

ST 14-30

Tax Type: Sales Tax

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

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

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS,
v.**

ABC FOUNDATION.

APPLICANT

**No: XXXX
Sales Tax Exemption Number**

**Kenneth J. Galvin
Administrative Law Judge**

RECOMMENDATION FOR DISPOSITION

APPEARANCES: Mr. John Doe, *pro se*, on behalf of ABC FOUNDATION, Mr. Daniel Edelstein, Special Assistant Attorney General, on behalf of the Department of Revenue of the State of Illinois.

SYNOPSIS: On September 6, 2013, the Department of Revenue of the State of Illinois (hereinafter the “Department”) issued a “Denial of Sales Tax Exemption” to ABC FOUNDATION (hereinafter the “Academy”) denying its 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 retailers’ occupation tax as set forth in 35 ILCS 105/1 *et seq.* On October 13, 2013, the Academy protested the Department’s decision and requested an administrative hearing which was held on June 3, 2014 with Mr. John Doe, President, and Mr. Jack Black, Treasurer, testifying.

The sole issue to be determined at the hearing was whether the Academy 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 denial of exemption dated September 6, 2013. Tr. pp. 8-9; Dept. Ex. No. 1.
2. "The Mission of ABC FOUNDATION is to support the Academy and to enhance the knowledge and effectiveness of those who create healthcare environments through the funding of critical educational and research activities." The Academy originated as a Committee. Tr. pp. 37-40; Taxpayer's Ex. C.
3. The Academy is formed under the Texas "Non-Profit Corporation Act," and its principal office is in Dallas. The Academy is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. The business and affairs of the Academy are managed by a Board of Trustees, which is not compensated. The Academy does not issue shares or pay dividends. Tr. pp. 18-19, 26, 50-51; Taxpayer's Ex. A, B and O.
4. In 2013, the Academy received donations from 22 individuals who were mostly architects, and healthcare architectural firms. Tr. pp. 19-21, 35-36, 47-48, 54-55; Taxpayer's Ex. G and I.
5. The Academy allocated up to \$XXXX for 2013-2014 research studies and sought proposals focusing on three areas: the impact of integrated project delivery on the practice of healthcare architecture; emerging models and typologies for ambulatory care centers, medical homes and physician practices; and how lean practices for healthcare delivery are affecting design. Tr. pp. 24-25; Taxpayer's Ex. C.

6. The Academy has sponsored the following completed studies: Comparative Analysis of Hospital Energy Use; Optimizing Toilet Location for Assisted Toileting; Environmental Correlates of Safety and Efficiency in Emergency Departments; Area Calculation and Net-Gross Ratios in Hospital Design; Understanding Hospital Staff Perceptions of Relative Efficacy of Various Charting and Collaborative Space Configurations in Acute Care Inpatient Units Using Electronic Medical Records; Patient Room Handedness and Caregiver Body Mechanics; Does the Size and Design of Family Areas within Patient Rooms Increase Family Involvement in Patient Care; Validating New Acoustic Guidelines for Healthcare Facilities Using a Collaborative and Trans-Disciplinary Approach for Improving Patient Outcomes; Impact of Single Family NICU Rooms on Family Behavior; Integrated Knowledge Database; Analysis of Departmental Areas in Contemporary Hospitals; and Development of Webinars for the Academy of Architecture for Health. Tr. pp. 14-16, 52-57, 59-60; Taxpayer's Ex. L and M.
7. The Academy has sponsored the following studies, not yet completed: Cross Cultural Comparison of Inpatient Nursing Units; Malawi Maternal Waiting Rooms; Value Analysis of Lean Process in Integrated Project Delivery; and Designing Team Spaces to Support Collaboration and Communications in Patient Centered Medical Homes. Tr. pp. 52-57, 59-60; Taxpayer's Ex. M.
8. The grantees of the studies publish their research and give presentations of the results. Attendees at the presentations, if they are architects, may fulfill continuing educational requirements. Presentations are attended by owners, interior designers, consultants, researchers, engineers, architects, healthcare consultants, hospital administrators, nurses and doctors. Tr. pp. 17, 30-31, 57, 60-61.

9. The Academy does not offer any classes. Tr. pp. 29-30.
10. The “Summer Leadership Summit” is held yearly in Anywhere. It is a “day and a half long educational event” starting Friday afternoon. The Academy has a fundraising event on Friday night to raise funds to pay for the research grants. The Academy does not sponsor any educational content at the Summit. Tr. pp. 63-65.

CONCLUSIONS OF LAW:

Section 2-5 of the Retailers’ Occupation Tax Act (“ROTA”) provides that gross receipts from the sale of tangible personal property sold to a corporation, society, association, foundation or institution organized exclusively for charitable purposes are exempt from tax imposed by the ROTA. 35 ILCS 120/2-5(11). Section 3-5 of the Use Tax Act (“UTA”) complements Section 2-5(11) of the ROTA and provides in pertinent part that use of the following tangible personal property is exempt from tax imposed by the UTA: Personal property purchased by a government body, by a corporation, society, association, foundation, or institution organized and operated exclusively for charitable purposes. 35 ILCS 105/3-5(4).

The Academy seeks to qualify 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); 35 ILCS 120/2-5(11). As statutory provisions exempting property or entities from taxation, Section 2-5(11) of the ROTA and Section 3-5(4) of the UTA must be strictly construed against exemption 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 taxpayer, in this case the Academy, 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).

All debatable questions must be resolved in favor of taxation. People ex rel. Nordland v. The Assoc of the Winnebago Home for the Aged, 40 Ill. 2d 91 (1968).

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

In Methodist Old People's Home v. Korzen, 39 Ill. 2d 149 (1968), (hereinafter "Korzen") the Illinois Supreme Court outlined several factors to be considered in assessing whether an organization is actually an institution of public charity: (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; and (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.

The above factors are guidelines for assessing whether an institution is a charity, but are not definitive requirements. DuPage County Board of Review v. Joint Comm'n on Accreditation of Healthcare Organizations, 274 Ill. App. 3d 461 (2d Dist. 1995). Thus, a rigid formula is not to be applied to all fact situations but instead "courts consider and balance the guidelines by examining the facts of each case and focusing on whether and how the institution serves the public interest and lessens the State's burden." *Id.* at 469.

In determining whether an organization is exclusively charitable in its purpose, it is proper to consider provisions of its charter. Rotary International v. Paschen, 14 Ill. 2d 387 (1987). The Academy's Mission, as stated in its "Request for Proposal Guidelines," is "to support the Academy of Architecture for Health and to enhance the knowledge and effectiveness of those who create healthcare environments through the funding of critical educational and research activities." Tr. pp. 37-40; Taxpayer's Ex. C. Enhancing the knowledge and effectiveness of those who create healthcare environments is not an endeavor recognized by Illinois courts as inherently "charitable." The Academy has not referred me to, and my own research does not indicate, any case in Illinois where an organization whose main purpose was to enhance the knowledge and effectiveness of those who create healthcare environments was found to be exclusively charitable.

Moreover, I am unable to conclude that the Academy lessens a burden on government, which according to Korzen, is a "distinctive characteristic" of a charitable organization. The fundamental ground upon which all exemptions in favor of charitable institutions are based is the benefit conferred upon the public by them and a consequent relief, to some extent, of the burdens upon the state to care for and advance the interests of its citizens. School of Domestic Arts and Sciences v. Carr, 322 Ill. 562 (1926). For example, public education is a governmental "burden" according to the Illinois Constitution because the State "has the primary responsibility for financing the system of public education." Ill. Const., art. X, § 1. My research indicates that there is no governmental burden to "fund critical educational and research activities" which will enhance the effectiveness of health care environments. There is no Illinois statute requiring the State to enhance the effectiveness of health care environments. No evidence was offered that the government requested the research that was funded by the Academy.

35 ILCS 105/3-5(4) requires that an organization be operated “exclusively” for charitable purposes in order to qualify for a sales tax exemption. The word “exclusively” as used in the phrase “organized exclusively for charitable purposes” has been defined by the Department in a regulation promulgated pursuant to the authority of the ROTA. Regulation 2005(n) provides that if a substantial purpose or activity of the purchaser is not charitable, the Department will not consider the purchaser to be organized and operated exclusively for charitable purposes within the meaning of the ROTA. 86 Ill. Adm. Code § 130.2005(n). An “exclusively” charitable purpose need not be interpreted literally as the entity’s sole purpose; it should be interpreted to mean the primary purpose, but not a merely incidental or secondary purpose or effect. Gas Research Institute v. Department of Revenue, 154 Ill. App. 3d 430, 436 (1st Dist. 1987). The word “charity” or “charitable” does not appear in the Academy’s Mission Statement. It would defy logic to conclude that the Academy is “exclusively charitable” or that its primary purpose is charitable, as required by Illinois statutes, when there is no distinctly charitable purpose noted in its Mission Statement.

Department Regulation 2005(g), entitled “Nonprofit Professional and Trade Associations” notes that organizations “which draw their funds largely from their own members,” and as to which an important purpose is to protect and advance the interests of their members in the business world, are not organized and operated exclusively for charitable purposes, even though such organizations may engage in some charitable work. 86 Ill. Adm. Code § 130.2005(g). In 2013, the Academy received donations from 22 individuals who were mostly architects, and healthcare architectural firms. Tr. pp. 19-21, 35-36, 47-48, 54-55; Taxpayer’s Ex. G and I. Clearly, the Academy draws its funding from those people interested in the healthcare architecture field. Furthermore, as pointed out by the Department’s Counsel in his closing argument, many of the donors to the Academy are also recipients of educational grants

from the Academy. Tr. pp. 67-68. Based on the record, I must conclude that the primary purpose of the Academy is to advance the interest of healthcare architects and firms in that field. To infer a charitable purpose to the healthcare architects and firms who donate to the Academy and who may subsequently receive educational grants is not realistic.

It was unclear to me, even after the evidentiary hearing, what exactly the “charity” is that the Academy was dispensing. The Academy’s “2013 Year End Summary” does not show any expenditures for charitable purposes. Taxpayer’s Ex. G. I deduce from the testimony that Mr. John Doe and Mr. Jack Black assumed that the Academy’s research studies were “charity.” Mr. John Doe was asked whether a “member of the public who isn’t proposing to do any research for the Academy [could] still receive funds from the Academy.” He responded that “someone in my judgment could receive funding outside of research which is compatible with our mission.” But “to this point,” that has not happened. Tr. p. 42. Funding has only gone to persons or firms connected to the healthcare architecture field or architecture related departments at universities. Accordingly, if the research studies are “charity,” it is charity for architects only since no provision has yet been made to the public. The record does not allow me to conclude that the Academy benefits an indefinite number of persons.

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 Ass’n, 365 Ill. 118 (1936). Funds that are being used to benefit a profession are conferring a direct benefit on the profession, but not the public. Tax exemptions are to be strictly construed since they are inherently injurious to public funds because they impose lost revenue costs on taxing bodies. Gas Research Institute v. Dep’t, 154 Ill. App. 3d 430 (1st Dist. 1987). These lost public funds may, in

fact, be otherwise used to fund state programs that benefit the public at large, rather than the members of a professional society.

One of the characteristics of a charitable organization according to Korzen is that the organization not place obstacles in the way of those who would avail themselves of its charitable benefits. If the Academy's research studies are "charity," limiting the funding of the studies to those connected to the healthcare architecture field is an obstacle to the public receiving this charity. It is impossible to conclude from the record that whatever "charity" the Academy is dispensing through its research studies is dispensed to all who need it.

Mr. John Doe testified that if you "look at the facts of what we have funded over the past 14 years, they focus on energy, energy efficiency, that could mean patient safety, patient falls, designing appropriate environments for care in emergency rooms, efficiency care." He identified a "variety of users" of the research studies, including architects, interior designers, planners and hospital administrators. Tr. p. 32.

But it is unclear from the records how the benefits of the Academy's research studies extend to the public at large. There is no immediate and obvious windfall to the public from the Academy's activities. A patient in a hospital may find himself in a safer and healthier environment with less chance of falling. But I can no more attribute that enhanced safety to the Academy's research studies than I can to the hospital's for-profit janitorial service. So any positive effect on the public from the Academy's studies is indirect and incidental and is not the primary or substantial purpose or effect necessary to warrant the granting of a charitable tax exemption. Gas Research Institute v. Dep't. of Revenue, 154 Ill. App. 3d 430 (1st Dist. 1987).

Another guideline from Korzen is that the organization has no capital, capital stock or shareholders and that the organization not provide gain or profit in a private sense to those connected to it. The Academy was formed under the Texas "Non-Profit Corporation Act," and

its principal office is in Dallas. There is no evidence in the record that any of the Academy's research studies were granted to architects, firms or universities in Illinois. Taxpayer's Ex. M. The only connection that the Academy has with Illinois appears to be the "Summer Leadership Summit," held yearly in Anywhere. This Summit is a "day and a half long educational event" starting Friday afternoon. The Academy has a fundraising event on Friday night to raise funds to pay for the research grants. The Academy does not sponsor any educational content at the Summit. Tr. pp. 63-65. There is no testimony in the record that the Academy dispenses any "charity" at the Summit.

The Academy is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. The business and affairs of the Academy are managed by a Board of Trustees, which is not compensated. The Academy does not issue shares or pay dividends. Tr. pp. 18-19, 26, 50-51; Taxpayer's Ex. A, B and O. Although the Academy does possess these characteristics of a charitable organization, it is simply not enough for me to recommend granting the Academy a sales tax exemption.

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

December 7, 2014

Kenneth J. Galvin
Administrative Law Judge