Shallow River Properties, Inc.

V.

Town of Northumberland

Docket No.: 17939-99EX

DECISION

The "Taxpayer," pursuant to RSA 72:34-a, appeals the Town's denial of a tax exemption for property located at 31 Brooklyn Street in the Village of Groveton (the "Property"). For the reasons stated below, the appeal is denied.

The Relevant Exemption Statute: RSA 72:23, V-a

At the hearing on December 13, 2000, the Taxpayer clarified, and the Town agreed, the exemption at issue is contained in RSA 72:23, V-a.[1] This section exempts from taxation:

> The real estate and personal property owned by any organization described in paragraphs I, II, III, IV or V of this section [RSA 72:23] and occupied and used by another organization described in said paragraphs, but only to the extent that such real estate would be exempt from taxation under said paragraphs if such property were owned by the organization occupying and using the property, as long as any rental fee and repairs, charged by the owner, are not in clear excess of fair rental value.

[1] Rather than RSA 72:23, IV, the "Educational" exemption provision cited on the appeal form filed with the board by the Taxpayer, apparently in error. The Taxpayer bases its specific claim for an exemption on RSA 72:23, V, referenced in RSA 72:23, V-a and discussed more fully infra.

To qualify for this specific exemption, at least three distinct requirements must be met:

(1) the Property must be owned by an organization that would qualify for an exemption if it occupied and used the Property itself;

(2) the Property must be occupied and used by another organization that also qualifies for an exemption; and

(3) the "rental fee and repairs" charged by the owner cannot be "in clear excess of fair rental value."

In this case, the evidence establishes that the Taxpayer[2] owns the Property and rents it, in its entirety, to an affiliated corporation, Northern New Hampshire Mental Health and Development Services ("NNHMHDS"). The Taxpayer is organized as a "voluntary" (nonprofit) New Hampshire corporation under RSA 292, is registered as a charitable trust, has the same board of directors as NNHMHDS, and manages property transferred to it previously by that organization. See Taxpayer Exhibits 2, 5, 6 and 9 (especially Note 1 thereto).

For purposes of this appeal, the parties have stipulated the second necessary element of this exemption statute is satisfied (i.e., that NNHMHDS would qualify for a charitable exemption if it owned the Property itself, rather than renting it from the Taxpayer), but disagree as to the first and third elements. The Town filed a Motion to Dismiss at the hearing, based on the first element (i.e., the Taxpayer "provides no [charitable] services and lacks a charitable purpose"), and evidence was also adduced at the hearing regarding the third element (fair rental value).

[2] Shallow River Properties, Inc., sometimes referred to in the exhibits as "SRP."

The board agrees with the Town that the Taxpayer has failed to sustain its burden of proof[3] on these separate elements involving charitable status and fair rental value. The board is mindful of the differing motives of municipalities responsible for raising sufficient tax revenues to fund public services and organizations seeking charitable tax exemptions. See Steven G. Brown, New Hampshire's Tax Exemption Statute: Religious, Educational and Charitable Organizations, 29 New Hampshire Bar Journal 161 (1988).[4] The board must also take into account how the choice of form of ownership or operation can impact an organization's qualification for a tax exemption. Here, an affiliated entity (NNHMHDS) occupies and uses the Property and may have qualified for a tax exemption if it owned the Property rather than leasing it from the Taxpayer. The parties chose, however, for reasons of their own, to transfer ownership to the Taxpayer in 1989 (see Taxpayer Exhibit 6) and enter into a lease-back arrangement. The board must decide how this distinction in the form of ownership and operation affects qualification for a specific tax exemption. In deciding this question, the board must apply

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[3] See RSA 72:23-m: "The exemptions afforded by RSA . . . 72:23-k, as well as exemptions granted by other provisions of law, shall be construed to confer exemptions only upon property which meets requirements of the statute under which the exemption is claimed. The burden of demonstrating the applicability of any exemption shall be upon the claimant."

[4] "For the most part, the self-interest and objectives of New Hampshire municipalities with

the relevant statutes and the common law of the State of New Hampshire.

Charitable Purpose

The Taxpayer asserts it would meet the requirements for a "charitable" exemption under RSA 72:23, V if it used and occupied the Property itself. For purposes of the exemption statutes, see RSA 72:23, VII, "charitable" is defined as follows:

> **72:23-l Definition of "Charitable."** The term "charitable" as used to describe a corporation, society or other organization within the scope of this chapter, including RSA 72:23 and 72:23-k, shall mean a corporation, society or organization established, and administered for the purpose of performing, and obligated by its charter or otherwise, to perform some service of public good or welfare advancing the spiritual, physical, intellectual, social or economic well-being of the general public or a substantial and indefinite segment of the general public that includes residents of the state of New Hampshire, with no pecuniary profit or benefit to its officers or members, or any restrictions which confine its benefits or services to such officers or members, or those of any related organization. *The fact that an organization's activities are not conducted for profit shall not in itself be sufficient to render the organization "charitable" for purposes of this chapter, nor shall the organization's treatment under the United States Internal Revenue Code of 1986, as amended.* This section is not intended to abrogate the meaning of "charitable" under the common law of New Hampshire. [Italics added]

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respect to taxation are diametrically opposed to those of . . . charitable organizations."

The Taxpayer's witnesses testified it was organized as a '501(c)(2)' corporation under federal tax law (exempt from federal income taxation as a corporation holding title to property and paying income to another tax exempt organization, NNHMHDS, a 501(c)(3) organization), see Taxpayer Exhibits 4 and 8-A, B and C. In New Hampshire, however, neither status as a "voluntary" (nonprofit) corporation nor federal tax exemption are sufficient, in and of themselves, to qualify an organization for a state or local property tax exemption, as the next-to-last sentence of RSA 72:23-l makes clear.[5]

The Town argues the Taxpayer fails to meet one "key test" under this statutory definition: whether the Taxpayer is "obligated by its charter or otherwise, to perform some service of public good or welfare advancing the spiritual, physical, intellectual, social or economic well-being of the general public or a substantial and indefinite segment of the general public." The Taxpayer's current charter is contained in its "Amended Articles of Agreement" dated June 19, 1989, and submitted as Taxpayer Exhibit 2. Article II of this document provides as follows:

> The purposes for which this corporation is established are as follows:
>
> A. To receive [sic] purchase, lease, hold and maintain real property associated with the provision of residential, treatment and administrative services to individuals in Coos, Carroll and Upper Grafton Counties.

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[5] See also Nature Conservancy v. Nelson, 107 N.H. 316, 319 (1966)("The fact that plaintiff's activities are not conducted for profit is not sufficient to qualify it for exemption . . .") and cases cited therein.

B. To manage, sell or otherwise dispose of real property.

The corporation's by-laws, as well as its articles of incorporation, can reflect its stated purpose. See The Housing Partnership v. Town of Rollinsford, 141 N.H. 239, 241 (1996). In this case, the by-laws, Taxpayer's Exhibit 3, replicate and add to the purposes stated in the articles, as follows:

> ARTICLE II - PURPOSES
> - to receive, purchase, lease, hold and maintain real property associated with the provision of residential, treatment and administrative services to individuals in Coos, Carroll and Upper Grafton Counties.
> - to manage, sell or otherwise dispose of real property.
> - to assist NNHMH&DS and affiliate corporations in carrying out their missions.

The Taxpayer is obligated, both by its articles of agreement (in Article III) and its by-laws (in Article XII), to distribute, upon dissolution, any of its remaining assets to NNHMHDS.

The board finds these cited provisions are insufficient to establish a charitable purpose because the Taxpayer is under no obligation during its ongoing existence (at least at any time before its dissolution) to carry out any substantial charitable purpose or objective. Even a for-profit institution, such as a realty management firm, for example, could hold property with similarly stated purposes.

While the Taxpayer was organized and exists primarily, if not exclusively, to serve an affiliated organization (NNHMHDS),[6] the Taxpayer cannot 'bootstrap' or 'piggy-back'[7] the

[6] Evidence presented at the hearing indicates the Taxpayer has no employees of its own, pays a management fee to NNHMHDS, and operates "for the purpose of owning, maintaining, managing, selling, and leasing real property associated with the provision of residential, treatment and administrative services for the clients and staff of [NNHMHDS]." Exhibit 9 (Note 1).

charitable purpose of this other entity, rather than having a direct charitable purpose of its own. In addition, "to qualify as a charitable institution, an obligation must exist to perform the obligation's stated purpose to the public, rather than simply to the members of the organization." Appeal of City of Franklin, 137 N.H. 622, 625 (1993), citing Society of Cincinnati v. Exeter, 92 N.H. 348, 352 (1943).

Recent case law further confirms that, in order to qualify for an exemption, the charitable purpose must be 'direct' and not simply "an adjunct to a charitable purpose." See Housing Partnership, supra. In that case, a nonprofit, federally tax exempt corporation claimed an RSA 72:23, V, property tax exemption on the basis that it provided affordable housing "to low and moderate income persons." The supreme court reversed the trial court's granting of a tax exemption because the evidence showed the rents were "close to market rates" and did not vary "depending on the income level of the tenant." Id. at 244. As the court concluded:

> The plaintiff has failed to demonstrate that the rental of the units is not simply an adjunct to its charitable purpose. . . . In other words, the plaintiff in this case has failed to demonstrate that the tenants' occupancy . . . is in any significant way different from tenants occupying housing run by a noncharitable organization.

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[7] The Taxpayer advanced a so-called "mirror" theory, based on the charitable purpose of its affiliate (NNHMHDS).

The board has a similar difficulty in concluding the Taxpayer's leasing activity at above market rental rates (an issue discussed more fully in the next section, "Fair Rental Value") reflects a direct charitable purpose or differs in any material respect from leasing activity by a noncharitable organization. In sum, the evidence supports the Town's position that the Taxpayer performs its "real estate management activities" as a "convenience" for NNHMHDS, and that this is not a charitable purpose cognizable under RSA 72:23,V.[8]

Fair Rental Value

Somewhat related on the facts is the third element of RSA 72:23, V – the requirement that "any rental fee and repairs" not be "in clear excess of fair rental value." To resolve this issue, the terms of the leasing arrangements between the Taxpayer and NNHMHDS should be examined more closely.

[8] The board has reviewed the Affidavit of Paul G. Gorman (Taxpayer Exhibit 17). Mr. Gorman is the Director of the Division of Behavioral Health for the New Hampshire Department of Health and Human Services. While the Taxpayer, an affiliate of NNHMHDS, may be bound by its contract with the state, and the state may be "well aware" of the relationship between these entities, these facts are insufficient to establish a legally sufficient charitable purpose for the Taxpayer.

According to the evidence, the property consists of 2,400 square feet of space and has been rented annually for a "minimum base rent" of $26,400 ($11 per square foot). See Exhibits 7A, B and C, the annual "Lease" agreements between the Taxpayer and NNHMHDS. The testimony indicated this rent has remained constant despite considerable fluctuations in the real estate market over the past ten years. Under the terms of each "Lease," the Taxpayer is responsible for utilities; when these expenses ($6,615) are deducted from the annual rent ($26,400), $19,785 is still left for debt service and a return on capital. Gerald Albert, Taxpayer's Chief Financial Officer, testified that amortized payments on an assumed 30-year mortgage for 80% of the Property's stated value (land: $8,500; buildings: $121,881) would be approximately $9,600. Deducting this debt service from the annual rent and expenses indicates an annual return of almost 40% on equity capital,[9] far in excess of what a market investor may require.

Mr. Albert also testified that NNHMHDS was now leasing property from an unrelated entity (in Berlin, N.H.) for approximately $6.00 to $6.50 per square foot on a "net" lease. This would equate to no more than about $8 per square foot on a "gross" lease basis, well under the $11 per square foot paid on the Property. This furnishes additional evidence that the rent

[9] Equity investment = 20% of $130,381, or $26,076; $19,785 net rent - $9,600 debt service = $10,185 annual income; annualized return on equity capital = $10,185 ÷ $26,076 = 39.05%. Note also that the lessee, not the Taxpayer, is responsible for maintenance expenses. See Taxpayer Exhibits 7A., B. and C.

charged by the Taxpayer is "in clear excess of fair rental value."

Summary and Conclusion

In summary, the board finds the Taxpayer failed to sustain its burden of proving it is entitled to an RSA 72:23, V-a exemption because of two independent elements: lack of charitable purpose and rents charged "in clear excess of fair market value." While it may be true that NNHMHDS might have qualified for an exemption if it owned the Property, and the Taxpayer and NNHMHDS are affiliated entities both exempt under federal income tax law, the ownership and transactional forms chosen by these entities matters significantly for purposes of state tax exemption. The appeal of the Taxpayer is therefore denied.

Rehearing Motion

A motion for rehearing, reconsideration or clarification (collectively "rehearing motion") of this decision must be filed within thirty (30) days of the clerk's date below, not the date this decision is received. RSA 541:3; TAX 201.37. The rehearing motion must state with specificity all of the reasons supporting the request. RSA 541:4; TAX 201.37(b). A rehearing motion is granted only if the moving party establishes: 1) the decision needs clarification; or 2) based on the evidence and arguments submitted to the board, the board's decision was erroneous in fact or in law. Thus, new evidence and new arguments are only allowed in very limited circumstances as stated in board rule TAX 201.37(e). Filing a rehearing motion is a prerequisite for appealing to the supreme court, and the grounds on appeal are limited to those stated in the rehearing motion. RSA 541:6. Generally, if the board denies the rehearing motion, an appeal to the supreme court must be filed within thirty (30) days of the date on the board's denial.

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Douglas S. Ricard, Member

Albert F. Shamash, Esq., Member

CERTIFICATION

I hereby certify that a copy of the foregoing decision has this date been mailed, postage prepaid, to Randall F. Cooper, Esq., counsel for the Taxpayer; Timothy Bates, Esq., counsel for the Town; and Chairman, Selectmen of Northumberland.

Date: February 5, 2001

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Lynn M. Wheeler, Clerk

Shallow River Properties, Inc.

V.

Town of Northumberland

Docket No.: 17939-99EX

ORDER

The board has reviewed the "Taxpayer's Motion for Rehearing" (the "Motion") and the Town's "Objection to Motion For Rehearing." The Motion, directed at the board's February 5, 2001 Decision denying the Taxpayer's appeal, is denied.

RSA 541:3 and TAX 201.37(d) state the applicable standards for a rehearing motion. The Taxpayer has the burden of establishing "good reason": specifically, "a showing shall be required that the [b]oard overlooked or misapprehended the facts or the law and such error affected the [b]oard's decision." No such showing has been made and no other basis exists for granting the Motion.

The Motion's emphasis on the Taxpayer's qualification for a charitable exemption under federal tax law (i.e., "§501(c)2 of the Internal Revenue Code") is misplaced. As specifically noted in the Decision (at p. 4), RSA 72:23-l expressly negates the relevance of

"an organization's treatment under [the federal statute]" in determining whether the organization is "charitable" under New Hampshire law.

The Taxpayer argues elsewhere in the Motion that the phrase "or otherwise" in RSA 72:23-l should be read expansively to include the Taxpayer's supposed "obligations . . . to the State of New Hampshire." Motion, ¶ 10. Here, however, the Taxpayer failed to present sufficient facts at the evidentiary hearing to establish this alternative test as the basis for exemption under New Hampshire law.

For similar reasons, the board cannot accept the Taxpayer's rationale, made for the first time in the Motion, that its management's "computation of rent . . . averaged all the properties involved irrespective of the communities, [sic] and the special purpose and the uniqueness of the building improvements." Motion at ¶ 11. Whether or not this is true, the Taxpayer simply failed to present any evidence that the constant rent charged for the Property ($11 per square foot per year as set forth in annual leases over the past decade) was not "in clear excess of fair rental value." See RSA 72:23, V-a; and Decision at pp. 7 - 8. Nor, for that matter, did the Taxpayer show any "special purpose" or "uniqueness" in the Property that would justify such a high rental rate, invariant to market conditions.

Finally, the board finds no basis for the allegation that it "misinterpreted" New Hampshire case law. Motion, ¶ 9. Cf. The Housing Partnership v. Town of Rollinsford, 141 N.H. 239 (1996); and Decision at pp. 5-7. As in Rollinsford, supra at 244, where the supreme court affirmed the denial of a property tax exemption to a corporation qualified as a "§ 501(c)(3) corporation," the Taxpayer "in this case has failed to demonstrate that the tenants' occupancy . . .

is in any significant way different from tenants occupying [realty] run by a noncharitable organization."

Pursuant to RSA 541:6, any appeal of this order by the Taxpayer to the supreme court must be filed within thirty (30) days of the date on this order.

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Douglas S. Ricard, Member

Albert F. Shamash, Esq., Member

CERTIFICATION

I hereby certify that a copy of the foregoing decision has this date been mailed, postage prepaid, to Randall F. Cooper, Esq., counsel for the Taxpayer; Timothy Bates, Esq., counsel for the Town; and Chairman, Selectmen of Northumberland.

Date: March 20, 2001

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Lynn M. Wheeler, Clerk

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