

Responses to legal questions

Property Tax Exemption Study
Committee

September 13, 2013

Topics to cover

- Constitutional parameters for taxing pious organizations
- Federal tax exempt status definitions
- Subsequent limits on public pious and charitable exemption

Constitutional limits on taxing pious property

First Amendment of Federal Constitution includes the Establishment and Free Exercise Clause

“Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof . . .”

Two separate components

- (1) State cannot endorse a state religion
- (2) State cannot interfere with religious practices

Difficult area for courts to draw lines

- “The Establishment and Free Exercise Clauses of the First Amendment are not the most precisely drawn portions of the Constitution.”
 - Walz v. Tax Comm. of NY City, 397 U.S. 664, 668 (1970)
- “The Court has struggled to find a neutral course between the two Religion Clauses, both of which are cast in absolute terms, and either of which, if expanded to a logical extreme, would tend to clash with the other.”
 - Walz v. Tax Comm. of NY City, 397 U.S. 664, 668-9 (1970)

Bottom line

States may exempt religious organizations from taxes, but they are not required to do so.

Establishment Clause

- States may exempt religious property without violating the Establishment Clause, but must do so broadly.
- Primary case from US Supreme Court is Walz v. Tax Comm. of NY City.

Walz v. Tax Comm. of NY City

Challenge was brought against NY's property tax exemption for religious properties on the basis that it impermissibly favored religion.

NY statute exempted:

“Real property owned by a corporation or association organized exclusively for the moral or mental improvement of men and women, or for religious, bible, tract, charitable, benevolent, missionary, hospital, infirmary, educational, public playground, scientific, literary, bar association, medical society, library, patriotic, historical or cemetery purposes . . . and used exclusively for carrying out thereupon one or more of such purposes . . .”

Walz v. Tax Comm. of NY City

US Supreme Court upheld the exemption reasoning the exemption did not single out a particular religion :

NY has “not singled out one particular church or religious group or even churches as such; rather, it has granted exemption to all houses of religious worship within a broad class of property owned by nonprofit, quasi-public corporations which include hospitals, libraries, playgrounds, scientific, professional, historical, and patriotic groups. The State has an affirmative policy that considers these groups as beneficial and stabilizing influences in community life and finds this classification useful, desirable, and in the public interest.”

Walz v. Tax Comm. of NY City

US Supreme Court also reasoned that the exemption did not lead to an excessive entanglement of state and church, nor did it amount to direct sponsorship of religious groups:

“The grant of a tax exemption is not sponsorship since the government does not transfer part of its revenue to churches but simply abstains from demanding that the church support the state. No one has ever suggested that tax exemption has converted libraries, art galleries, or hospitals into arms of the state or put employees ‘on the public payroll.’” Id., at 675.

Walz v. Tax Comm. of NY City

US Supreme Court also found significant that since the founding of our country, no state nor the federal government taxed all church property or income:

“Few concepts are more deeply embedded in the fabric of our national life, beginning with pre-Revolutionary colonial times, than for the government to exercise at the very least this kind of benevolent neutrality toward churches and religious exercise generally so long as none was favored over others and none suffered interference.” Id., at 666-67

Establishment Clause summary

- States may exempt religious property but must do so broadly.
- Contrast Walz with Texas Monthly v. Bullock, 489 U.S. 1 (1989).

Free Exercise Clause

- States are not required to exempt pious property.
- While all 50 states and the federal government exempt religious organizations and religious property from taxation in some form, the scope of those exemption vary.
- However, religious organizations and their employees do pay certain taxes, particularly income, employment, and sales taxes.

Jimmy Swaggart Ministries v. BOE of California,
493 U.S. 378 (1990)

- Jimmy Swaggart Ministries was a 501(c)(3) that sold religious items to church members and the public as part of its religious events held in California. The State claimed its generally applicable sales tax applied to these sales. JSM contested the tax, claiming that the Free Exercise Clause required an exemption.
- The Court noted “Our cases have established that ‘[t]he free exercise inquiry asks whether government has placed a **substantial burden** on the observation of a central religious belief or practice and, if so, whether a compelling governmental interest justifies the burden.’” Id. At 384-85.

Jimmy Swaggart Ministries v. BOE of California, 493
U.S. 378 (1990)

The Court found that the burden of paying generally applicable taxes was **not substantial**.

“There is no evidence in this case that collection and payment of the tax violates appellant's sincere religious beliefs. California's nondiscriminatory Sales and Use Tax Law requires only that appellant [JSM] collect the tax from its California purchasers and remit the tax money to the State. The only burden on appellant is the claimed reduction in income resulting from the presumably lower demand for appellant's wares (caused by the marginally higher price) and from the costs associated with administering the tax. . . . **[T]o the extent that imposition of a generally applicable tax merely decreases the amount of money appellant has to spend on its religious activities, any such burden is not constitutionally significant.**” Id. at 391.

Summary of constitutional limits on pious property

- States can exempt religious property, but are not required to do so.
- All 50 states provide some type of property tax exemption for religious properties, but vary on the scope of property exempted.
- Any exemption or tax should be broadly structured to avoid singling out religion, religious beliefs, or religious practices.

Federal tax exempt organizations

Under Section 501(c) of the Internal Revenue Code, certain types of organizations are exempt from income taxes.

Under Section 170 of the Internal Revenue Code, donations to certain types of 501(c) organizations are deductible from the donor's income.

Obtaining federal tax exempt status is most desirable for organizations soliciting donations, or seeking grants that require 501(c) status.

Types of 501(c) organizations

501(c)(3) is most common form:

- Any corporation, community chest, fund, or foundation
- Organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition, or for the prevention of cruelty to children or animals
- No part of the net earnings of which inures to the benefit of any private shareholder or individual
- No substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in, any political campaign on behalf of (or in opposition to) any candidate for public office.

Filing requirements

1. Organization must apply for status and process typically takes 3 to 11 months
2. Most organizations must pay an application fee
3. Annual filing requirements that include certain types of financial disclosures that are open to public inspection, and monetary penalties for failing to file

State requirements for non-profit corporations

- Must be organized under state law to further a particular purpose – not connected to federal tax exempt status
- No shareholders or distribution of profits
- Two types
 - Public benefit corporation – charity that benefits others
 - Example = public library
 - Mutual benefit corporation – non-profit that benefits specific group
 - Example = private golf club
- Biennial report required – less extensive than federal filing requirements and not subject to public disclosure

State non-profits filing requirements

- Must incorporate under state law and file with the Secretary of State
- Biennial reports required after that – much less extensive than federal 501(c) reports
- No financial disclosures required

Limitation on public, pious and charitable property exemption

- 32 VSA 3802(4) provides an initial exemption from education and municipal taxes for public, pious and charitable properties.
- Vermont courts have held that if there is a subsequent statute that is more specific, the subsequent statute will control.

32 VSA 3832 – Clarifying the scope of public, pious and charitable (effective 1959)

- Public, pious and charitable exemption DOES NOT include:
 - (1) Property held in trust for a municipality outside the boundaries of the municipality
 - (2) Property held by a religious society, other than a parsonage, outbuildings related to the parsonage or church edifice, a building used as a convent, school, orphanage, home or hospital, parking lot not used to produce income, lawn, playground, garden, any building associated with property named in this subsection, and so-called glebe lands.
 - (3) Property of railroad corporations
 - (4) A municipal electric light plant outside of the town that it serves
 - (5) Property held by the state and located in any town other than that in which the institution of which it forms a part is located.
 - (6) Property kept by a home, orphanage or hospital that is leased to others for income or profit
 - (7) Property used for recreation and fitness, unless the town so votes

32 VSA 3831 – college and university property (effective 1959)

- (a) & (b) Property acquired after 1941 shall be set in the grand list and taxed at a value fixed by the next appraisal, unless the town votes to exempt the property, or it belongs to class of lands owned by a college before the town in which it resides was organized
- (c) Adjusts the taxable value for college and university property in a town that undergoes a reappraisal after 1982

32 VSA 3840 – Charitable and fraternal organizations (effective 1961)

- Property owned by charitable and fraternal organizations may be exempt upon a vote of the town

“When a society or body of persons associated for a charitable purpose, in whole or in part, including fraternal organizations, volunteer fire, and ambulance or rescue companies, owns real estate used exclusively for the purposes of such society, body or organization, such real estate may be exempted from taxation, either in whole or in part, for a period not exceeding 10 years, if the town so votes. Upon the expiration of such exemption, a town may vote additional periods of exemption not exceeding five years each.”

32 VSA 5404a

- Maintains certain exemptions from the statewide education tax for 10 years after adoption of Act 60
 - Town voted exemptions voted before 1997
 - Certain tax stabilization agreements voted by a town
 - Agreements related to affordable housing approved by VEPC or the Commissioner of Taxes
 - Certain subsidized housing units