the Wing Commander. I have concluded that the Lease is, in reality, a nontaxable license. This conclusion is not affected by the jurisdiction that the Government holds over the individual Parcels.

The State of Utah has similarly found that improvements quit-claimed by the Government, as part of an MHPI Project, were exempt from property taxation because they remained in U.S. government ownership. In Application of Boyer Hill Military Housing L.C. for Property Tax Exemption for Improvements on Parcels, Davis County

Board of Equalization, Utah (2009), Boyer Hill Military Housing filed an exemption for leased premises improvements “within the confines of Hill Air Force Base.” The leased premises were acquired at a time when jurisdiction was ceded to the Federal Government by Utah, subject to Utah’s reserved “right to impose taxes on the Leased Premises to the extent it is used by private individuals or entities to conduct business thereon.” “The Leased Premises are, accordingly, within an area of concurrent state and federal jurisdiction.” *Id.* at 2.

The decision of the Davis County Board of Equalization discusses the MHPI and the Hill AFB Project. The terms of the Project are strikingly similar to SAFBP’s, including a 50 year Lease, a Lockbox Agreement, a “vacancy buffer” before rental to non-military personnel, and control by the Air Force of the design for renovated and newly constructed homes. The Davis County Board found that, pursuant to 10 U.S.C. § 2878, Congress has specifically provided that the Federal Government’s conveyance or lease of property or facilities under the [MHPI] shall not be subject to the Federal Government’s waiver of sovereign immunity to allow state and local taxation. “Accordingly, the Leased Premises Improvements are exempt from local taxation as a matter of federal law, “notwithstanding the presence of joint state and federal jurisdiction.” *Id.* at 6. The Davis County Board found further that the Air Force had retained the most significant incidents of ownership of the Leased Premises Improvements and the Air Force, rather than the developer, “should be deemed to be the owner of the Leased Premises for tax purposes.”<sup>4</sup> *Id.* at 6.

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<sup>4</sup> Application of Boyer Hill, discussed in SAFBP’s Post-Hearing Memorandum of Law, was not mentioned in St. Clair County’s Post-Hearing (Response) Brief.

There is no indication in the MHPI that it is ever used by the Government for the purpose of raising revenues. Mr. Vaughn testified at the evidentiary hearing that the “motivation” behind the MHPI was to “get financing off the federal balance sheet.” Tr. p. 91. He testified further that the Secretary of the Air Force entered into the Lease in order to “leverage private capital to build adequate housing for service members at Scott AFB.” “And they do it at a rate that’s much, much faster than they could do it under a traditional [military construction] program.” Tr. p. 111.

This testimony is supported by the Air Force’s RFP for this Project, which solicited “proposals from qualified entities interested in entering into a business arrangement with the Government” in order to improve Scott AFB. SAFBP was the “Successful Offeror (“SO”) on the Project.”<sup>5</sup> Tr. pp. 107-108. The RFP states that the goal of the Scott AFB privatization initiative is to provide military families access to safe, secure, quality, affordable well-maintained housing in a military community where they choose to live. “Privatization will accelerate housing improvements, alleviate housing shortages, and reduce waiting times for adequate housing, ultimately improving morale of Air Force personnel.” “Since traditional military construction [MILCON] funds are unavailable to meet this goal in a timely manner, Government officials have determined that the best solution is to use privatization to leverage available resources.” App. Ex. No. 10. The federal government has a long history of using publicly owned corporations to achieve governmental purposes. Va. Atty. Gen. Op. No. 04-057, 2004 Va. AG LEXIS 37, July 21, 2004. “The ‘privatization’ contained in The Military Housing Privatization

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<sup>5</sup> SAFBP is a member managed LLC, the manager of which is Scott Family Housing, LLC, organized for profit, which is itself wholly owned by Hunt ELP, a Texas limited partnership, organized for profit, the managing general partner of which is HBGP, LLC, a Nevada limited liability company, organized for profit. Tr. pp. 107, 153-155.

Initiative is an example of the federal government seeking to use private sector expertise to accomplish a governmental function.” *Id.*

Paragraph 3.2.3.10 of the RFP specified the “Desired Financial Features” of a successful bid. App. Ex. No. 10. SAFBP financed the Project’s required construction of new housing and renovation and demolition of old housing by borrowing a \$173 million senior loan from GMAC for a 40 year period. SAFBP also borrowed \$24 million from GMAC as a bridge loan. The Government then gave SAFBP a commitment for \$24 million to pay off GMAC’s bridge loan when construction was completed. SAFBP contributed \$11 million in equity. Tr. pp. 104-106.

Mr. Vaughn testified that the Lease in the instant case “is what enables us to get private financing.” The Lease gives a lender “the security they need to invest in the Project, to loan the Project money.” Without the Lease, the lender does not “have the ability to put a lien on anything that would give them the ability to step into your shoes should you fail to do what you are supposed to do.” Tr. pp. 111-112.

On January 1, 2006 the United States, through the Secretary of the Air Force, and SAFBP executed a “Mortgage Security Agreement and Agreement to Share Proceeds,” (hereinafter “Security Agreement”) which was recorded with St Clair County. Recital B of the Security Agreement states that SAFBP and the Government have entered into one or more Project documents including the Lease. Recital D states that SAFBP has agreed to execute and deliver this Security Agreement “in order to evidence and secure its agreement to share certain sale or refinancing proceeds with the Government by placing a [Government] lien upon its Leasehold Interest in the land which is subject to the Lease and its fee simple interest in the [new] land which is subject to the Use Agreement... together with the improvements and personalty which are or will be located on the land.”

Paragraph 2 states that SAFBP is obligated to pay to the Government 60% of the “capital event gross proceeds” paid to SAFBP from the sale or refinancing of the Project. App. Ex. No. 8.

Paragraph 7 of the Security Agreement states that SAFBP grants to the Government a lien on and security interest in the property and a security interest in the UCC Collateral to secure the performance of its obligations under this Agreement.” Paragraph 7(b) states that the lien and the security interest granted to the Government shall be subordinated to the lien of any financing secured by the property that has been approved by the Government. According to the testimony at the hearing, Paragraph 7(b) of the Security Agreement gives lenders to the project, such as GMAC, assurance that the Government lien is subordinate to their financing of the Project. “This is absolutely essential” in order to get financing for the Project. Tr. pp. 54-58, 67-68, 112-114, 215-216; App. Ex. No. 8.

I conclude from the testimony and the evidence that the Government enters into an agreement with a Successful Offeror under the MHPI so that the Successful Offeror can obtain private financing to take the place of unavailable MILCON funding. In the instant matter, the Government entered into a “Lease” with SAFBP as a means to facilitate private financing for construction and improvement of housing, a “government function,” at Scott AFB. Section 1.1 of the RFP identified the authorities conferred by Congress in the MHPI which it would, and would not, utilize in the Scott AFB proposal. App. Ex. No. 10. The RFP used the term “Lease” because Congress, in drafting the MHPI, used the term “Lease.” It was essential for the Government to enter into the “Lease” with SAFBP because the “Lease” gives the lender something to put a lien on, with the Government’s lien subordinate to the lender’s. Tr. pp. 111-112. I also conclude

from the testimony and evidence that it was essential that SAFBP enter into a “Lease” with the Government in order to allow SAFBP to obtain the financing that the Government required and intended SAFBP to obtain.

The existence of a lease depends upon the intention of the parties and this intention must generally be inferred from the circumstances of the particular case. People v. Chicago Metro Car Rentals, 72 Ill. App. 3d 626 (1<sup>st</sup> Dist. 1979). In the instant matter, the circumstances show that the document, denominated as a “Lease,” was intended only to allow for a security interest to a lender, so that the Government, through SAFBP, could access private financing to accomplish a “governmental function.”

In Cole Hospital, Inc. v. Champaign County Board of Review, 113 Ill. App. 3d 96 (4<sup>th</sup> Dist. 1983), the hospital, which was the owner of the subject real estate, could not obtain traditional financing for the construction of a new facility. The hospital was forced to convey the property to Safe Care, Inc. subject to a lease-back arrangement. Safe Care advanced Cole \$5.5 million, but required a conveyance and lease-back arrangement. “The ostensible purpose was to permit Safe Care, in the event of default by Cole, to acquire the property immediately without foreclosure proceedings and to resell or relet it.” *Id.* at 98. The issue in the case was whether the Safe Care lease so divested Cole of ownership that it could no longer qualify for property tax exemption.

The record was undisputed that Cole had made extensive efforts to obtain traditional financing. “It approached a major lender in New York, management corporations, hospital management corporations, bond underwriters, commercial mortgage lenders, and the City of Champaign, all without success.” The court then stated that “Cole should not be penalized for failure to obtain conventional financing.” *Id.* at 100.

In Cole Hospital, the lease-back arrangement permitted Safe Care to take over the property in the event of a default without foreclosure proceedings. In the instant case, the Government took a lien and security interest against SAFBP's Leasehold and then subordinated the Government's interest to a private lender per the Security Agreement. Mr. Vaughn testified that the Lease gives a lender "the security they need to invest in the Project, to loan the Project money." Tr. pp. 111-112. Because of the Lease, the Government has access, through SAFBP, to private financing. In the instant case, taxing SAFBP's Lease, in effect, penalizes the Government for using a Lease under the MHPI to access private financing rather than using "conventional," but unavailable, MILCON funding.

**The Government's Intent and Understanding that the Project is Taxable:** 35 ILCS 200/15-50 provides that all property of the United States is exempt, "except such property as the United States has permitted or may permit to be taxed." St. Clair County argues, first, that the Government has not withheld its consent to taxation of this leasehold and, second, that the Government intended leaseholds such as that owned by SAFBP to be taxed. Int. Response, p. 22. According to St. Clair County, there are "glaring and ubiquitous references" throughout the Project documents indicating "an understanding and intent by the Government that the Project would be taxable." Int. Response, p. 15.

I conclude that there are, in fact, references throughout the Project documents that the Government understood or recognized that the Project would be taxed. The RFP states in Paragraph 3.2.4 entitled "Property Taxes," that the SO shall be responsible for the payment of any property taxes assessed on the Project. "[SO's] proposal shall assume that property taxes will be assessed on the Project and include such costs in its financial

projections.” Any savings during the project realized from an exemption from or abatement of property taxes shall be distributed pursuant to the terms of the “Lockbox Agreement.” Should tax consequences for the Project change, “the SO acknowledges that the Government will not be held responsible for the results of such changes and the SO remains responsible for any property taxes assessed.” Tr. pp. 122-124, 133, 166-167, 214-215; App. Ex. No. 10.

The Lockbox Agreement, referred to in the RFP, sets up several different accounts, which are funded according to an order of priority. There are two funding schedules, the first entitled “Transfers from Lockbox Revenue Account Prior to Completion Date [of the Project]” and the second entitled, “Transfers from Lockbox Revenue Account After the Completion Date.” In both of these schedules, the “Imposition Reserve Account” is the third account funded. This account covers applicable property taxes and insurance premiums. App. Ex. No. 12.

On January 1, 2006, the United States, acting by and through the Secretary of the Air Force, transferred to SAFBP, by Quitclaim Deed, all right, title and interest of the Government in and to certain family housing units and ancillary improvements and all personal property contained therein now existing and located at Scott AFB. The transfer was made subject to the terms and condition of the Lease. The Quitclaim Deed states that “Future Tax Bills” [should be sent to] SAFBP, El Paso, Texas. According to the Intervenor, this statement shows an understanding and intent by the Government that the Project would be taxable. Int. Response, pp. 14-15.

Similarly, Condition 8.1 of the Lease, entitled “Taxes,” states that the lessee shall pay to the proper authority, when due, all taxes, assessments and other charges which, during the term of the Lease, may be imposed on the lessee or the Project. However,

each party to the Lease shall have the right to contest such taxes, assessments or other charges, and to take any action as may be necessary to contest the validity of the taxes, to minimize such taxes, or to assert any exemption which may be available.

No one from the Government testified at the evidentiary hearing and there is nothing in the record of this case to show conclusively that the Government withheld its consent to taxation of SAFBP's Lease. The "glaring and ubiquitous" references throughout the Project documents must be interpreted as the Government allowing for taxation of the Lease, but with SAFBP having the right to contest the taxation either by minimizing the taxes or by asserting any exemption available. If the Government was not allowing the Lease at issue to be taxed, there would be no need for language in the Project documents giving SAFBP the right to minimize the taxes or apply for an exemption.

SAFBP argues that St. Clair County "ignores case law aplenty that does not give such [taxation] terms the significance the County would have the Department ascribe to them." SAFBP Reply, p. 8. In Atlantic Marine Corps Communities, LLC v. Onslow County, N.C., 497 F. Supp. 743 (E.D. N.C. 2007), companies bidding on the project, similar to SAFBP's bidding in the instant matter, were required to "assume that full property taxes and/or possessory taxes will be assessed ... and include all such costs in their financial projections. *Id.* at 748-749. The court noted that the taxing authorities, in attempting to tax the Marine Corps Land, "attempt to imbue with significance" the development company's agreement to assume that property taxes will be assessed on the property. The court found nothing more in the bid solicitation language than a "precaution on the Government's part to guard itself against liability for payment of any

state taxes ‘lawfully assessed’ against its lessee.” Humble Pipe Line v. Waggoner, 376 U.S. 369 (1964).

In the instant case, the Government is taking the same precaution in the RFP of guarding against its own liability for taxes. But the Government guarding “itself” against liability for state taxes “lawfully assessed” against the lessee cannot be interpreted to mean that the Government does not understand or recognize that the Lease may be lawfully assessed. I agree with St. Clair County that the language of the Lease and the Project documents show that the Government has not withheld its consent to taxation of the Leased Premises.

**The Lockbox Agreement.** On January 1, 2006, the United States, through the Secretary of the Air Force, and SAFBP executed the “Lockbox Agreement,” which controls the revenues and expenditures from the Project. The Lockbox Agreement sets up several different accounts, which are funded according to an order of priority. Any change in priorities requires prior written Government consent. There are two funding schedules, the first entitled “Transfers from Lockbox Revenue Account Prior to Completion Date [of the Project]” and the second entitled, “Transfers from Lockbox Revenue Account After the Completion Date.” In both of these schedules, the “Imposition Reserve Account” is the third account funded. This account covers applicable property taxes and insurance premiums. In the funding schedule for “prior to completion date” of the project, there is no provision in the schedule for distribution of excess funds to either SAFBP or the Government. App. Ex. No. 12. Mr. Vaughn testified at the hearing that SAFBP has not yet received a distribution of any excess funds from the Project. Tr. pp. 132-133. The Lockbox Agent is GMAC Commercial Mortgage Corporation. Tr. p. 128.

In the funding schedule for “after the completion date” of the Project, the last funding priority states that the residual balance, if any, of the Lockbox Revenue Account shall be deposited for each year of the Government Lease as follows: 70% to the Reinvestment Account and the remaining 30% to SAFBP. The Reinvestment Account is controlled by an “Authorized Officer of the Government.” Tr. pp. 128-132, 167-169, 210-214; App. Ex. Nos. 10, 12. Mr. Vaughn testified at the hearing that SAFBP would only get a 30% distribution of the residual balance of the funds after the completion of the Project.<sup>6</sup> Tr. pp. 132-133.

In In re Application of Rosewell, 69 Ill. App. 3d 996 (1<sup>st</sup> Dist. 1979), the court determined that agreements between the City of Chicago and various parking operators to operate parking garages were licenses and not leases. The parking lot operators collected the revenue from the garages and transferred the revenue directly to the City. From this revenue, the City paid the operators a specific percentage as “compensation which represents a reasonable base payment for management services to be rendered by the operators.” The court believed that it would be unrealistic to characterize this payment of a specific percentage of the profits as “rent.” *Id.* at 1002-1003.

In the instant case, all Project revenues go into the Lockbox Account. Distributions are made according to a predetermined priority, with payments for debt, operations and maintenance being funded first. Several accounts can only be disbursed after approval by the lenders and the Government. Disbursement from one Lockbox Account is incentive-based and dependent on the satisfactory evaluation of Scott AFB’s

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<sup>6</sup> The Lockbox Agreement is not SAFBP’s only source of income from the Project. Mr. Vaughn testified that SAFBP has “three opportunities for income in the Project from a service provider point of view.” “There was the design-build contract, which was a contract for the construction and renovation and demolition of the Project; there was a development agreement or development contract, which, you know, compensated the developer for its services to bringing financing and entitlement and other issues to the Project; and then there’s the property management agreement.” Tr. pp. 216-217.

Wing Commander. Tr. pp. 239-240. The Lockbox Agreement between SAFBP and the Government, which gives SAFBP a specific percentage of excess funds after completion of the Project, resembles the fee determination and payment schedule in Rosewell, where the agreement with the operators was determined to be a license, rather than a lease. Additionally, the Government exercises as much control over the disbursements in the instant case as the City did in Rosewell.

The only “rent” being paid according to Paragraph 4.1 of the Lease, is the \$1 “base rent,” which the Lease calls “nominal,” and which was “paid as consideration for the entire term of the lease.”<sup>7</sup> App. Ex. No. 3. This is not \$1 rent for 1 year, but \$1 rent for 50 years. The \$1 “rent” is not based on tenant occupancy. Tr. pp. 109-110. On March 29, 2007, SAFBP and the Government amended the Lease with the Government requesting, *inter alia*, that SAFBP not demolish the housing units in the portion of the subject property called “Galaxy,” as required in the original Lease, but rather retain those units for temporary living facilities. Tr. pp. 103-104; App. Ex. No. 7. No adjustment was made to the \$1 rent charged in the Lease. The rent is obviously not related to SAFBP’s activities on the Leased Premises.

One of the requirements of a lease is a “definite and agreed rental price.” Jackson Pk. Yacht Club v. Dept. of Gov’t Affairs, 93 Ill. App. 3d 542 (1<sup>st</sup> Dist. 1981). The \$1 rent called for in the Lease between SAFBP and the Government appears to fit the requirement of a lease that there be a definite and agreed rental price. But the \$1 rent in the instant case is, in reality, an indication of the consideration for the creation of the

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<sup>7</sup> “Additional rent” may be charged to SAFBP for police and fire protection services provided by the Government. App. Ex. No. 3.

Leasehold itself. Int. Response, p. 13. I must conclude that the \$1 rent is ceremonial. In a true “lease,” \$1 rental for 50 years would not be anticipated or envisioned.

The characteristic of a lease that the lease include a “definite and agreed rental price” is lacking in the Lease between SAFBP and the Government. The lack of a monthly, quarterly or annual “rent” in the Lease, other than the \$1 specifically identified as “nominal,” for the 50 year term, demonstrates that the document at issue was never envisioned or intended by the parties to be a true lease and is further evidence that the term “Lease” as used in the agreements between SAFBP and the Government was used solely in order for SAFBP to obtain the financing that the Government required and intended SAFBP to obtain.

**New Land:** The RFP required that at the closing of the transaction, the SO would provide “new land” for the construction of privatized housing units. The Government did not have enough land on Scott AFB to build all of the housing it wanted at the density it wanted. Therefore, the Government required the SO to bring some land into the Project that was outside the main component area of Scott AFB. Tr. p. 115. The RFP required that “[T]he land will consist of no more than three parcels, all within a 10 mile radius of the base proper.” The SO was required to construct housing units on the new land within 10 years after the closing of the transaction. App. Ex. No. 10.

As part of SAFBP’s proposal, it had to put an option on a piece of land as evidence that it had control of a suitable parcel to construct 381 units. SAFBP acquired suitable property from the Heberer Brothers. Tr. pp. 114-117; App. Ex. No. 10. The Heberer Brothers’ new land is owned in fee simple by SAFBP, and SAFBP has not applied for an exemption on the new land. The new land is not part of the P.I.N.S at issue in this proceeding. Tr. pp. 222-224.

Scott AFB's perimeter fence is the back of the new land. A resident has to exit Scott AFB to get onto the new land. The new land has its own gate where a resident would put in an identification code or a visitor would call a resident to gain entry. The new land has a separate officer neighborhood and senior enlisted neighborhood. Tr. pp. 245-247, 250-251.

The RFP required that the new land would be subject to a "Use Agreement." On January 1, 2006, the United States, through the Secretary of the Air Force, and SAFBP executed a "Declaration of Restrictive Covenants and Use Agreement for Military Housing Project," ("Use Agreement"), which governs operation of the new land.<sup>8</sup> The purpose of the Use Agreement "is to subject the property to the material provisions of the [RFP] and the legal instruments agreed to by the parties that are deemed important by the Government for the successful operation of the Project." App. Ex. No. 10.

Paragraph 2.1 of the Use Agreement states that SAFBP declares that the Government is the intended beneficiary of the Use Agreement, and it is the intent of both parties that the Use Agreement shall constitute a covenant in favor of or for the benefit of the Government. The Use Agreement states that the Government and SAFBP understand that the Use Agreement further[s] the purposes for which SAFBP was provided with a portion of the permanent financing, a Lease of Leased Premises at Scott AFB and a conveyance of certain improvements located on Scott AFB. App. Ex. No. 11.

Article 17 of the Use Agreement restricts and targets the tenants who may rent housing on the new land. Within 10 days following the end of each month, SAFBP must inform the Scott AFB Housing Management Office of all actual and projected vacancies

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<sup>8</sup> The Use Agreement and covenants do not apply to the parcels within the Leased Premises owned by the Government. Tr. p. 188.

on the new land. The Housing Management Office will then provide a list to SAFBP identifying any target tenants, their pay grade and the number of dependents. A target tenant is “an active duty service member and his or her family authorized to reside in Scott AFB’s family housing units” or “an individual designated by the Commander as ‘key and essential’ and his or her family.” All housing units shall be designated by pay grade and entitlement and shall be made available to target tenants and other eligible tenants. Tr. pp. 117-118, 184-187; App. Ex. No. 11. The housing units built on the new land are governed by the same occupancy plan and management plan that govern units on the Leased Premises. Tr. p. 223. Rental rates on the new land are at the same rates as on the Leased Premises. Tr. p. 246.

Mr. Vaughn testified that SAFBP understood the RFP to be a “package deal,” meaning that the Government would only lease the 490 acres at Scott AFB to SAFBP, if SAFBP could provide new land to the Government. Tr. p. 116. According to Mr. Vaughn, the leasing of the new land is part of the same MHPI Project that includes the Government’s Lease to SAFBP. Tr. pp. 222, 224. This testimony is supported by statements in the Lease. The Recitals at the beginning of the Lease state that the term “Project” as used in the Lease refers collectively to the Leased Premises, the Leased Premises improvements, the new land, and the improvements on the new land. Section 6.1 of the Lease requires that SAFBP make available, after completion date, 1,593 units, “up to 465 of the required units may be located on the [new land].” Section 19.2 of the Lease states that the name used by SAFBP “for any portion of the Project is subject to the prior written approval of the Government.” Section 21.1.4 of the Lease states that SAFBP may not transfer or assign the Lease ... separate from SAFBP’s interest in the [new land].”

The “Recitals” at the beginning of the Use Agreement, which govern operation on the new land, also support Mr. Vaughn’s testimony. The Recitals state that the Government has agreed to provide a portion of the permanent financing, lease certain real property on Scott AFB and convey certain improvements located on such leased real property to SAFBP. “In consideration of the Government’s undertakings set out above,” SAFBP has agreed to execute and deliver this Use Agreement, “for the purpose of setting forth terms and conditions relating to SAFBP’s responsibility for the demolition, design, construction, renovation, operation and maintenance on the new land.” App. Ex. No. 11.

As discussed above, on March 29, 2007, SAFBP and the Government amended the Lease with the Government requesting, *inter alia*, that SAFBP not demolish the housing units in the portion of the subject property called “Galaxy,” as required in the original Lease, but rather retain those units for temporary living facilities. Tr. pp. 103-104; App. Ex. No. 7. No adjustment was made to the obligations of the parties. There was no change in the \$1 rent paid by SAFBP for the 50 years of the Lease. The amendment to the Lease also states that upon the Government determination that SAFBP has satisfactorily completed the demolition of certain parcels, the Lease will be amended to release these parcels and the land and the improvements located in such parcels “shall be returned to the Government.” App. Ex. No. 7. There is no mention in the Amendment of an adjustment being made to the obligations of the parties upon the demolition of these parcels and their return to the Government.

In Ceres Illinois v. Scrap Processing, 114 Ill. 2d 133 (1986), the Court stated that in Illinois, for a lease to be valid, there must be agreement as to the extent and bounds of the lease. In Millennium Park Jt. Venture v. Houlihan, 393 Ill. App. 3d 13 (1<sup>st</sup> Dist. 2009), appeal allowed, 234 Ill. 2d 525 (Nov.25, 2009), the plaintiff argued that the

Agreement between the parties lacked a sufficient description of the premises to satisfy the definitiveness required of a lease. The defendants, citing Ceres, responded that as long as the parties understood the extent and bounds of the property, the lease requirement was satisfied. The court, however, agreed with the plaintiff finding that “the vagueness of the description” of the premises at issue in the case was more indicative of a license than a lease. *Id.* at 30.

In the instant case, SAFBP argues that the Lease that was assessed by St Clair County, does not define the “extent and bounds” of the Agreement entered into by SAFBP and the Government. According to SAFBP, the MHPI Project was never limited to just the Lease. The number of units available on the Leased Premises was not sufficient to meet the Government’s requirements, from the start, and it was always contemplated that this Project would encompass both the Leased Premises provided by the Government, and assessed by the County, and the new land provided by SAFBP. In exchange for the Lease to SAFBP, the Government received a Use Agreement over land it did not own. Additionally, as the Lease was amended, the obligations of the parties in the Lease were not amended, further indicating that the scope of this Project exceeded the extent and bounds of the “Lease.” SAFBP argues, as in Millennium Park, that the “vagueness” of the Lease, as far as defining the complete agreement between the parties, shows that the document is more indicative of a license than a lease.

However, St. Clair County correctly points out in its Response that the Exhibits to the Lease Memorandum specifically identify the property at issue in the Lease. Int. Response, p. 13. What has been assessed by St. Clair County in this case is specifically described in the Exhibits to the Lease Memorandum. App. Ex. No. 15. According to St

Clair County, “[T]here can be no question that the property at issue here has a definite extent and bounds.” Int. Response, p. 13.

I agree with SAFBP that MHPI Project was never limited to just the Lease. However, as far as the Lease, itself, is concerned, St. Clair County is correct that the property assessed is specifically and comprehensively defined in the Lease Memorandum. The property assessed in the Lease, at issue here, has definite extent and bounds. I conclude, however, that this factor cannot be controlling here because the control exercised by the Government in the instant case is so pervasive and all-encompassing, as discussed below, that the Government gave SAFBP a license, rather than a lease, and this license is not a taxable interest under the Property Tax Code.

**The Quitclaim Deed, Lease and Operating Agreement and Government Control over the Leased Premises:** On January 1, 2006, the United States, acting by and through the Secretary of the Air Force, transferred to SAFBP, by Quitclaim Deed, all right, title and interest of the Government in and to certain family housing units and ancillary improvements and all personal property contained therein now existing and located at Scott AFB. The transfer was made subject to the terms and conditions of the Lease. The Quitclaim Deed states that the Deed neither quitclaims nor conveys any interest in the land underlying the improvements. The Quitclaim Deed was filed and recorded with the St. Clair County Recorder of Deeds. Tr. pp. 22-28, 61-62; App. Ex. Nos. 1 and 2.

On January 1, 2006, the United States, acting by and through the Secretary of the Air Force, entered into a “Lease” with SAFBP for the eight parcels of land situated within the boundaries of Scott AFB. The “Recital” to the Lease states that the Secretary, under the authority contained in 28 U.S.C. § 2878, has determined that the leasing of

certain property will be advantageous to the United States and in the public interest. The term of the Lease is for 50 years. App. Ex. No. 3.

The Lease specifically “incorporated into and made a part of the Lease” the “Operating Agreement.” On January 1, 2006, the United States, through the Secretary of the Air Force and SAFBP executed the “Operating Agreement.” The Operating Agreement controls the operational aspects of the Project from initial construction and development to who can occupy the units, the rates to be charged and maintenance of the facilities. The Operating Agreement “sets forth detailed procedures and requirements to be followed by [SAFBP] in designing, demolishing, constructing, renovating, operating and maintaining the Leases Premises.” The Lease provides that SAFBP shall operate the Project in accordance with each of the following plans, which are included as attachments to the Operating Agreement: Construction Management Plan; Rental Rate Management Plan; Unit Occupancy Plan; Property Operations and Management Plan; Facilities Maintenance; Scott AFB Housing Leases for Military/Non-Military Tenants; Community Development Plan; Fee Management Plan; Unit Design Plan; Transition Plan; Severability Plan; Quality Control Plan.<sup>9</sup> App. Ex. No. 3. I conclude that the Government maintains control over this entire Project through the Lease and the Operating Agreement and its attachments.

An instrument that merely gives to another the right to use premises for a specific purpose with the owner of the premises retaining the possession and control of the premises, confers no interest in the land and is not a lease, but a mere license. Holladay v. Chicago Arc Light & Power Co. 55 Ill. App. 463 (1<sup>st</sup> Dist. 1894). In the instant case, SAFBP has been given the right to use the premises for one “sole purpose.” Condition

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<sup>9</sup> The Operating Agreement and Attachments are 367 pages.

6.1 of the Lease states that the “sole purpose” for which the Leased Premises and the Leased Premises Improvements that are now or will be erected, in the absence of prior written approval of the Government, is for design, demolition, construction, renovation, operation and maintenance of a rental housing development for use by military personnel and their dependents. To the extent that St. Clair County argues that the Project holds a proprietary purpose for SAFBP, I must conclude that SAFBP’s purpose is foreshadowed by the purpose of Scott AFB, which is to provide housing for military personnel pursuant to very strict rules as to the use of the property.

Note that the Lease gives SAFBP the right to use the Leased Premises for one “sole purpose” or as stated in Holladay, one “specific purpose.” The “specific purpose” is further limited by Condition 6.2 of the Lease which states that, in no event, shall the leased premises be used by SAFBP for any retail sales or services or commercial recreational operations or activities. Tr. pp. 9, 13; App. Ex. No. 3.

The rental housing development will contain 1,430 units prior to the completion date, and 1,593 units after completion date, primarily for use by military personnel and their dependents, authorized to live on Scott AFB. Up to 465 of the required units may be located on the new land. Tr. pp. 40-41, 108-110, 121-122, 144-145, 175-179; App. Ex. No. 3.

The provisions of the Lease and the Operating Agreement force me to conclude that the U.S. Government, as owner of the Leased Premises, retains possession and control over them, in effect, making the Lease at issue, a “mere license.” Condition 27.1 of the Lease states that nothing in the Lease shall be construed to diminish limit or restrict any right, prerogative, or authority of the Commander of Scott AFB over the Leased Premises, relating to the security or mission of the Installation, the health, welfare, safety

or security of persons on the Installation or the maintenance of good order and discipline on the Installation, as established in law, regulation or military custom. Condition 27.2 of the Lease states that the Commander has the right at all times to order the permanent removal and “barment” of anyone from the Installation, including but not limited to tenants, if he or she believes, in his or her sole discretion, that the continued presence on the Installation of that person represents a threat to the security or mission of the Installation, poses a threat to the health, welfare, safety or security of persons occupying the Installation or compromises good order and/or discipline on the Installation. Tr. pp. 146-147; App. Ex. No. 3. This clause gives the Commander, in his or her “sole discretion,” ultimate control over the Leased Premises.

A lease gives the tenant the right of possession both against the landlord and strangers. Exclusive possession is essential to the character of a lease. Holladay v. Chicago Arc Light & Power Co. 55 Ill. App. 463 (1<sup>st</sup> Dist. 1894). In the instant case, Condition 2.1 of the Lease states that the Government shall have the right to reserve unto itself or to grant to third parties additional easements, rights of way, licenses or other property interests with respect to the Leased Premises. It is not reasonable to conclude that SAFBP has “exclusive possession” over the Leased Premises when Condition 2.1 would allow the Government to grant a license, right-of-way, a lease or “other property interest” to a third party, a “stranger.” SAFBP does not control the Leased Premises against the Commander of Scott AFB, who can act in his sole discretion, or against third parties, who may be granted a property interest in the Leased Premises.

“Exclusive possession” is denied SAFBP by other Conditions in the Lease. Condition 13.1 of the Lease states that any agency of the United States, its officers, agents, employees and contractors may enter upon the Leased Premises and Leased

Premises Improvements, at all times for any purposes not inconsistent with SAFBP's quiet use and enjoyment under the Lease. Condition 17.6 states that the Government and its representatives shall have access to the Leased Premises and Leased Premises Improvements before, during and after construction of the improvements for purposes of monitoring, observing, making inquiries, and taking samples of materials for testing as may be necessary to evaluate the physical characteristics of the Leased Premises Improvements. With agencies of the United States able to enter the premises at all times, and the Government having access to the Leased Premises "before, during and after construction," it is not reasonable to conclude that SAFBP has "exclusive possession."

Section 5(a) of the Operating Agreement states that the Leased Premises and the Leased Premises Improvements are subject to periodic inspection by Scott AFB security personnel. "SAFBP will cooperate with these inspections ... to ensure that law enforcement activities are not hindered and that Scott AFB security requirements are met." Section 5(c) of the Operating Agreement states that the Government retains the right to refuse access to Scott AFB, including the Leased Premises, by SAFBP, its officers, agents, employees, independent contractors and subcontractors, during a national emergency, or other compelling reasons as determined by the Commander in his "sole discretion." "Compelling reasons" are not defined in the Operating Agreement. In the instant case, SAFBP does not have a right of possession against the Government or against third parties who may be granted a property interest by the Government. Possession of the Leased Premises is shared by SAFBP and the Government. SAFBP lacks "exclusive possession" over the Leased Premises and this lack of exclusive possession indicates that the Lease is truly a license.

In In re Application of Rosewell, 69 Ill. App. 3d 996 (1<sup>st</sup> Dist. 1979), the court determined that agreements between the City of Chicago and various parking operators to operate parking garages were licenses and not leases. In Rosewell, the court noted that the reservation of a concurrent right of possession or restriction of rights granted to a single use, does not necessarily prevent an instrument from constituting a lease, but that an agreement which merely entitles one party to use property subject to management and control of another granted only a license. In the instant matter, SAFBP has been granted a “single use” of the Leased Premises and the Government has reserved a “concurrent” right of possession as indicated by the clauses in the Lease and the Operating Agreement, as discussed above.

Moreover, other clauses in the Lease and the Operating Agreement show conclusively that SAFBP uses the Leased Premises, subject to the management and control of the Government. With a license, the owner retains control. Stevens v. Rosewell, 170 Ill. App. 3d 58 (1<sup>st</sup> Dist. 1988). In Millennium Park Jt. Venture v. Houlihan, 393 Ill. App. 3d 13 (1<sup>st</sup> Dist. 2009), appeal allowed, 234 Ill. 2d 525 (Nov.25, 2009), where the court determined that a “Concession Permit Agreement” between the plaintiff and the Chicago Park District was a license rather than a lease, the court noted that the Park District had approval of all signs used by the plaintiff and any name change for plaintiff’s business. In In re Application of Rosewell, 69 Ill. App. 3d 996 (1<sup>st</sup> Dist. 1979), the Operating Agreement prohibited the posting of signs, billboards or other advertisements without prior written consent of the City. *Id.* at 998-999.

In the instant matter, Condition 17.12 of the Lease between SAFBP and the Government requires that SAFBP shall not construct any permanent structure on the Leased Premises and shall not construct any advertising sign on the Leased Premises or

make structural modifications, alterations or additions to the Leased Premises without the prior written consent of the Government. Condition 19.2 of the Lease requires that the name used by SAFBP for any portion of the Project be subject to the prior written approval of the Government. App. Ex. No. 3.

In Rosewell, the agreement between the City and the parking lot operators provided that the parking lot operator could make no alterations or additions to the premises without the prior written consent of the City. *Id.* at 999. In the instant matter, the control exhibited by the Government over SAFBP's renovation work is much more pervasive than the City's control over the parking garages in Rosewell. Condition 17.1.2 of the Lease requires that all housing design plans and site design plans be submitted to the Government for review. Condition 17.9 requires that any Leased Premises Improvements that will be demolished by SAFBP shall be demolished in accordance with a demolition plan prepared by SAFBP and approved by the Government. Condition 17.10 requires that all matters of ingress, egress, contractor haul routes, construction activity and disposition of excavated material shall be approved by the Government. Condition 17.18 requires that no housing unit shall be occupied by a tenant until the Government has provided a written notice to SAFBP that such housing unit may be so occupied. App. Ex. No. 3.

In Rosewell, the City determined the rates to be charged for parking and reserved the right to change the rates. *Id.* at 999. In the instant matter, the Government has complete control over not only the rental rates that can be charged by SAFBP, but also over the tenants that SAFBP can rent to.

Condition 19.4 of the Lease requires SAFBP to first offer to rent units to "target tenants" at the rates specified for those target tenants pursuant to the Rental Rate

Management Plan, included as an attachment to the Operating Agreement. App. Ex. No. 3. “Target tenants” are military families assigned to Scott AFB. Certain units in the Project are called “designated quarters” and only certain people who fill essential positions are allowed to live there. The local Air Force Commander determines those positions considered as “key and essential.”

Condition 19.7 of the Lease requires that if the occupancy rate of the Project falls below 95% for a given period of time, the Property Manager shall have the right to offer vacant housing to other eligible tenants at rates that are no lower or more favorable than the target rate charged to target tenants. Non-target tenants, in terms of priority placement, are first, married military members whose spouses live elsewhere, federal civil service employees, retired military members and families, guard and reserve military members and families, retired federal civil service, Department of Defense contractors, and finally, the general public.<sup>10</sup> Tr. pp. 230-232; App. Ex. No. 13.

There was testimony at the hearing was that there is currently one “non-military” resident on the subject property, the maintenance supervisor, who is a SAFBP employee. The maintenance supervisor is not eligible to use the service facilities, including the library, bowling alley, movie theater and golf course. He cannot shop on Scott AFB in the Base Exchange or the Commissary or purchase fuel on Base. He cannot “vouch” a guest onto the Base, by calling the Visitor Center, tell them who is coming, for how long, and where they will be staying. He must drive to the nearby “Subway,” meet his guests who leave their car there, and drive them back to the Base. Ms. Baker testified that “[I]t took

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<sup>10</sup> Some military members live off-base. Members living off-base can use their housing allowance off-base. Approximately 80 military members are “key and essential,” as determined by the Commander, and must live on-base. Housing is provided to them almost immediately upon request. Other military members requesting houses can usually move into housing in one day. Tr. pp. 245-246.

us months to get that worked out where they would allow his mom to come on Base.”  
Tr. pp. 230-233, 246, 253-253.

Before the Property Manager will show a prospective tenant a property, the tenant needs a referral from Scott AFB’s “Military Housing Office.” Prospective tenants would show the Military Housing Office their military ID and a copy of their orders, which show spouse, children and dependents. The Military Housing Office bases the housing on the number of dependents, which determines the number of bedrooms the tenant is entitled to. Tr. pp. 241-242, 253.

There are currently 1,595 homes in the Project and 172 (11%) of the homes are occupied by non-target tenants.<sup>11</sup> These 172 homes are occupied by 115 “geographically single” military members (married military members who did not bring their spouse with them to Scott AFB) and guard and reserve members, 30 federal civil service employees, 26 [Air Force] retirees and one member of the “general public,” the Scott AFB maintenance supervisor, discussed above, who lives on the property. Tr. pp. 230-233, 246, 252-253.

Condition 19.6 of the Lease requires that each target tenant shall be required to sign a tenant lease, in a form approved by the Government, as included in the attachments to the Operating Agreement. SAFBP shall not make any “material revision” to the tenant lease agreement without the prior written approval of the Government. App. Ex. No. 3.

Similar to Rosewell where the City controlled the parking rates, SAFBP does not set the rental rate for the units. Condition 19.9 of the Lease requires that all units shall be designated by pay grade and entitlement and shall be made available to target tenants and

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<sup>11</sup> There was testimony that occupancy at Scott AFB and the new land was approximately 60% in 2006 and 2007 because new homes had not been built and anticipated improvements had not been completed. Occupancy rates increased in 2008 and 2009. Tr. pp. 248-249.

other eligible tenants in accordance with the Unit Occupancy Plan, included as an attachment to the Operating Agreement. App. Ex. No. 3.

Attachment B of the Operating Agreement is entitled the “Rental Rate Management Plan.” This Plan details how rent is going to be charged on each individual unit for various service members depending on their pay grade and housing allowance. The rent charged is equivalent to the basic allowance for housing that the military member receives, which is dependent on their rank, length of time in the service, and whether the member has dependents. SAFBP can set the rate for non-target tenants but the rate cannot be below the base allowance for housing. Non-target tenants receive a standard commercial-type lease. Tr. pp. 243-244. As in Rosewell, where the parking lot operators could not change the parking rates, SAFBP cannot change the rental rates. All changes to the rental rates are subject to the prior written approval of the Air Force. Tr. pp. 146-147; App. Ex. No. 13.

In addition, Condition 15.6.1 of the Lease requires SAFBP to offer renter’s insurance to each target tenant and other eligible tenant as part of the tenant lease application process. Such renter’s insurance shall be provided at the sole cost and expense of SAFBP. App. Ex. No. 3.

The Rental Rate Management Plan states that if a service member is promoted and wishes to move to a new house, then the service member’s new housing allowance will apply and a new one-year lease will be signed. The Property Manager will accept all referrals from Scott AFB’s Military Housing Office. The Property Manager will make available any vacant home to the appropriate grade individual at the top of the waiting list. Acceptance or rejection of the available home will be at the sole discretion of the referred military member. Lease agreements with tenants other than referred military

members will be limited to one-year duration. In the event that the general public is offered a home in the community, the Property Manager shall first locate the resident in the most “severable” location in the community. The Air Force reserves the right to refuse occupancy to other eligible tenants based on the result of a background check of available criminal files to determine any evidence of sex offense convictions, probation or parole for serious offenses or other credible evidence of current or past criminal misconduct. App. Ex. No. 13.

The Rental Rate Management Plan also states that the Air Force will have unrestricted access, through use of a web-based software program, to produce reports independently, or request reports on an as-needed basis. This capability includes the ability to view receivables, payables, property data, performance records and any other functions related to property operations. The Property Manager will hold quarterly property review meetings attended by personnel from the Air Force, *inter alia*. App. Ex. No. 13. Ms. Baker testified that she meets weekly with the Director of the Military Housing Office. She meets every other week with the Mission Support Group Commander. She meets monthly with the Wing Commander. Tr. pp. 234, 237-238.

Condition 26.1 of the Lease provides that, at all times during the Lease Term, the Government may inspect and request copies of any of SAFBP’s records, files, reports and related material pertaining to the assets and to the performance under the Lease. Condition 26.2 requires SAFBP, at its sole expense, to create, administer and comment upon the results of an annual customer satisfaction survey comprised of content and format to be provided by the Government. SAFBP shall be required to use the Government’s surveying company of choice to complete this task. App. Ex. No. 3.

The Government also exercises control over the accounts required by the Lockbox Agreement. Disbursement from the Operating Reserve Account and the Insurance and Condemnation Account shall be made pursuant to a disbursement request from an authorized officer of SAFBP, approved by the construction lender, the senior lender and the Government. App. Ex. No. 12. A portion of the compensation that SAFBP receives from the “Performance Incentive Account” is incentive based and dependent on the satisfactory evaluation of Scott AFB’s Wing Commander. This incentive is related to, *inter alia*, the number of maintenance responses, the level of occupancy, and whether SAFBP’s financial statements are delivered on time. Tr. pp. 239-240; SAFBP Memo., p. 15. Article V of the Lockbox Agreement requires that the Government, the construction lender, the senior lender and the lockbox agent, shall be provided such access to the property and the books and records of SAFBP, as shall be reasonably necessary to permit the parties to take all necessary action to assure the compliance by SAFBP with the Lockbox Agreement. App. Ex. No. 12.

In Rosewell, the agreement between the City and the parking lot operators listed seven categories of maintenance responsibilities to be assumed by the parking lot operators. *Id.* at 999. Similar to the City’s control over “maintenance” in the parking garages in Rosewell, the Facilities Maintenance Plan, included as an attachment to the Operating Agreement between SAFBP and the Government, requires that all proposed major landscape work, other than routine pruning, trimming, mowing and maintenance, be approved by the Wing Commander. App. Ex. No. 13. Ms. Baker testified that there are 22 general officers living on Scott AFB and two four-star generals. “They want to not only be informed but to approve whenever I trim a tree that either can be seen from the

four-star [general's] house, can be seen from the parade ground or can be seen from the main road into Scott [AFB].” Tr. p. 239.

The Government exerts other forms of control over SAFBP's employees. Paragraph 5(b) of the Lease requires that SAFBP's officers, agents, employees, independent contractors and subcontractors, must obtain identification passes from Scott AFB police before admission to the Base. Vehicles of such personnel must be registered with and issued temporary passes by Scott AFB before they may be driven onto the Base. The vehicles are subject to inspection by Scott AFB security police before temporary passes will be issued. App. Ex. No. 13.

The Government also exerts extensive control over the process of having visitors enter the Leased Premises. To get visitors on the Base, residents must call a visitor's center, and tell them who is coming, for how long and where they will be staying. This puts the visitors on an access list. The visitor then needs to go to the visitor's center, produce proof of identity and have their social security number checked for outstanding warrants before they are allowed on the Base. Tr. pp. 229-234. The “Unit Occupancy Plan,” an attachment to the Operating Agreement, states that social visits to military personnel assigned to Scott AFB are limited to 30 days. App. Ex. No. 13.

St. Clair County argues in its “Post-Hearing Brief” that “it is the nature of the property and the fact that it was and continues to operate as a United States Air Force Base that necessarily creates certain restrictions on the use of the property.” “There are certainly national security interests at stake with respect to the subject property, thereby restricting its use.” Int. Response, p. 16. Government control over security on Scott AFB is necessary for the highly important military purposes to which Scott AFB has been dedicated. However, the control exercised by the Government over the Leased Premises

goes beyond what is necessary for national security. St. Clair County fails to show how the Government's control over advertising and naming rights, rental and occupancy rates and landscape are related to national security.

In Rosewell, the agreement provided that the parking lot operators could not assign or transfer the agreement or any of the rights or privileges under it without the prior written approval of the City. *Id.* at 998. In Jackson Pk. Yacht Club v. Dept. of Gov't Affairs, 93 Ill. App. 3d 542 (1<sup>st</sup> Dist.1981), the court determined that the agreement that two yacht clubs had with The Chicago Park District were licenses rather than leases. The court noted that a license is not assignable and merely gives another the right to use the premises for a specific purpose with the owner retaining possession and control. In Jackson Park, the yacht clubs' permits were not assignable without the written consent of the Park District. *Id.* at 547.

Similar to Rosewell and Jackson Park, Condition 21.1 of the Lease between SAFBP and the Government states that SAFBP shall neither transfer nor assign the Lease or any interest therein or any property on the Leased Premises, nor sublet the Leased Premises, Leased Premises Improvements or any part or any property, nor grant any license, privilege or interest, without prior written consent of the Government. Such consent shall not be unreasonably withheld. An assignee must assume all of SAFBP's obligations and responsibilities under the Lease and the Operating Agreement. SAFBP cannot transfer or assign the Lease separate from its interest in the new land. App. Ex. No. 3.

However, pursuant to the Security Agreement between SAFBP and the Government, even if the Government were to give its consent to an assignment, the Government still retains a lien and security interest in the Leased Premises and SAFBP is

required to pay the Government 60% of the proceeds from such a transfer. Accordingly, any transferee would have to obtain a release of the lien from the Government or subject itself to the requirements of the Security Agreement. App. Ex. No. 8. These restrictions on SAFBP's ability to transfer its interest exceed those in Rosewell and Jackson Park, which were sufficient for the court to find that the disputed interests were licenses rather than leases.

In Charlton v. Champaign Park District, 110 Ill. App. 3d 554 (4<sup>th</sup> Dist. 1982), taxpayers challenged the right of the Park District to contract with a private party to build and operate a waterslide on Park District property. The court observed that it did not have to determine whether the Park District could lease its property because the contract was a license rather than a lease. Under the contract, the Park District established prices, similar to the Government setting rental rates in the instant case. Under the contract in Charlton, rates could not be raised more than 15% in any year without Park District approval. *Id.* at 560. In the instant matter, all changes to the rental rates are subject to prior written approval of the Air Force. Tr. pp. 146-147; App. Ex. No. 13.

In Charlton, the Park District had the power to discharge the private party's employees. *Id.* at 560. In Millennium Park Jt. Venture v. Houlihan, 393 Ill. App. 3d 13 (1<sup>st</sup> Dist. 2009), appeal allowed, 234 Ill. 2d 525 (Nov.25, 2009), the court noted that the Park District required that certain "key men" or "alternate key men" operate the facilities "to insure the quality of the plaintiff's operations." *Id.* at 27-28.

Section 3(a) of the Operating Agreement between SAFBP and the Government requires that SAFBP cannot enter into any "property management agreement" or agreement with a "management company" without the prior written approval of the Government. Tr. pp. 135-136; App. Ex. No. 13. On January 1, 2006, SAFBP entered into

a “Management Agreement” with American Management Services Central and HBC Property Managers Limited Partnership (hereinafter the “Property Manager”) to manage the Project, including the Leased Premises and the new land. American Management Services Central is no longer part of the management team. HBC is the sole property manager. Government approval was required for this change. Tr. pp. 137-138; App. Ex. No. 14.

In Atlantic Marine Corps Communities, LLC v. Onslow County, N.C., 497 F. Supp. 743 (E.D. N.C. 2007), the court noted that the “level of control retained by the United States under the Project” satisfied the court that the Government holds the lands subject to its primary jurisdiction and control. According to the court, under the terms of the Lease, the United States will be the sole owner of the land and the improvements at the end of the Lease term. Plaintiff is limited in its use of the subject lands to activities spelled out in the Lease.

This is similar to the situation in the instant matter. Condition 9.1 of the Lease states that upon termination of the lease, SAFBP shall remove all of the Leased Premises Improvements and its other property from the Leased Premises and restore the Leased Premises to the reasonable satisfaction of the Government. Funds to pay for such demolition and restoration shall be obtained from the “Replacement Reserve Account,” as defined in the Lockbox Agreement. Condition 9.5 of the Lease states that after any demolition of the Leased Premises Improvements requested by the Government, SAFBP shall “peaceably surrender possession” of the Leased Premises to the Government upon termination of the Lease. App. Ex. No. 3. According to the court in Atlantic Marine Corps, these and other control factors indicate that the Marine Corps Lands, as a whole, and the specific properties managed by the developer, continue to be used for military

purposes. “There is no indication that the government’s operation of the [Marine Corps Lands] will change in any significant respect in the wake of its agreement to join the Project with the [private property developer].” *Id.* at 758.

In the instant case, the Government granted SAFBP a Lease, subject to detailed and comprehensive restrictions on its use of the Leased Premises, solely as a means to facilitate financing for construction. The Lease has not deprived the Government of its “control” over the Leased Premises. SAFBP lacks exclusive possession over the Leased Premises and does not have a right of possession against the Government or “strangers.”

In considering all of the interdependent transactions and the scope of the MHPI Project in the instant case, I conclude that SAFBP received a contractual license for use of the Leased Premises and Leased Premises Improvements which did not rise to the level of a taxable interest in the property, notwithstanding the document’s denomination as a “Lease.”

For these reasons, I recommend that the Department’s determination be reversed, and that the Leasehold Interest not be assessed for tax purposes in the 2007 assessment year.

ENTER:

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Kenneth J. Galvin  
Administrative Law Judge

June 29, 2010