

ST 12-12

Tax Type: Sales Tax

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

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

THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS,

v.

EXCELLENCE UNIVERSITY,

APPLICANT

Docket No: XXXXX

Sales Tax Exemption

Kenneth J. Galvin
Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

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

SYNOPSIS: On October 26, 2011, the Illinois Department of Revenue (hereinafter the “Department”) denied Excellence University’s (hereinafter “EU”) 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 November 4, 2011, EU protested the Department’s decision and requested a hearing, which was held on July 17, 2012, with Mr. John Doe, President, Mr. Black and Mr. White, EU students, testifying. The sole issue to be determined at the hearing was whether EU qualified for an exemption identification number as “a

corporation, society, association, foundation or institution organized and operated exclusively for educational ... 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 *prima facie* case, inclusive of all jurisdictional elements, is established by the admission into evidence of the Department’s second denial of exemption dated October 26, 2011. Tr. p. 4; Dept. Ex. No. 1.
2. EU, located in Anywhere, USA, offers a Master of Science Degree in Martial Arts and an “Associate of Occupational Studies in Business Administration and Entrepreneurship” with a major in Martial Arts/Taekwondo.” “The curriculum at EU has a strong foundation in the traditional roots of martial arts.” Tr. pp. 5-6, 11; App. Ex. Nos. 1, 4, 7 and 8.
3. The Master of Science Degree in Martial Arts is a two year program. “Traditional methods of martial arts are taught.” “Classes are taught by Professors and Grand Masters.” The Associate Degree is also a two year program “in which students are prepared for both the business management and the teaching side of the Martial Arts Center ownership.” “The curriculum includes courses in management, instruction, training techniques, emotional development, promotions, judging and referring, martial arts business research and other topics related to martial arts instructions and running a martial arts facility.” Tr. pp. 8-9, 12; App. Ex. Nos. 8 and 9.
4. The purpose of EU, according to its Bylaws, is to establish and operate a school for eligible students of any race, color or creed. Tr. p. 6; App. Ex. No. 6.

5. EU is exempt from income tax under section 501(c)(3) of the Internal Revenue Code. Tr. p. 6; App. Ex. No. 2.
6. EU is exempt from sales tax in the State of Anywhere, USA. Tr. p. 6; App. Ex. No. 3.
7. EU's Income Statement for December 31, 2010 shows "Tuition and Other Income" of \$XXXXXX, "Operating Expenses" of \$XXXXXX, resulting in a "Net Income" of \$XXXXXX. The largest Operating Expenses are for Payroll (\$XXXXXX), Rent (\$XXXXXX) and Repairs and Maintenance (\$XXXXXX). Tr. p. 9; App. Ex. No. 10.

CONCLUSIONS OF LAW:

An examination of the record establishes that EU has not demonstrated, by the presentation of testimony or through exhibits or argument, evidence sufficient to warrant an exemption from use tax. Accordingly, under the reasoning given below, the determination by the Department denying EU a sales tax exemption number should be affirmed. In support thereof, I make the following conclusions.

The Use Tax Act ("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 free from imposition of the 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." 35 ILCS 105/3-5(4). Section 2-5(11) of the Retailers' Occupation Tax Act ("ROTA") contains a similar provision. 35 ILCS 120/2-5(11).

The Department's denial of the taxpayer's claim for an exemption identification number is presumed to be correct, and the taxpayer has the burden of clearly and conclusively proving that it is entitled to the exemption. Wyndemere Retirement Community v. Department of Revenue, 274 Ill. App. 3d 455 (2nd Dist 1995). To prove its case, a taxpayer must present more than testimony denying the Department's determination. The taxpayer must present sufficient documentary evidence to support its claim. Sprague v. Johnson, 195 Ill. App. 3d 798 (4th Dist. 1990). It is well established that there is a presumption against exemption and that therefore, "exemptions are to be strictly construed" with any doubts concerning the applicability of the exemption "resolved in favor of taxation." Van's Material Co. Inc. v. Department of Revenue, 131 Ill. 2d 196 (1989). In the instant case, there is insufficient documentary evidence in the record for me to conclude that EU is entitled to a sales tax exemption number.

Pursuant to its authority under Section 12 of ROTA (35 ILCS 120/12), the Department of Revenue promulgated 86 Ill. Admin. Code § 130.2005. This regulation acknowledges that there is no specific exemption in the Illinois Constitution for "educational purposes" as to any kind of tax, but Section 6, Article IX of the Constitution authorizes the General Assembly to grant a property tax exemption for property that is used for "school purposes." "Consequently the Department will construe the Retailers' Occupation Tax exemption for 'educational purposes' as meaning for 'school purposes,' as the phrase 'school purposes' has been interpreted or may be interpreted by the Supreme Court." 86 Ill. Admin. Code § 130.2005 (1)(1). The Illinois Supreme Court has concluded that an institution is not organized for "school purposes" unless the institution: (1) offers an established, commonly accepted program of academic instruction, which compares favorably with courses of study offered in tax-supported schools; and (2)

substantially lessens what would otherwise have been a government obligation. A school, within the meaning of the constitutional provision, is a place where systematic instruction in useful branches is given by methods common to schools and institutions of learning. See Coyne Electrical School v. Paschen, 12 Ill.2d 387, 392-293 (1957); 86 Ill. Admin. Code 130.2005(1)(2).

The purpose of EU, according to its Bylaws, is to establish and operate a school for eligible students of any race, color or creed. Tr. p. 6; App. Ex. No. 6. EU is exempt from income tax under section 501(c)(3) of the Internal Revenue Code. Tr. p. 6; App. Ex. No. 2. EU is exempt from sales tax in the State of Anywhere, USA. Tr. p. 6; App. Ex. No. 3. Mr. John Doe testified that EU was created in 2006. “We started as a private school with six students...” EU is seeking the sales tax exemption because it “needs a lot of supplies, operation and furniture.” “Anywhere, USA does not have a big store, so we come to Illinois to shop for furniture and office supplies.” “So every time we come, we have to pay the tax.” “So we applied to the State of Illinois because we come to buy many supplies from the Anywhere area.” Tr. pp. 11-12.

EU has failed to prove that its course of study fits into the scheme of education offered by public schools. EU offers a Master of Science Degree in Martial Arts and an “Associate of Occupational Studies in Business Administration and Entrepreneurship” with a major in Martial Arts/Taekwondo. “The curriculum at EU has a strong foundation in the traditional roots of martial arts.” Tr. pp. 5-6, 11; App. Ex. Nos. 1, 4, 7 and 8. The Master of Science Degree in Martial Arts is a two year program. “Traditional methods of martial arts are taught.” “Classes are taught by Professors and Grand Masters.” The Associate Degree is also a two year program “in which students are prepared for both the business management and the teaching side of the Martial Arts Center ownership.” “The

curriculum includes courses in management, instruction, training techniques, emotional development, promotions, judging and referring, martial arts business research and other topics related to martial arts instructions and running a martial arts facility.” Tr. pp. 8-9, 12; App. Ex. Nos. 8 and 9.

EU did not offer its course catalog into evidence.¹ EU did not offer a written description of its curriculum into evidence. EU did not offer a school calendar into evidence. There is no evidence in the record that EU offers courses in traditional disciplines such as reading, writing, mathematics, history or literature. Whereas EU’s instruction in the martial arts may be informative and thus “educational” in the broadest sense of the word, there is no evidence in the record that EU’s activities involve instruction in traditional academic subject areas such as those offered in tax supported schools. Without a course catalog, description of the curriculum and a school calendar, I am unable to conclude that EU offers “systemic instruction” within the meaning of the constitutional provision for “schools.” Mr. Black testified that “Master John Doe runs an institution of higher learning similar to any other university or college.” Tr. p. 13. I cannot reach this same conclusion without a school calendar and course catalog and documentary evidence regarding the curriculum. The deficiencies in the evidence do not allow me to conclude that EU’s course of study fits into the scheme of education offered by public schools.

The record in this case is also devoid of any evidence that the martial arts and taekwondo instruction offered by EU substantially lessens what would otherwise have

¹ In a letter dated January 31, 2011, from the Provost of AU to the Department’s Litigator, the Provost stated that AU did not have a printed catalog as “we are a very small university with average graduating classes of 7 or 8.” App. Ex. No. 1. AU’s Income Statement for December 31, 2010 shows “Printing and Copying” costs of \$3,597.

been a government obligation. EU has not referred me to, and my own research does not indicate, any Illinois statute or regulation that would require the State to offer either Masters Degrees or Associates Degrees in martial arts or taekwondo. If EU were not in operation, the taxpayers of Illinois would not be obliged to support a school that offered training in martial arts or taekwondo. I am unable to conclude from the very limited record in this case that there would be a “public gain” that would inure to the people of Illinois from releasing EU from its burden of paying sales tax, and its request for exemption must therefore fail. *Id.* at 857-858.

Tax exemptions are inherently injurious to public funds because they impose lost revenue costs on taxing bodies and the overall tax base. In order to minimize the harmful effects of such lost revenue costs, and thereby preserve the Constitutional and statutory limitations that protect the tax base, statutes conferring tax exemptions are to be strictly construed in favor of taxation. People ex rel. Nordland v. Home for the Aged, 40 Ill. 2d 91 (1968). In addition, great caution must be exercised in determining whether an institution is organized and operated exclusively for educational purposes. Otherwise, any increases in lost revenue costs attributable to unwarranted application of the use tax exemption will cause damage to public treasuries and the overall tax base. In this case, EU has failed to prove that it falls within the limited class of organizations that the Legislature meant to be exempt from use tax purchases of tangible personal property.

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

ENTER: September 20, 2012

Kenneth J. Galvin