

PT 08-14
Tax Type: Property Tax
Issue: Charitable Ownership/Use

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

THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS

v.

COULTERVILLE CARE, INC.

Applicant

Docket # 07-PT-0008
PIN 16-043-056-50

Tax Year 2006

RECOMMENDATION FOR DISPOSITION

Appearances: Robin Gill, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Alan R. Farris, Attorney at Law, for Coulterville Care, Inc.

Synopsis:

This case concerns whether a parcel of property located in Randolph County that contains a long-term skilled nursing care facility should be exempt from property taxes for the year 2006. Coulterville Care, Inc. (“applicant”) owns the property and alleges the property should be exempt pursuant to section 15-65 of the Property Tax Code (35 ILCS 200/15-65) on the basis that the property is both owned by a charitable organization and used exclusively for charitable purposes. The County Board of Review recommended that the exemption be granted. The Department of Revenue (“Department”) reviewed the

Board's decision and determined that the exemption should be denied on the basis that the property is neither owned by a charitable organization nor used for charitable purposes. The applicant timely protested the Department's decision, and an evidentiary hearing was held. After reviewing the record, it is recommended that this matter be resolved in favor of the Department.

FINDINGS OF FACT:

1. The applicant is an Illinois not-for-profit corporation that was organized on July 20, 1995; it has no capital, capital stock, or shareholders. (App. Ex. A; Tr. pp. 19-20)
2. The applicant is exempt from federal income taxes under section 501(c)(3) of the Internal Revenue Code pursuant to a determination made by the IRS on May 15, 2007. The applicant is exempt from retailers' occupation taxes and use taxes pursuant to a determination made by the Department on May 9, 2003. (App. Ex. D, E)
3. The original articles of incorporation indicate the purpose of the corporation is to provide charitable, civic, and social services as a not-for-profit. The articles, as amended, indicate, *inter alia*, that the "corporation is organized exclusively for charitable, education, religious or scientific purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code." (App. Ex. A, B)
4. The applicant operates a 75-bed Medicaid and Medicare-certified skilled nursing care facility in the Village of Coulterville ("Village"). The facility is known as Coulterville Care Center ("Center"). (Dept. Ex. #1; App. Ex. I, p. 151)

5. The property on which the Center was built was donated to the Village, and the Village donated it to the applicant in 1998. The Village financed the construction of the Center by issuing bonds, which were the sole source of funding. The Center was expected to open June 1, 1999, but due to delays in construction, it did not open at that time. (Dept. Ex. #1; App. Ex. F; Tr. pp. 14-15, 20-22)
6. The Village sold revenue bonds, 1998 Series A for \$3,615,000, 1998 Series B for \$245,000 and 1998 Series C for \$140,000. The proceeds were used to construct and furnish the Center and to pay for the costs relating to the development of the Center. The debt is due in various annual installments plus semi-annual interest payments and is secured by all of the real and personal property of the Center. (App. Ex. I, p. 154)
7. According to the Official Statement concerning the bonds, if the Center failed to achieve a census of 77% during the year 2000, it would have a material adverse effect on the Center's gross revenue and the applicant's ability to make payments on the bonds. The applicant did not achieve a 77% census during 2000. (App. Ex. F, p. 52; Tr. p. 60)
8. The applicant enters into a contract with the residents who reside at the Center. Under the section of the contract titled "Charges for Services," it states the basic rate is \$108.00, which is due on the first day of each month and shall be considered late if not received by the fifth day of each month.¹ Any payment not received by the fifth day of the month shall be subject to simple interest at the rate of 18% per annum. (App. Ex. G, p. 131)

¹ The \$108.00 rate, which is the amount on the sample contract provided by the applicant, is the daily rate (see App. Ex. H comparing daily rate with Medicaid reimbursements). On an annual basis the rate would be \$39,420, and monthly it would be \$3,285.

9. The basic rate compensates the applicant “for the provision of nursing care and services, personal care, laundry, room and board for the period of one calendar month.” (App. Ex. G, p. 131)
10. The contract includes a paragraph concerning additional costs and states, “A Resident shall also be liable for any treatment or service requested and accepted by the Resident if it is not a service designated within the description of the Basic Rate.” (App. Ex. G, p. 131)
11. The contract also includes the following paragraph under charges for services:

Unless subject to either governmental limitation or otherwise, a Resident shall be responsible for the payment of the Services and Products set forth on the attached Prices Schedule for Specified Supplemental Services and Products (attached hereto and incorporated by reference).² (App. Ex. G, p. 131)
12. The applicant does not require its residents to pay a security deposit. (App. Ex. G, p. 131)
13. Under the section of the contract titled “Private Pay Residents,” the following paragraph is included:

Exhaustion of Private Funds. If a private pay Resident exhausts funds available for the payment of care and thereafter seeks payment through public payment sources, this facility shall not discharge that Resident on that basis alone. (App. Ex. G, p. 132)
14. The section of the contract concerning its duration indicates it may be terminated if, *inter alia*, the resident is compelled to leave by a change in physical or mental health. (App. Ex. G, p. 134)
15. The contract states the resident may be transferred or discharged only for one or more of the following reasons:

² This attachment was not included in the record.

- For medical reasons;
- For the resident's physical safety;
- For the physical safety of other residents, facility staff, or facility visitors; or
- For either late payment or non-payment for the resident's stay, except as prohibited by law. (App. Ex. G, pp. 135-136)

16. The applicant's audited financial statement for the year ending December 31,

2006 shows the following as its Statement of Operations:

Unrestricted Revenues, Gains and Other Support	
Net patient service revenue	\$4,152,557
Other	<u>10,966</u>
	4,163,523
Expenses	
Salaries and wages	1,288,168
Employee benefits	289,199
Purchased services and professional fees	890,415
Supplies and other	728,155
Depreciation and amortization	126,800
Interest	307,085
Provision for uncollectible accounts	<u>49,622</u>
	3,679,444
Operating Income	484,079
Interest Income	<u>9,673</u>
Excess of Revenues over Expenses	\$493,752
(App. Ex. I, p. 148)	

17. The directors and officers of the corporation are not compensated for their services. (App. Ex. C; Tr. p. 19)

18. Approximately 77% of net patient service revenues were from participation in the Medicare and Medicaid programs for the year ending December 31, 2006. (App. Ex. I, p. 152)

19. At December 31, 2006 and 2005, the applicant was in violation of certain financial covenants in the mortgage loan agreements with the Village, and the

applicant had not made principal payments as required. The owners of the revenue bonds have the right to accelerate the maturity of the mortgage loans. In total, the applicant was delinquent on \$430,000 of principal payments as of December 31, 2006. The applicant made an interest payment of \$292,631 for the year ending December 31, 2006. (App. Ex. I, p. 154)

20. The applicant has a management agreement with St. Andrew's Management Service ("Manager") to manage and supervise the programs, operations and business affairs of the Center. "As part of its management responsibilities, the Manager supervises the Center's programs, personnel, financial statement preparation, billings, account collections, budgets, quality controls, public relations, repairs, materials management and general operations. The monthly management fee is computed as the greater of 5% of gross revenue, as defined, or \$12,000." Management fees for the year ending December 31, 2006 were \$207,622. (App. Ex. I, p. 155)

CONCLUSIONS OF LAW:

Article IX, section 6 of the Illinois Constitution of 1970 authorizes the General Assembly to grant property tax exemptions in limited circumstances and provides in part 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. Ill. Const. 1970, art. IX, §6.

Pursuant to this constitutional authority, the General Assembly enacted section 15-65 of the Property Tax Code, which allows exemptions for charitable purposes and provides in part as follows:

All property of the following is exempt when actually and exclusively used for charitable or beneficent purposes, and not leased or otherwise used with a view to profit:

(a) Institutions of public charity....

(c) Old people's homes, facilities for persons with a developmental disability, and not-for-profit organizations providing services or facilities related to the goals of educational, social and physical development, if, upon making application for the exemption, the applicant provides affirmative evidence that the home or facility or organization is an exempt organization under paragraph (3) of Section 501(c) of the Internal Revenue Code or its successor, and either: (i) the bylaws of the home or facility or not-for-profit organization provide for a waiver or reduction, based on an individual's ability to pay, of any entrance fee, assignment of assets, or fee for services, or (ii) the home or facility is qualified, built or financed under Section 202 of the National Housing Act of 1959, as amended.

An applicant that has been granted an exemption under this subsection on the basis that its bylaws provide for a waiver or reduction, based on an individual's ability to pay, of any entrance fee, assignment of assets, or fee for services may be periodically reviewed by the Department to determine if the waiver or reduction was a past policy or is a current policy. The Department may revoke the exemption if it finds that the policy for waiver or reduction is no longer current....35 ILCS 200/15-65(a), (c).

Property may be exempt under subsection (a) if it is (1) owned by an entity that is an institution of public charity, and (2) actually and exclusively used for charitable purposes.

Id.; Chicago Patrolmen's Association v. Department of Revenue, 171 Ill. 2d 263, 270 (1996); Methodist Old People's Home v. Korzen, 39 Ill. 2d 149, 156-157 (1968).

Whether property is actually and exclusively used for charitable purposes depends on the primary use of the property. Methodist Old Peoples Home, at 156-57. If the primary use

of the property is charitable, then the property is “exclusively used” for charitable purposes. Cook County Masonic Temple Association v. Department of Revenue, 104 Ill. App. 3d 658, 661 (1st Dist. 1982).

In Methodist Old Peoples Home, *supra*, Supreme Court provided guidelines for determining whether property meets the constitutional standards for a charitable purposes exemption. The guidelines are as follows: (1) whether the benefits derived are for an indefinite number of people, persuading them to an educational or religious conviction, for their general welfare or in some way reducing the burdens of government; (2) whether the organization has no capital, capital stock or shareholders, and earns no profits or dividends, but rather derives its funds mainly from public and private charity and holds them in trust for the objects and purposes expressed in its charter; (3) whether the organization dispenses charity to all who need and apply for it, does not provide gain or profit in a private sense to any person connected with it, and 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; and (4) whether the primary purpose for which the property is used, not any secondary or incidental purpose, is charitable. Methodist Old Peoples Home, at 156-57. In Eden Retirement Center, Inc. v. Department of Revenue, 213 Ill. 2d 273 (2004), the Supreme Court indicated that these guidelines must be considered in addition to determining whether the applicant meets the requirements under subsection (c) of section 15-65. *Id.* at 290-291. The guidelines are to be balanced with an overall focus on whether and how the organization and use of the property serve the public interest and lessen the State’s burden. See DuPage County Board of Review v.

Joint Commission on Accreditation of Healthcare Organizations, 274 Ill. App. 3d 461, 468-469 (2nd Dist. 1995).

It is well-established that property tax exemption provisions are strictly construed in favor of taxation. People ex rel. County Collector v. Hopedale Medical Foundation, 46 Ill. 2d 450, 462 (1970). The party claiming the exemption has the burden of proving by clear and convincing evidence that it is entitled to the exemption, and all doubts are resolved in favor of taxation. *Id.*; City of Chicago v. Department of Revenue, 147 Ill. 2d 484, 491 (1992); Evangelical Hospitals Corporation v. Department of Revenue, 223 Ill. App. 3d 225, 231 (2nd Dist. 1992).

The applicant believes that charity is any effort to better the condition of society, and the applicant does this without respect to income or ability to pay. The applicant notes that the opening of the Center was delayed, bond payments were missed, the initial census was low, the Center was initially mismanaged, and it is now facing bankruptcy.³ The applicant contends that although it temporarily may not have the financial ability to reduce a resident's bill or waive fees, all funds are being used for the overall purpose of keeping the Center open. The applicant asserts that the community is almost entirely people with low to moderate income, and the Center is open to every person, no matter what income or assets they have. The applicant contends that it gives the same care to Medicare and Medicaid residents as it does to private pay residents. The applicant refers to the dissent in Fairview Haven v. Department of Revenue, 153 Ill. App. 3d 763, 775 (4th Dist. 1987) (Lund, J., dissenting) where Justice Lund argues that providing a home for the elderly is charitable. The applicant believes it is not a commercial enterprise, and its

³ The audit report states the financial statements were prepared assuming the Center will continue as a going concern, but because the Center is in default on its mortgage loan, this raises substantial doubt about its ability to continue as a going concern. (App. Ex. I)

efforts are not motivated by profits. The Department, on the other hand, contends the Center is a commercial enterprise, and its primary purpose is to serve paying customers.

The applicant does provide a valuable service to the community, but it did not present sufficient evidence to show clearly and convincingly that it is a charitable organization that uses the property for charitable purposes under the guidelines of Methodist Old Peoples Home, *supra*.⁴ The evidence does not show the applicant provides charity to an indefinite number of people or that charity is given to all who need and apply for it. For the year in question, the applicant did not give specific instances or documentation showing it waived fees for residents who were unable to pay them. The testimony referred to one resident whose payments were delayed until the family was able to sell some assets (Tr. pp. 134-135), but no specific information or substantiation was given concerning residents who requested charity and received it. During 2006, the applicant's bylaws did not state it would waive fees if a resident is financially unable to pay them, and the applicant did not have a written benevolent plan that states it will waive fees for anyone based on financial need.⁵

The contract that was used during 2006 included a paragraph titled "Exhaustion of Private Funds" and states the applicant will not discharge a private pay resident on the basis that the resident has exhausted his or her funds and is seeking payment through government sources. This provision applies only to private pay residents and was the applicant's only specific policy regarding ability to pay. The testimony indicated that the

⁴ Having a charitable exemption from income taxes or from sales and use taxes is not determinative of whether the applicant is entitled to a charitable exemption from property taxes. See Hopedale Medical Foundation, at 464.

⁵ The testimony indicated that in September 2007 the bylaws were amended to include a written charity policy; a copy of the amendment was not provided because the amendment was not during the year in question. (Tr. p. 124)

time period between applying for and receiving government payments could be anywhere between 3 to 18 months, and when the resident becomes eligible to receive government payments, the payments may cover all, some, or none of the months during the gap. (Tr. pp. 140-141) The applicant did not provide evidence showing whether any of these fees were actually waived during 2006, and nothing indicates that fees are ever waived for purposes of admission. The charging of fees does not automatically disqualify an organization as charitable as long as it furnishes its facilities or services to those who are unable to pay. See Small v. Pangle, 60 Ill. 2d 510, 515-516 (1975). The applicant has failed to present evidence demonstrating that it provides care to those who are unable to pay for it.

The testimony and arguments suggest that because the applicant is behind on its bond payments and has been in financial straits, it has been unable to provide charity and will do so when it is financially able. The Manager's chief financial officer testified that the applicant's Board would like to have quarterly meetings whereby it reviews requests for charitable services, but at this point the Board cannot review charitable requests because the applicant does not have sufficient money to provide charity. (Tr. pp. 69-70) Notwithstanding the applicant's financial condition, providing free care only in relation to one's financial circumstances is not charity. See Wyndemere Retirement Community v. Department of Revenue, 274 Ill. App. 3d 455, 460 (2nd Dist. 1995). Although the applicant contends that any excess money is used for the overall purpose of keeping the Center open, the fact that money may be used to serve a charitable purpose does not automatically entitle the property to an exemption. See Salvation Army v. Department of

Revenue, 170 Ill. App. 3d 336, 344 (2nd Dist. 1988). The use to which the property is devoted is decisive, and the use must be charitable. *Id.*

The applicant indicated that it provides a substantial amount of non-financial charitable services. It sponsors activities for the community such as an Easter egg hunt in which several hundred children participate, a Thanksgiving luncheon, a New Year's Eve party, a July 4th barbecue, and a Halloween party. (App. Ex. H; Tr. pp. 106-119) The applicant contends the community would not have these benefits without the applicant's presence. Although the applicant's presence is certainly an asset to the community, the free activities that the applicant sponsors are not the primary activities of the organization. The primary activity of an organization must be charitable in order to receive the exemption. See North Shore Post No. 21 v. Korzen, 38 Ill. 2d 231 (1967); Rotary International v. Paschen, 14 Ill. 2d 480 (1958). The applicant's primary purpose is to provide skilled nursing care, and as indicated previously, the evidence does not include substantiation that charity care was given to those residents who needed it.

In addition, the applicant does not derive its funds mainly from public and private charity; the applicant derives its funds primarily from fees. The applicant suggests that the difference between the fee it receives from Medicaid and the fee it receives from private pay residents is charity. (See App. Ex. H) The court in Riverside Medical Center v. Department of Revenue, 342 Ill. App. 3d 603, 610 (3rd Dist. 2003), however, found that the discounted care that is provided through contracts with Medicare, Medicaid, and private insurers is not charity. Furthermore, the audit report indicates approximately 77% of the net patient service revenues during 2006 were from participation in the Medicare and Medicaid programs. If the government provides the majority of the applicant's

revenue, then the applicant is not lessening the government's burdens, which is another consideration under Methodist Old People's Home, *supra*.

Furthermore, the evidence supports a finding that the applicant is operated more like a business rather than a charity. The applicant's financial statements include an expense for uncollectible accounts (i.e., bad debt expense) of \$49,622, but the statements do not include an expense for charitable care. The Manager's operations director testified that because the applicant does not have a formal charity policy and has been in financial straits, the applicant has not been able to grant specific charitable relief; instead, the applicant simply has not collected money from residents who are unable to pay it. (Tr. pp. 120-121) Therefore, if a resident was unable to pay a fee during 2006, this was apparently written off as a bad debt expense. Under Illinois law, writing off a bad debt is not charity. See Alivio Medical Center v. Department of Revenue, 299 Ill. App. 3d 647, 652 (1st Dist. 1998). Although a person who is unfamiliar with property tax laws may not recognize a distinction between charity and bad debt, expecting to be paid in full for services and writing off fees only when they cannot be collected is more akin to operating a business rather than a charity. Charity is a gift (Methodist Old Peoples Home, at 156), and the applicant has not clearly established that it provides free services that are gifts rather than debt that could not be collected.

Other factors suggest the applicant is operated more like a business rather than a charity. According to the contract, payments received after the fifth day of each month are subject to simple interest at the rate of 18% per annum. Also, failure to pay fees may be a reason to discharge the resident. Although the applicant contends these provisions only apply to those who are able to pay, because the applicant does not have a formal

benevolent policy, these provisions may deter residents who cannot pay from applying. Nothing indicates the general public is aware of the possibility of free care. In addition, the monthly management fee is computed as the greater of 5% of gross revenue or \$12,000.⁶ Having the fee based on gross revenue suggests a business-like method of compensating the Manager.

As previously mentioned, exemption provisions are strictly construed, and all doubts must be resolved in favor of taxation. See Wyndemere, *supra*. The evidence raises doubt concerning the charitable nature of the organization and the use of the property because it includes the following: (1) the applicant did not actually provide charity or waive fees for anyone during 2006; (2) the applicant did not have a standard charitable policy in existence during 2006; (3) the majority of the applicant's revenue was from fees rather than donations; and (4) the applicant's operations are more analogous to a business rather than a charity. Therefore, the applicant has not met its burden of showing clearly and convincingly that it is a charitable organization that uses the property for charitable purposes.

Recommendation:

For the foregoing reasons, it is recommended that the applicant's request for a charitable exemption for the year 2006 be denied.

Linda Olivero
Administrative Law Judge

Enter: June 26, 2008

⁶ During 2006, the total fee was \$207,622, which on a monthly basis averaged approximately \$17,302.