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Kentucky Supreme Court Rules Industrial Development Corporation not Exempt from Property Tax

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In *Connie Hancock, Floyd County Property Valuation Admin v. Prestonsburg Industrial Corporation, et al.*, Case No. 2010-SC-000376-DG (4/26/2012), the Kentucky Supreme Court reversed a Court of Appeals decision and held that a local industrial development corporation did not qualify for a property tax exemption as a charitable institution.

Prestonsburg Industrial Corporation (“PIC”) was founded in 1968 by a group local businessmen as a private nonprofit corporation to attract business and industry to Prestonsburg for economic development purposes. PIC would buy property, make improvements, and then sell the property to various businesses, all for the betterment of the community through growth and industry. Any profits derived from those sales were rolled back into PIC for additional purchases and improvements. PIC was not organized as a statutory industrial development authority but instead, as a private nonprofit corporation.

The Internal Revenue Service had previously determined that PIC qualified for a federal income tax exemption under Section 501(c)(4) of the Internal Revenue Code. According to the dissenting opinion (J. Scott), no one had ever questioned PIC’s status as a purely public charity from its formation in 1968 until 2001 – some thirty-three years.

The Floyd County Property Valuation Administrator (the “PVA”) in 2001 sought to list certain property purchased by PIC from the City of Prestonsburg as taxable property on the county tax rolls. To confirm its exemption, PIC filed an application with the Kentucky Revenue Cabinet (the predecessor to the current Kentucky Department of Revenue)(“Revenue”) seeking a determination that the property was exempt under Section 170 of the Kentucky Constitution. Ky. Const. § 170 exempts from taxation “public property used for public purposes” and “institutions of purely public charity.” Revenue denied the application, and PIC appealed that denial to the Kentucky Board of Tax Appeals.

The Board affirmed Revenue’s determination on the basis that PIC was not a governmental body or agency and therefore the property did not qualify for the exemption for public property used for public purposes in Ky. Const. § 170. *See Prestonsburg Industrial Corporation v. Floyd County Property Valuation Admin.*, KBTA Order in File No. K04-S-38 (6/24/05). The Board did not address whether PIC qualified as an institution of purely public charity.

On appeal, the Floyd Circuit Court reversed the Board, finding the property exempt because PIC was both a charitable institution and PIC's property was public property used for public purposes. On further appeal, the Kentucky Court of Appeals found that because PIC was a private corporation, the property was not public property. However, the Court affirmed the circuit court's finding that PIC was a charitable institution because PIC's "activities ... reasonably better the condition of mankind." The Kentucky Supreme Court granted the PVA discretionary review of the Court of Appeals decision solely to determine whether PIC qualified as a public charitable organization.

The Kentucky Supreme Court began its analysis by noting that provisions granting tax exemptions are strictly construed. Turning to the language in Ky. Const. § 170, the Court explained that to be "purely" charitable, an organization must be "wholly altruistic in the end to be attained, and that no private or selfish interest should be fostered under the guise of charity." Op. at 4. The court identified the appropriate test to be twofold: "First, the institution must itself be a charity and the income from its property must be used to further its charitable purpose; secondly, the property must be employed purely for a charitable purpose." *Id.*

The Court noted that a design to achieve goals beneficial to the community is common to all charitable purposes, but that it did not follow that all such designs constitute a "purely public charity" for purposes of Ky. Const. § 170. When the organization's principal activities center around promoting the interests and gratifying the wishes of its own membership and the charitable outcome is merely incidental, the organization does not qualify as a "purely public charity." *Id.* at 5.

PIC argued that it was a purely public charity because of the expected indirect effects on the local economy and tax base in the form of job creation and commercial development. The Court rejected this argument, noting that while elimination of unemployment is a "public purpose" that does not equate to "charitable use" or "charitable purpose" and that two Kentucky Attorney General opinions had concluded such industrial organizations would not qualify for property tax exemptions.

The Court found that PIC's activities primarily serve and benefit the buyers or customers of PIC. The Court found significance in the lack of any evidence that PIC's customers were persons or organizations in need of charity or public assistance and the failure of PIC to claim that it actually created jobs directly, as opposed to only incidentally by bringing new businesses to the community which may potentially create jobs. The Court also noted that members of PIC consisted of local businesses whose own interests would be served by an increase in commercial and economic development.

The Court concluded that PIC had not established its activities were "wholly altruistic in the end to be attained ... [so] that no private or selfish interest should be fostered under the guise of charity." *Id.* at 8. The Court reasoned that "commercial and economic development are the promotion of business interests and not, therefore, indicative of actions of a purely public charity." *Id.*

J. Scott, whose judicial district includes the City of Prestonsburg and Floyd County, dissented.

The impact of this decision is unclear. Most local industrial development authorities in Kentucky are organized pursuant to the Local Industrial Development Authority Act (KRS 154.50-301 to 154.50-346). These authorities constitute governmental agencies and property owned by such authorities is specifically exempted from property taxation by statute. *See* KRS 154.50-343 (“All property acquired ... shall be exempt from taxation to the same extent as other property used for public purposes.”)