

ST 12-10
Sales Tax

Issue: Exemption From Tax (Charitable or Other Exempt Types)

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

THE DEPARTMENT OF REVENUE OF THE STATE OF ILLINOIS	}	No: XXXXX
v.		Sales Tax Exemption
ABC CLUB,		Kenneth J. Galvin Administrative Law Judge
TAXPAYER		

RECOMMENDATION FOR DISPOSITION

APPEARANCES: Mr. John Doe, *pro se*, on behalf of ABC Club; Ms. Paula Hunter, Special Assistant Attorney General, on behalf of the Department of Revenue of the State of Illinois.

SYNOPSIS: On June 21, 2011, the Illinois Department of Revenue (hereinafter the “Department”) denied ABC Club’s (hereinafter “ABC Club”) second request that the Department issue it an exemption identification number so that it could purchase tangible personal property at retail free from the imposition of use tax, as set forth in 35 ILCS 105/1 *et seq.* On August 12, 2011, ABC Club protested the Department’s decision and requested a hearing, which was held on March 13, 2012, with Mr. John Doe, Treasurer of ABC Club, testifying. The sole issue to be determined at the hearing was whether ABC Club qualified for an exemption identification number as “a corporation, society, association, foundation or institution organized and operated exclusively for charitable ... purposes.” 35 ILCS 105/3-5(4). Following a careful review of the evidence and

testimony presented at the hearing, I recommend that the Department's denial be affirmed.

FINDINGS OF FACT:

1. The Department's case, inclusive of all jurisdictional elements, is established by the admission into evidence of the Department's second denial of exemption dated June 21, 2011. Tr. p. 6; Dept. Ex. No. 1.
2. ABC Club was incorporated under the Illinois "General Not For Profit Corporation Act" in February, 1996. According to its Articles of Incorporation, ABC Club "was organized to provide the children of ABC Club with special events." "These include the fourth of July picnic and fireworks, Easter egg hunt, Halloween costume parade and bonfire." "The club also performs civic projects." "These civic projects vary based on the need and the amount of funds available to the club." Tr. pp. 10-11; App. Ex. No. 1.
3. ABC Club's Bylaws state that the club shall have one class of members: "A male resident of the village of ABC Club who is head of his household." Prospective members' names shall be submitted by a regular member (sponsor) to the Board of Directors. Members shall be elected by a majority vote of the Board of Directors. Any male residing out of the village shall be eligible for associate membership. An associate member shall not be eligible to vote or hold office. Acceptance of an associate member shall be by a majority vote of the Board of Directors. Dues of the regular and associate member "shall be a one-time fee of \$15" which may be changed. Tr. pp. 10-12; App. Ex. No. 1.
4. ABC Club is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. Tr. p. 16; App. Ex. No. 3.

5. In 2010, ABC Club received “personal donations” of \$28,338 and “corporate donations” of \$1,750 and incurred expenses for “event advertising,” of \$1,408, “children’s Easter egg hunt” of \$1,195, “4th of July fireworks” of \$22,052, “children’s Halloween party” of \$1,218 and “children’s Christmas party,” of \$362. Donations exceeded expenses by \$3,853. Tr. pp. 16, 20; App. Ex. No. 4.

CONCLUSIONS OF LAW:

The Use Tax Act (35 ILCS 105/1 *et seq.*) imposes a tax upon the privilege of using in Illinois tangible personal property purchased at retail from a retailer. 35 ILCS 105/3. Section 3-5 of the Act provides a list of tangible personal property that is exempt from tax, and includes the following: “(4) Personal property purchased by a governmental body, by a corporation, society, association, foundation or institution organized and operated exclusively for charitable, religious or educational purposes...[.]” “On or after July 1, 1987, however, no entity otherwise eligible for this exemption shall make tax-free purchases unless it has an active exemption identification number issued by the Department.” 35 ILCS 105/3-5(4). Section 2-5(11) of the Retailers’ Occupation Tax Act, 35 ILCS 120/1 *et seq.* contains a similar provision. (See 35 ILCS 120/2-5(11)).

ABC Club has requested an exemption identification number pursuant to these provisions, which the Department has twice denied on the basis that ABC Club did not demonstrate that it operates exclusively for charitable purposes. Dept. Ex. No. 1. The Department’s denial of an applicant’s claim for an exemption identification number is presumed to be correct, and the applicant has the burden of clearly and conclusively proving its entitlement to the exemption. See Wyndemere Retirement Community v.

Department of Revenue, 274 Ill. App. 3d 455, 459 (2d Dist. 1985). To prove its case, an applicant must present more than just testimony denying the Department's determination. Sprague v. Johnson, 195 Ill. App. 3d 798, 804 (4th Dist. 1990). Rather, the applicant must present sufficient documentary evidence to support its claim. *Id.*

It is well established in Illinois that there is a presumption against exemption and that therefore, "exemptions are to be strictly construed" with any doubts concerning the applicability of the exemptions "resolved in favor of taxation." Van's Material Co. Inc. v. Department of Revenue, 131 Ill. 2d 196 (1989). The applicant bears the burden of proving "by clear and convincing" evidence that the exemption applies. Evangelical Hospitals Corp. v. Department of Revenue, 223 Ill. App. 3d 225 (2d Dist. 1991).

Although it was in a case concerning a property tax exemption, the Illinois courts have used guidelines set forth in Methodist Old Peoples Home v. Korzen, 39 Ill. 2d 149 (1968), in determining whether an entity qualifies as one organized and operated exclusively for charitable purposes. Wyndemere Retirement Community, *supra*. These guidelines are: (1) the benefits derived are for an indefinite number of persons [for their general welfare or in some way reducing the burdens on government]; (2) the organization has no capital, capital stock or shareholders; (3) funds are derived mainly from private and public charity, and the funds are held in trust for the objects and purposes expressed in the charter; (4) the charity is dispensed to all who need and apply for it, and does not provide gain or profit in a private sense to any person connected with it; (5) the organization does not appear to place obstacles of any character in the way of those who need and would avail themselves of the charitable benefits it dispenses. Korzen, *supra* at 156-57. The evidence and testimony presented at the hearing were not

sufficient for me to conclude that ABC Club is a charitable institution or that its activities are charitable in accordance with the guidelines set forth in Korzen.

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According to ABC Club’s financial statements, the organization derives the majority of its funds from public and private charity. In 2010, ABC Club received “personal donations” of \$28,338 and “corporate donations” of \$1,750. ABC Club used the funds received for event advertising, a children’s Easter egg hunt, 4th of July fireworks, a children’s Christmas party and a children’s Halloween party. Of the approximately \$30,000 received by ABC Club in donations in 2010, \$22,052 or 73% was used for the 4th of July fireworks.¹ App. Ex. No. 4.

I find no support in Illinois case law for concluding that providing children with “special events,” including sponsoring children’s parties and a 4th of July fireworks display, constitute “charity.” Charity, in the legal sense, may be defined as a gift, for an indefinite number of persons, either by bringing their hearts under the influence of

¹ Mr. Dill testified as to several “projects” that Sleepy Hollow has worked on. Tr. pp. 13-15. No documentary evidence was admitted to support the testimony. The only documentary evidence showing Sleepy Hollow’s projects and activities is the unaudited financial statement listing the expenditures for 2010. App. Ex. No. 4.

education or religion, by relieving their bodies from disease, suffering or constraint, by assisting them to establish themselves for life, or by erecting or maintaining public works, or otherwise lessening the burdens of government. Crerar v. Williams, 145 Ill. 625, 643 (1983). Special events, including children's parties and fireworks displays, do not recognizably relieve a body from disease or suffering or assist participants to establish themselves for life.

Additionally, ABC Club is not relieving a burden on government. The reason for exemptions in favor of charitable institutions is the benefit conferred upon the public by them, and a consequent relief, to some extent, of the burden upon the State to care for and advance the interests of its citizens. People v. Young Men's Christian Association of Chicago, 365 Ill. 118, 122 (1936). "Conditioning charitable status on whether an activity helps relieve the burdens on government is appropriate." Each tax dollar lost to a charitable exemption is one less dollar affected governmental bodies will have to meet their obligations directly. If a charitable institution wishes to avail itself of funds which would otherwise flow into a public treasury, it is only fitting that the institution provides some compensatory benefit in exchange. Provena Covenant Medical Center v. Department of Revenue, 236 Ill. 2d 368, 395 (2010).

The problem with ABC Club's request for a sales tax exemption, and the reason that I cannot recommend it, is that ABC Club's special event expenditures are not reducing a burden on government. Mr. John Doe did not refer me to, and my own research does not indicate, any Illinois statute requiring a city or county to sponsor a children's Halloween, Christmas or Easter egg party or a fireworks display. Mr. John Doe argued that it is a "very common occurrence for all municipalities in Illinois" to sponsor such activities. Tr. p. 19. The public may find these activities enjoyable, but

without a legal mandate requiring a municipality to sponsor them, there is no “compensatory benefit” or “consequent relief” of a burden upon the State. It may be a “common occurrence” for a city or county to have fireworks, as Mr. John Doe suggests, but I am unable to conclude that a city or county has a “burden” to do so.

Additionally, there is no testimony or evidence in the record as to the standards utilized by ABC Club for determining how to spend its funds. Because ABC Club offered no evidence as to the standards used to determine which events to sponsor, it cannot clearly and convincingly be found that ABC Club does not place obstacles in the way of those who need and would avail themselves of the benefits it dispenses. The Korzen criteria that a charitable organization place no obstacles in the way of those needing its benefits is “more than a guideline.” It is an “essential criteria” and it “goes to the heart of what it means to be a charitable institution.” Provena Covenant Medical Center v. Department of Revenue, 384 Ill. App. 3d 734, 750 (4th Dist. 2008), aff’d, 236 Ill. 2d 368 (2010). The fact that the record does not allow me to conclude that this guideline is met by ABC Club weights heavily against them.

Moreover, according to ABC Club’s Bylaws, the organization has “one class of membership” defined as follows: “A male resident of the village of ABC Club who is head of his household.” Membership was not specifically discussed by Mr. John Doe at the hearing but it appears that the “one class of membership,” described in the Bylaws, includes ABC Club’s fathers. In addition, any male residing outside of the village shall be eligible for associate membership. An associate member shall not be eligible to vote or

hold office.² Dues of the regular and associate member “shall be a one-time fee of \$15” which may be changed. Tr. pp. 10-12; App. Ex. No. 1.

The fact that ABC Club is a membership organization is evidence that it exists to serve a limited class of persons, namely male, heads-of-household. Department Regulation 2005(g) notes that organizations whose activities primarily serve to benefit its members are not operated exclusively for charitable purposes even though such organizations may engage in some charitable work. 86 Ill. Adm. Code. §130.2005(g). In Albion Ruritan Club v. Dep’t. of Revenue, 209 Ill. App. 3d 914, 918 (5th Dist. 1991), the court found that a community service organization’s property did not warrant a tax exemption. Albion’s constitution listed its objectives, *inter alia*, as “[T]o promote fellowship and good will among its members and the citizens in the community, and to inspire each other to higher efforts.” In denying a property tax exemption to Albion, the court noted that “it must be shown that the benefits accrue to mankind directly; it is not sufficient that incidental benefits accrue to the public as a result of the property’s use.” Similarly, in Rogers Park Post No. 108 v. Brenza, 8 Ill. 2d 286, 291-292 (1956), the Court found that the primary purpose of the membership organization was “to foster love of country, respect for our civil institutions and to benefit and afford comradeship to its members.” Fostering “love of country” is strikingly similar to ABC Club’s sponsorship of the 4th of July fireworks display. According to the Court in Rogers Park, the organization’s purposes were “patriotic, laudable and public spirited.” “Nonetheless, they do not constitute charitable purposes, however desirable or however beneficial.” The Court found that the activities of the Rogers Park Post “stamp it” plainly as patriotic and social, but not as charitable.

² “Associate membership” would appear to be another “class of membership,” in contravention of the Bylaws. No explanation was offered for this.

I am unable to conclude from the very limited record in this case and the lack of evidence on how ABC Club determines which programs to sponsor, whether the benefits of its special events accrue to “mankind directly,” as required by Albion, supra, or primarily serve to benefit its membership. If the primary benefit of an organization flows to its members and not the public, then an exemption will be denied. Board of Certified Safety Professionals of the Americas v. Johnson, 112 Ill. 2d 542, 547 (1986); Chicago Bar Association v. Department of Revenue, 177 Ill. App. 3d 896 (2d Dist. 1988).

In addition, prospective ABC Club members must be sponsored by a regular member and elected by a majority vote of the Board of Directors. Acceptance of an associate member is by a majority vote of the Board of Directors. App. Ex. No. 1. These restrictions on membership again indicate that ABC Club’s primary purpose is social rather than charitable. It is reasonable to conclude that ABC Club could be a group of fathers meeting socially to sponsor activities for their children. An organization must be exclusively charitable to be exempted from sales tax. An “exclusively” charitable purpose need not be interpreted literally as the entity’s sole purpose; it should be interpreted to mean the primary purpose, and not a merely incidental or secondary purpose or effect. Gas Research Institute v. Department of Revenue, 154 Ill. App. 3d 430 (1st Dist. 1987). The limited record in this case does not allow me to conclude that the special events sponsored by ABC Club are not “incidental” and secondary to the social benefits of membership for male, heads-of-household, in this club.

Given the nature of ABC Club’s expenditures, it is difficult to justify granting the organization an exemption number. An exemption identification number might well be used to reduce ABC Club’s costs of putting on its Halloween, Christmas and Easter parties and fireworks display, but not directly used to further any charitable activities that

would relieve a burden on government. Tax exemptions are inherently injurious to public funds because they impose lost revenue costs on taxing bodies and the overall tax base. Such detriments can only be warranted if lost resources are otherwise used to directly benefit the public through the support of truly charitable expenditures.

For the above stated reasons, I recommend that the Department's second determination denying the applicant a sales tax identification number be affirmed.

ENTER:

Kenneth J. Galvin

July 17, 2012