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The Idaho Youth Ranch v. Ada County Board of Equalization Appellant's Reply Brief Dckt. 41256

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IN THE SUPREME COURT OF THE STATE OF IDAHO

THE IDAHO YOUTH RANCH,
INC., IDAHO YOUTH RANCH
NAGEL CENTER, LLC,

Petitioner-Appellant

vs.

ADA COUNTY BOARD OF
EQUALIZATION,

Respondent.

Supreme Court Case No. 41256

APPELLANT'S REPLY BRIEF

Appeal from the District Court of the Fourth Judicial District for Ada County
Honorable Melissa Moody, District Judge, presiding

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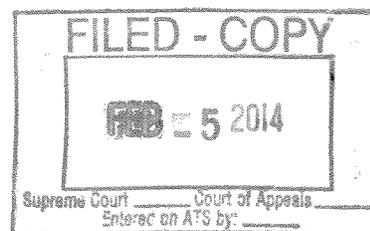


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ARGUMENT

The Idaho Youth Ranch does not dispute that the LLC is the record owner of the subject property or that the LLC is a separate legal entity. The parties disagree, however, as to whether an organization may be considered “charitable” if its charitable activity consists of supporting another charitable organization. The Youth Ranch and the LLC contends that the LLC’s support of the Youth Ranch - another charitable organization - is a valid charitable function.

A. Support of a charitable organization is a qualifying charitable activity

Charitable organizations whose only function is to support other charitable organizations have long been recognized in the law. Section 509(a)(3) of the Internal Revenue Code recognizes as charitable organizations those that function “exclusively for the benefit of” other charitable organizations. *See* 26 USC § 509(a)(3). Moreover, if benefiting another charitable organization does not qualify as a charitable activity, then virtually all foundations and other 509(a)(3) charitable support organizations would be disqualified.

Idaho Code § 63-602C also does not make this distinction. On the contrary, the statute extends the property tax exemption to a broad class of nonprofit organizations: “fraternal, benevolent, or charitable limited liability companies, corporations or societies.”

In the present case, the LLC supported the Idaho Youth Ranch by providing a building thereby also supporting the charitable activities of the Youth Ranch. The LLC quite literally put a roof over the head of the Youth Ranch, enabling the Youth Ranch to put a roof over the heads of children and to provide countless other services to Idaho families.

B. Not a Commercial Lease

An attempt has been made to characterize the relationship between the Youth Ranch and the LLC as a commercial lease arrangement, as might exist between any landlord and tenant. The record, however, demonstrates that this relationship was *not* a commercial lease. As explained on pages 9 – 10 of Appellant’s opening brief, the lease was not commercial because it was not entered into for profit; rent was set at an amount only sufficient to cover the mortgage payments; the rent was believed to be below market value; the lease was not an arm’s-length transaction, as specifically noted in the Bank’s lending documents; and the tenant was required to guarantee the landlord’s mortgage.

Moreover, Idaho Code § 63-602C makes a distinction between property “leased for commercial purposes” and property leased for exempt purposes. The subject property here was not leased to the Youth Ranch for commercial purposes but, instead, was leased to support the charitable activities of the Youth Ranch.

Further support for the position is found in *Boise Central v. Board of Ada County Commissioners*, 122 Idaho 67, 831 P.2d 535 (1992), cited in Appellant’s opening Brief. In *Boise Central*, the Supreme Court held that an exempt organization’s lease to its *own members* was *not* commercial, but was consistent with the organization’s purpose. *Id.* 122 Idaho at 72, 831 P.2d at 540.

It has been argued that *Boise Central*’s is inapplicable here, because that case involved a *fraternal* organization, instead of a charitable one. This distinction is not significant, however, because Idaho Code § 63-602C includes both fraternal organizations *and* charitable organizations as qualifying organizations. Moreover, like the fraternal organization in the *Boise*

Central case, the LLC in this case had the function of supporting its own – and only – member, the Youth Ranch. The lease was consistent with this function and therefore not commercial.

C. Factors under the *Sunny Ridge Manor* case.

As discussed by both parties, there are eight non-exclusive factors identified in *Canyon County v. Sunny Ridge Manor, Inc.*, 106 Idaho 98, 100, 675 P.2d 813 (1984).

(1) Purpose.

One of the factors in *Sunny Ridge* is “the stated purpose of its undertaking.” *Id.* In its brief, Respondent makes much of the fact that the operating agreement contains the standard “any lawful business” language, and that the type of business listed on the IRS Form SS-4 (the form used to apply for a tax ID number) was real estate. These are red herrings and should not be used to determine the “purpose of undertaking,” for several reasons.

First, the statements are not inconsistent with the charitable purposes, which are specifically stated elsewhere. When asked about the SS-4, Nancy Proctor, the Youth Ranch’s Chief Financial Officer, explained:

Ms. Proctor: If you look at No. 8a, you’d see that the type of entity is checked as “disregarded entity,” as “other.” So it was always considered to be a disregarded entity *and have the same mission as its single member*, which originally was the Foundation and subsequently was Idaho Youth Ranch, Inc.

Question [Mr. Hinton]: And I think you covered this in your original testimony: Were both of those charitable organizations?

A. [Ms. Proctor]: They are.

TR 58, LN 3 – 10 (emphasis added).

The mission of the LLC was the mission of the Youth Ranch, which may be found at several places. First, the Articles of Incorporation, which are set forth in the Supplemental Exhibit (Clerks Record, page 25), note that those purposes were “To provide troubled children and their families a bridge to a valued, responsible and productive future” and also “*to establish other organizations or corporations to assist in the advancement of the charitable purposes of the Idaho Youth Ranch.*” (Emphasis added.) The Idaho Youth Ranch Foundation was one such charitable organization. See TR 18 and Exhibit 2. The LLC was another.

By the time of the tax year at issue in this case, the Foundation had been merged back into the Youth Ranch so that the LLC was owned directly by the Youth Ranch.

IRS Form 990 (Exhibit 14) reported all the Activities of the overall Youth Ranch (including those of the LLC), where they are also stated to be “charitable.” See Exhibit 14, at page 1 and Schedule O.

Moreover, as detailed in the testimony of this case, the purpose of the LLC was to support the Youth Ranch by providing a building. (TR 21, LN 22-25; TR 61, LN 21 - 23).

The charitable purposes were also expressed in the Agreement with Nagel Beverage Company, which recognized that the property being transferred would be held for charitable purposes. (TR 26, LN 19 to TR 27, LN 16, and Exhibit 8, Addendum paragraph D.)

(2) **Charitable Functions**

The LLC’s charitable function of providing a building has been discussed above, and also in Appellant’s opening brief. See Appellant’s Opening Brief, pages 16 – 17.

(3) **Support by Donations.**

Respondent makes much of the fact that the \$350,000 donation from the ALSAM Foundation, as well as the matching grants from the public were actually received by the Youth Ranch and then subsequently used to improve the subject property owned by the LLC. However, the initial charitable contribution of property by Nagel Beverage in the amount of \$1.136 million was received *directly* by the LLC. This is not an insignificant charitable contribution, and it actually exceeds the amount received indirectly through the Youth Ranch.

(4) **Whether Recipients of Services are Required to Pay for the Services**

This factor was previously addressed in appellant's opening brief. See Appellant's Brief, at pages 17 -18.

It should be noted that the payments made by the Youth Ranch to the LLC were only sufficient to cover the mortgage payment. (TR, LN 21 to TR, LN 7), and that *Sunny Ridge* specifically recognized that an organization may still qualify for a tax exemption even if fees are charged to cover operating expenses. 106 Idaho at 101, 675 P.2d at 821.

Idaho Code § 63-602C also recognizes that lease payments may be made in non-commercial leases, and still qualify for the exemption.

(5) **General Public Benefit**

Although disputed by Respondent, the Youth Ranch contends that the LLC provided a general public benefit. Similar to other support-type charitable organizations, the LLC in this case provided public benefit by assisting the public charities with which it was associated. This "support" function is discussed at the beginning of this brief.

Respondent argues, however, that a general public benefit must be more “direct.” One case cited by Respondent is *Housing Southwest, Inc. v. Washington County*, 128 Idaho 335, 913 P.2d 68 (1996). There, the court stated:

The question of whether a corporation provides a general public benefit is closely connected to the questions of whether a corporation is supported by donations.

For a corporation’s uses to be considered charitable it is essential that they provide some sort of general public benefit. If the general public does not receive a direct benefit from a corporation’s donations, then the question presented by the “general public benefit” factor is whether the corporation fulfills a need which the government might otherwise be required to fill. While the requirement that a corporation lessen the burden of government is but one factor to be considered in determining tax exempt status, it is nevertheless an important one.

Id., 128 Idaho at 339, 913 P.2d at 72 (internal citations omitted).

Housing Southwest is distinguishable from the present case. As previously noted, the LLC did receive charitable contributions, both directly and indirectly. Moreover, by supporting the Youth Ranch, the LLC supported programs which lessened the burden of government, by facilitating adoptions, providing drug and alcohol treatment for children and families, and providing numerous other programs and services. It should also be noted that the Court in *Housing Southwest* did not use the term “direct” in the same sense urged by Respondent; *Housing Southwest* was not a case involving one charitable organization supporting another to provide a public benefit.

Respondent also cites *Owyhee Motorcycle Club, Inc. v. Ada County*, 123 Idaho 962, 855 P.2d 47 (1993). However, a fair reading of this case does not support Respondent’s contention that there was no public benefit in the present case. In *Owyhee Motorcycle*, the Supreme Court noted that the “general public benefit” factor dealt with “whether the organization fulfills a need which the government might otherwise be required to fill.” 123 Idaho at 965, 855 P.2d at 50. The Court went on to hold, “Recreational motorcycling is not the type of need that the

government is required to fulfill. Accordingly, [Owyhee Motorcycle Club] must show that it benefits the community at large rather than a select group of persons. While motorcycling does provide a recreational benefit, here the record indicates that [Owyhee Motorcycle Club]'s services primarily benefit club members rather than the community at large.”

The Owyhee Motorcycle Club is easily distinguished from the LLC in the present case. First, the activities that took place on the LLC's property were not “recreational” services, but were adoptions, counseling, drug and alcohol treatment and other administrative programs to help children and families. By providing a building facility to support the Youth Ranch, the community at large was benefited. Every child adopted, counseled for abuse, or who received drug and alcohol treatment, is a benefit to the community. Every family counseled because the LLC made the facility available, is a benefit to the community. The LLC supported the Youth Ranch in these activities, by providing the literal roof under which these activities took place. Many of these activities were provided pursuant to government programs.

Second, the membership of the LLC (the Youth Ranch) was a charitable organization, not merely individual motorcyclists. Therefore, the benefit conferred on the charitable organization in this case did not end with its membership, but extended to the larger community, served by the organization.

(6) **Lack of Profit**

The testimony at trial was that the revenue and expenses for the financial accounting for the LLC and “all intercompany profits of any kind are eliminated under Generally Accepted Accounting Principles.” (TR 29, LN 7-8.) Therefore, there were no profits realized by the LLC under Generally Accepted Accounting Principles. See also Exhibit 13 and TR 29, LN 9 – 23.

(7) **Where Assets Would Go on Liquidation**

The LLC Operating Agreement provided that assets would be distributed in accordance with “applicable law.” The applicable state law is Idaho Code § 30-6-708, which provides that the assets upon dissolution are returned to the members. Here, the member was the Youth Ranch, a charitable organization. The applicable federal law includes 26 USC §501(c)(3) which also restricts transfers to non-charitable organization which would result in a private enrichment. Most importantly, the assets of the LLC were actually transferred to the Youth Ranch.

(8) **Charity Based on Need.**

This factor has been previously briefed, above and in Appellant’s opening brief. See Appellant’s Brief, pages 19 – 20. In summary, the services of the Youth Ranch have been widely utilized since its inception in 1954. The Youth Ranch needed a building to help it provide those services to the children and family who relied upon them. The LLC fulfilled this need and thereby helped fulfilled the needs of the Idaho community at large.

CONCLUSION

It is respectfully urged that the Court apply the Sunny Ridge factors to conclude the subject property qualifies for a property tax under Idaho Code § 63-602C.

However, the *Sunny Ridge* opinion also noted that these factors were not exclusive. The case was decided prior to the amendment of Idaho Code § 63-602C which added “charitable limited liability companies.” It is likely the *Sunny Ridge* Court would recognize the support of

another charitable organization as a valid charitable function, in and of itself. Such a conclusion would also be consistent with this Court's opinion in the *Boise Central* case, where leasing building space to member organizations qualified for the exemption.

DATED THIS 5th day of February, 2014.



John B. Hinton,
Law Office of John B. Hinton
Attorney for the Appellant

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 5th day of February, 2014, I caused to be served a two (2) true copies of the foregoing APPELLANT'S REPLY BRIEF by the method indicated below, and addressed to the parties marked served below:

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