CHURCH EXEMPTION FROM FORM I-990: VESTIGIAL FIRST AMENDMENT MISINTERPRETATION

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I. INTRODUCTION

Current IRS reporting standards require most tax exempt organizations to file a Form I-990 to publicly disclose key aspects of their management structure, such as governing board members and the salaries and identities of their highest paid employees. However, churches (a form of tax-exempt organization) are not required to file an I-990, nor are they required to publicly disclose this key management information. This lack of disclosure requirement allows a minority of church leaders to violate the no private inurement tax exempt requirement[1] at the expense of the reputations of the remainder of religious organizations.[2]

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[1] The main purpose behind tax exemption for religious organizations exists not to subsidize religious activities, but to subsidize charitable and educational behaviors that emerge from religion. See *Kessler v. Commissioner*, 87 T.C. 1285, where the court denied petitioner rights to tax exempt status on First Amendment and Fourteenth Amendment grounds when the petitioner claimed that his religion required him to vacation to Puerto Rico once a year. The court found these expenses to be in violation of the no-private inurement requirements of I.R.C. §170, reasoning that

> "Usually people contribute to charitable and educational objects out of their surplus. After they have done everything else they want to do, after they have educated their children and traveled and spent their money on everything they really want or think they want, then, if they have something left over, they will contribute it to a college or to the Red Cross or for some scientific purposes. Now, when war comes and we impose these very heavy taxes on incomes, that will be the first place where the wealthy men will be tempted to economize, namely, in donations to charity. They will say, "Charity begins at home."

Kessler v. Commissioner, 87 T.C. 1285, 1291 (T.C. 1986). The *Kessler* court did not question the validity of the petitioner's beliefs, they concluded that "Petitioners are free to practice their religion, they just won't be subsidized." Id.

[2] One well known case of no private inurement violation was that of the infamous *Bakker* case in 1987. According to the Los Angeles Times, PTL founders Jim and Tammy Bakker found themselves under investigation for luxury items purchased with ministry funds, ranging from a $592,000 ocean front condominium in Palm Beach, Fla., to an $800 Gucci briefcase…. Such purchases are among $1.3 million dollars of items charged by the Bakkers to PTL between 1981 and 1983 and which the IRS auditors have questioned as possible personal expenses in the course of their continuing audit into the finances of the tax exempt organization….." *See* Author Unknown, *IRS Questions $1.3 million in Purchases Bakkers Charged to PTL*, L.A. Times, May 17, 1987, Part I, at 17, Col. 1. The nature of the couple's no inurement violations were so egregious and attracted so much negative media attention that the original sentence of 45 years in prison and a fine of $500,000, was vacated upon appeal on the grounds that the trial judge had impermissibly taken his own religious convictions into account. *United States v. Bakker*, 925 F. 2d 728 (4th Cir. 1991). Judge Potter, the original sentencing judge, claimed that "He [Bakker] had no thought whatsoever

The most salient argument against imposing[3] and enforcing[4] church tax filing requirements (like the Form I-990) is that it is impermissible and irreconcilable to fundamental First Amendment values of freedom from excessive government interference with religion.

This paper will argue that it is *not* impermissible to require churches to file an I-990 under First Amendment standards (rather, it may be *required* under First Amendment standards), for several reasons.

The first of these reasons is that neither the Framers' original intent nor subsequent First Amendment interpretations are violated by this mandatory I-990 reporting requirement. While the First Amendment guarantees the freedom from government interference with *personal* religious *preference*, the freedom from government interference to worship had different connotations and context in the 1700s than the modern day, in which churches are subject to the complex modern income tax structure.[5] The Framers did not forsee the need for public managerial disclosure in the context of today's modern progressive income tax structure, much less the subsequent requirement for filing the I-990, given the Founders' aversion to taxation without representation (progressive taxation).[6]

Secondly, requiring all churches to file an I-990 would be nondiscriminatory, simplifying practice, especially given the IRS's nebulous and outdated definition of "church"[7] that unconstitutionally[8] discriminates against some legitimate churches that are currently required to file Form I-990 under the current category of "religious

about his victims and those of us who do have a religion are ridiculed as saps from money grubbing preachers or priests." Id.

[3] *See* Worthing, Sharon, "The State Takes Over a Church," in Kelley, D.M., ed., Annals of the American Academy of Political and Social Science, 446:137 (Nov., 1979).

[4] In 1980, the California branch of the Worldwide Church of God unsuccessfully appealed to the United States Supreme Court to reclaim their assets seized in violation of the no inurement requirement of their tax exempt status, claiming that the seizure and subsequent control of their church (shutting it down) was a violation of their First Amendment Free Exercise rights. Among their no inurement violations included a multimillion dollar home for the lead pastor in Beverly Hills, California and annual reported salary of $300,000 a year. *See* Appendix, Petition for Certiorari at 170b-172b, *Worldwide Church of God, Inc. v. California*, 449 U.S. 900 (1980) (*denying cert.*).

[5] See Daniel A. Smith., Tax Crusaders and the Politics of Direct Democracy, 21-23. (1998), 21-23.

[6] Id.

[7] While integrated auxiliaries of churches are also exempt from this filing, an integrated auxiliary as defined by the I.R.S. and Treasury must have a parent church as defined by the I.R.S. to sponsor their exemption from filing, and thus this paper will therefore focus on the constitutionality of filing for the churches, which will indirectly determine the constitutionality of the integrated auxiliaries acting under their tax exempt umbrella of no reporting requirements. See I.R.C. § 508(c)(1)(A)(2006); I.R.C. § 6033(a)(2)(A)(i)(2006).

[8] Many constitutional scholars believe that any attempt by the government to define religion at all should be resisted as a First Amendment violation. Milton Konvitz has written, "Not only should the question of religious truth or falsity and sincerity or hypocrisy of religious professions e beyond the cognizance of government, but even the very meaning or definition of "religion," as the term is used in the First Amendment, should be outside the area of governmental inquiry." Milton Konovitz, Religious Liberty and Conscience: A Constitutional Inquiry 32 (1968).

organizations."[9] The current I.R.S. definition of "church" is furthermore increasingly discriminatory as more church organizational structures move away from the traditional church definition, given the recent advent and trend towards multi-site, multi-partner, and internet-based church ministries.[10]

Thirdly, the same accounting transparency principles that apply to nonreligious and religious non-church tax-exempt organizations still apply to religious organizations classified as churches[11] and integrated auxiliaries[12] by the IRS, despite the long standing public policy decision to remove churches from financial accountability.[13] Logistical complications, such as internal groupthink, and divisions between countless sects would make an efficient, nonbiased creation of uniform religious transparency standards from *within* the religious community unlikely. Therefore, rather than inhibiting it, the Free Exercise Clause of the First Amendment would be *enhanced* by full disclosure requirements of an I-990 filing by giving internal leaders and congregants a transparency reporting mechanism that currently does not exist.[14]

Lastly, there would be minimum additional reporting burden. Inconvenience in imposing the Form I-990 filing requirements in addition to the Form 1096 would be minimal, given current reporting requirements, and might in fact *lower* the need for complicated government audits of churches by increasing transparency from within and increasing the likelihood of a self-governing checks and balances system.

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[9] Also exempt from filing I-990s are organizations labeled as auxiliary organizations or churches. See I.R.C. § 508; I.R.C. § 6033, *supra* note 7.

[10] Amy L. Sherman. "Wasted Charity." Christianity Today, November 11, 2011.

[11] The word "church" is not in the Constitution, nor is it in the First Amendment. Therefore, the I.R.S. needed to create their own definition to be able to give churches as they define churches special tax exempt status over other religious organizations. Yet the Supreme Court has ruled consistently that one need not belong to a church or denomination to be religious under constitutional grounds. *See Torcasco v. Watkins*, 367 U.S. 488, 488 (1961); *United States v. Seeger*, 380 U.S. 163, 165 (1965); *Welsh v. United States*, 398 U.S. 333, 346 (1971).

[12] According to the Senate Report that led to the 1969 Revenues Act that for the first time taxed nonrelated business revenues of churches and their "integrated auxiliaries", the term "integrated auxiliary" was defined as an organization including "missions societies and the church's religious schools, youth groups, men's and women's groups." *See* S. Rep. No. 552, 91st Cong., 1st Sess. 52, reprinted in 1969 U.S. Code Cong. & Admin. News 2027, 2029. This definition was further amended in 1976 by the Treasury Department who defined "integrated auxiliary as one" whose primary purpose is "to carry out the tenets, functions, and principles of faith in the church" and whose activity directly promotes religious activity within the church." *See* Prop. Treas. Reg. § 1.60332-(g)(5)(i), 41 Fed. Reg. 6073 (1976).

[13] This lack of accountability is revocable under the nebulous criteria of "reasonable belief" that the church is not exempt under 501(a) or is engaged in taxable activities. I.R.C. § 7611(a)(2)(2006).

[14] Under IRS regulations issued in April 1999, a tax-exempt organization must make its 990 filings available for public inspection for a period of three years following the filing of the form. The new regulations require tax-exempt organizations to provide photocopies of the Form 990 to anyone making a request. These copies must be made available immediately to anyone requesting them in person and within 30 days to anyone requesting them in writing. *See* Gina M. Lavarda, Nonprofits: Are You At Risk of Losing Your Tax Exempt Status?, 94 Iowa L. Rev. 1473, 1476-77 (2009) [hereinafter Lavarda].

This paper will first begin with a brief explanation of the Form I-990 and the implications it has upon tax exempt accountability. Next, this paper will discuss the evolving tax code and how the evolution from the Revolutionary ideal of "no taxation without representation" to the modern progressive income tax and its tax exempt derivatives. Then this paper will discuss the progressive historical interpretation of the First Amendment and why the prohibition of church filings of Form I-990 is constitutionally *required*, using an analysis of the *Lemon* test as it applies to religious taxation issues. Finally, this paper will propose a constitutionally acceptable solution of eliminating the "church" IRS definition and requiring all religious organizations to file the Form I-990.

II. I-990: WHO FILES, REPORTING INFORMATION, AND HOW IT RELATES TO CHURCHES

Most tax exempt organizations, with the notable exception of churches, are annually required to file the IRS Form I-990 under IRC 501(a).[15] The purpose of the Form I-990 is to provide accountability to the public about these organizations' fiscal behavior and management, and is often the sole or primary source of this information to prevent 501(c)(3) violations of no private inurement.[16] Tax exempt organizations required to file an I-990 must comply with all Form I-990 disclosure requests.[17] This means that tax exempt organizations are required to make their I-990 information available both through individual disclosure requests, and publicly, through online disclosure. A tax exempt organization must make its I-990 filings available for public inspection for a period of three years following the filing of the form, and tax exempt organizations must provide photocopies of the Form 990 to anyone making a request.[18] These copies must be made available immediately to anyone requesting them in person and within 30 days to anyone requesting them in writing.[19] Failure to comply with disclosure requests brings a heavy penalty. IRS regulations dictate that any corporate official refusing to provide copies of the organization's Form 990 filings to a member of the public requesting the forms may be assessed a personal penalty of $20 per day, up to a maximum penalty of $10,000. This is in the case of negligent failure to timely comply with disclosure requests. An additional penalty of up to $5,000 may apply in cases of willful refusal to comply with a disclosure request. An aggregate penalty of up to $15,000 would be a hefty amount for many churches to pay, especially small financially struggling churches in 2011.[20]

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[15] "2010 Instructions for Form 990 Return of Organization Exempt from Income Tax" U.S. Department of the Treasury, 2010 [hereinafter 2010 Instructions for Form 990 Return]
[16] *Lavarda*, *supra* note 13 at 1476.
[17] Id.
[18] Id.
[19] Id.
[20] Id.

Because the I-990 is often the sole and primary source of this internal management information, congregants within churches cannot assess as easily the usage of their donations.[21] I-990s would thus provide a tool of church governance that currently does not exist. If churches were required to file Form I-990, then their highest paid employees, their corresponding salaries, and the governing board members of these churches will be publicly revealed, along with their corresponding salaries.[22] If the identities of these governing church members were publicly available, it would open the door to accountability for organizational culture and financial practices. It would also grant members an internal pinpoint for bringing internal grievances to church leadership or bring internal grievances to external IRS attention, if necessary, using a combination of the IRS whistleblower program[23] or anonymous tips. Given the huge return on investment, informants have reduced the number of no change audits, thereby saving scarce government resources and reducing the number of no change audits, thereby saving scarce government resources and benefiting complaint taxpayers. If church leaders do not comply with internal sanctions, congregants then can report suspected fraud to the IRS (external governance). If deductions do not match the criteria above, then suspicious congregants can impose internal sanctions upon their financial leadership (internal governance). It is preferable that congregants use this method of self-correction first, as it minimizes costly and perhaps inefficient government interference. Congregants can choose the method of correction and enforcement that best suits their particular organizational needs and practices, which government agencies may be ill equipped to do.

Reporting suspicious tax filings[24] can be done anonymously by filing IRS Form 3949-A[25]. Because whistleblowers are rewarded 15 to 30 percent[26] of collected back taxes from noncompliant organizations, internal congregants and outside whistleblowers would provide a vital and efficient potential source of enforcement of the I-

[21] 2010 Instructions for Form 990 Return, *supra* note 14.
[22] Id.
[23] The IRS whistleblower program has an enormous rate of return on the IRS reporting budget. For example, in 2007 the IRS took an enforcement budget of $7 billion and used it to collect $59.2 billion in unpaid taxes. Edward Morse. *Whistleblowers and Tax Enforcement: Using Inside Information to Close the "Tax Gap,"* 24 Akron Tax J. 1, 7 (2009).
[24] Deductions (like salaries) of tax exempt organizations must be comparable to ordinary and necessary expenses that was paid or incurred during the taxable year in carrying on a trade or business activity. *See* IRC § 162 (2006).
[25] "How do You Report Suspected Tax Activity?" I.R.S. instructions, accessible at http://www.irs.gov/individuals/article/0,,id=106778,00.html, (November 11, 2011 9:00 P.M.).
[26] The Pension Protection Act of 2006 increased the possible reward for whistleblowing by eliminating the monetary cap on the possible reward for whistleblowers. *See* David M. Schizer. *Enlisting the Tax Bar,* 59 Tax. L. Rev. 331, 331 (2006).

990 reporting requirement for churches at minimal additional cost to the government,[27] especially in the light of the current recession and subsequent limited government resources.

Tax exempt organizations are required to provide the public with their I-990s within a reasonable amount of time (defined as two weeks)[28]. Through a mandatory I-990, church members who are suspicious of pastors' overcompensation or general management structure can externally retrieve their pastors' financial records from external sources, rather than risk castigation or paralyzing groupthink behavior by asking for these records internally.[29] Publicly available I-990s will thus create a platform for internal accountability for good reporting practices that previously did not exist, especially if the reported salaries do not match the congregants' tithes and other expenses and appear to violate the no private inurement requirement[30] of tax exempt organizations.

If the I-990 filings were required for churches as they are for other nonprofits, congregants then can compare their pastors' reported compensation with their contributions, and the ostensible lifestyle of their leadership, and make appropriate internal corrections.[31]

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[27] Id. at 331.

[28] 2010 Instructions for Form 990 Return, *supra* note 14.

[29] In 2008, the Wall Street Journal reported the arrest and incarceration of Karolyn Caskey, a 71 year old Sunday School teacher. Ms. Caskey, a member of Allen Baptist Church, gave ten percent of her pension to the church and paid its electricity bills on occasion when it was struggling financially. *See* Alter, Alexandra. *Banned From Church,* Wall Street Journal, January 18, 2008, Page W1 [hereinafter Banned From Church].

Prior to her arrest, Ms. Caskey had questioned the church organizational practices during their governing board meetings and asking for a broader board of elders to help govern the church's organizational structure, rather than forcing the congregants to follow the lead of a few elite. Upon entering the church grounds on a Sunday morning following their disagreement, the lead pastor called the police to report her as a trespasser and had her arrested. They refused to recommend her to another Baptist Church, a requirement for membership in her denomination. Id. While Ms. Caskey's case is rather extreme, for small, financially struggling churches like Ms. Caskey's, whose unscrupulous pastors may be currently using their exempt status to inhibit the First Amendment Establishment rights of their congregants to worship freely (in Ms. Caskey's case, this is evident in their refusal to refer her to another Southern Baptist Church), this requirement would deter this First Amendment inhibiting and intimidating behavior by forcing churches to be open with their members and those outside their church with their financial structure. The insular organizational model of smaller churches makes them especially susceptible to the groupthink phenomenon that would make true internal accountability difficult sans external, neutral reporting mechanisms. Id.

For example, if one of the reasons Ms. Caskey wanted to have a larger board of elders was to find a more democratic way to govern the churches finances, then she could offer externally available evidence of the current governing elders' compensation as part of her proof to other congregants.

[30] One of the main criteria for obtaining and maintaining tax exempt status is no private inurement, meaning that the compensation for tax exempt employees cannot exceed that of which would be otherwise be paid in a similar position in a for-profit environment. Violation of no private inurement would be grounds for immediate revocation of the organization's tax-exempt status. *Better Business Bureau of Washington D.C. Inc. v. United States,* 326 U.S. 279, 284 (1945).

[31] In 2009, Senator Charles Grassley, the leading Republican chairman of the Senate Finance Committee, in collaboration with private Christian financial watchgroup organizations, led a probe of six televangelist ministers suspecting of violating the no private inurement rule. Rod Pitzer, the chairman of Ministry Watch in North Carolina, stated criticized such church management as a "dictatorship" and that ministries lacking accountability "give a black

If a tax-exempt organization fails to file an I-990 for three consecutive filing periods, it loses its tax-exempt status with the IRS. According to a 2011 report published by the Urban Institute, a nonprofit dedicated to independent reporting of social organizations throughout the United States, nearly a quarter of a million nonprofits (279,599) lost their nonprofit status for failure to comply with filing their I-990s for the fiscal year ending in 2010.[32]

If a church's gross receipts were over $10,000, then in order to regain their nonprofit status, they would have to reregister as a nonprofit with the IRS, and pay an $850 refiling fee. This refiling fee process should deter churches who do not comply with good accounting and financial reporting practices from not complying. These penalties would keep churches from their failure to timely file the I-990 and encourage timely, public disclosure of the I-990, thanks to the external and neutral IRS regulations and enforcement that already exists. More importantly, the churches that do not file their I-990 in a timely manner, or who are flagged by parishioners for fiscal abuse can quickly and efficiently be differentiated from churches who are behaving fiscally honest.

Failure to comply with disclosure requests brings a heavy penalty. IRS regulations provide that any corporate official refusing to provide copies of the organization's I-990 filings to a member of the public requesting the forms may be assessed a personal penalty of $20 per day, up to a maximum penalty of $10,000. This is in the case of negligent failure to timely comply with disclosure requests. An additional penalty of up to $5,000 may apply in cases of willful refusal to comply with a disclosure request. An aggregate penalty of up to $15,000 would be a hefty amount for many churches to pay, especially small financially struggling churches in 2011.[33]

According to a 2011 article by *Christianity Today*, much of American religious charitable giving either "is either wasted or actually harms the people it is targeted to help."[34] Quoting author veteran urban minister and "Toxic Charity" author Robert Lupton,[35] the 2011 article bemoans that Americans evaluate their giving "by the rewards we receive through service, rather than the benefits received by the served."[36] The author goes on to state that "our free food and clothing distribution encourages ever-growing handout lines, diminishing the dignity of the poor while

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eye to churches and Christians who are trying to do things in the right manner." See Laura Strickler, *Senate Panel Probes 6 Top Evangelists.* (December 12, 2011, 1:00 A.M.). http://www.cbsnews.com/stories/2007/11/06/cbsnews_investigates/main3456977.shtml

[32] See Author Unknown, *Over 279,000 Nonprofits Lose Tax Exempt Status.* http://www.philanthropyjournal.org/news/top-stories/over-279000-nonprofits-lose-tax-exempt-status (December 11, 2011, 9:00 A.M.).

[33] "Tax Guide to Churches and Religious Organizations," Publication 1828 (11-2009) Catalog Number 21096G U.S. Department of the Treasury (2009), [hereinafter Tax Guide to Churches].

[34] Amy L. Sherman. "Wasted Charity." Christianity Today, November 11, 2011.

[35] Robert D. Lupton. Toxic Charity: How Churches Hurt Those They Help (and How to Reverse It), 25 (2011).

[36] Id.

increasing their dependency."[37] In contrast to religious organizations at the tax exemption's inception in the late 1800s, which were often the only efficient means available to distribute aid to the needy, Lupton criticizes that the modern "compassion industry" is "almost universally accepted as a virtuous and constructive enterprise," but its "outcomes are almost entirely unexamined."[38] Many of these outcomes could be examined much more adequately if there was a more neutral, external way to pinpoint the governing officers of all religious organizations through the Form I-990. Church managers who are wasteful of their resources can thus be more easily targeted and removed.[39]

Thus, requiring a Form I-990 actually creates the opportunities to *decrease* the need for costly government oversight of tax procedures because it *increases* transparency *within* the organization and thus *increases* the opportunity for reliable self-governance through good accounting practices. Increasing reliable self-governance through good accounting practices will also decrease the overall desire to abuse the system and decrease wasteful (tax-funded!) further complications to the tax code designed to prevent these abuses.

In addition to the numerous transparency advantages of making churches file an I-990, it will lead to a more conducive worship environment because of the result of less intra-church conflict. Thus, the Free Exercise Clause would be more adequately catered to.

Enforcing church I-990 filings will lead to less intra-church conflict because unscrupulous or irresponsible pastors will have fewer mechanisms to hide poor financial management from congregants and outsiders. More efficient and transparent financial reporting structures less resources would be wasted on inefficient management structures.

Enforcing church I-990 filings will also lead to more freedom of congregants to worship freely because allowing full disclosure *before* entering the church will allow outsiders to objectively and independently assess the pastors' financial legitimacy both internally, within the congregation, and externally, with the IRS. If potential new church members were able to objectively and independently assess a pastor's financial integrity before they joined a church as members, this can eliminate much of the groupthink or fear of castigation by demagogical and financially corrupt pastors because congregants will not have had the time to create the social and emotional bonds that create the paralyzing groupthink accountability models.

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[37] Id.
[38] Id.
[39] Id.

Because churches are currently required to fill out Form 1096 (Annual Summary and Transmittal of U.S. Tax Information Returns) and all the 1099s and W-2s of all employees,[40] the additional reporting burden to file an I-990 would likely be very minimal because the churches would already have the additional reporting information at hand. Furthermore, church ministers and employees must file individual income tax returns with the government, and can hand over their records to reconcile with the church's internal balance sheets. In order to count as church clergy under IRS purposes, pastors need to file a Form W-2, which they then can report to the church governing board who prepares the church's taxes.

Despite the potential increase in transparency and reduction in the complexity of the tax code that requiring churches to file the form I-990 would entail, why are churches exempt from filing the I-990? More importantly, would requiring churches to file the I-990 violate the First Amendment's Establishment and Free Exercise clauses? The following two sections will discuss the history behind the church exemption from the I-990 filing and juxtapose this history with the United States Supreme Court's interpretation of the constitutionality of governmental interference with religious practice.

III. EVOLVING CHURCH TAX CODE: FRAMERS' INTENT TO MODERN COMPLEXITIES

Concern for financial abuses within churches have long preceded American tax history, since biblical times.[41] Financial abuse by church leadership was one of the primary concerns of the Catholic church that led to the Reformation and the Protestant Church schism in Martin Luther's day.[42] This concern continues today in America in the form of a minority of pastors taking financial advantage of their congregants in blatant violation of the no inurement policies.[43] The lack of requirement for churches to file an I-990, which is a remnant of the Revenue Act of 1943 that required tax exempt organizations *with the exception of churches* to file the I-990 is a vestigial remainder of a common misinterpretation of the Establishment Clause of the First Amendment.

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[40] See Tax Guide to Churches, *supra* note 32.

[41] According to the Christian tradition, Judas Iscariot, the first treasurer of the Christian church who betrayed Jesus Christ for thirty silver pieces, stole repeatedly from the disciples' money bag. *See* John 12:6.

[42] One of the main perceived financial abuses that Martin Luther (a law school dropout who became a priest known as the Father of the Reformation), fought in the earliest days of the Reformation was the perceived financial abuses in the form of heavy indulgence sales. Indulgences were fees worshippers were induced to pay to the Catholic Church in exchange for their salvation and the right to remain in good standing with God.

This was summed in the famous 95 Thesis that he nailed upon the Wittenburg University door in 1520, most poignantly expressed in Thesis 86, in which he lamented, "Why does the pope, whose wealth today is greater than the wealth of the richest Crassus, build the basilica of Saint Peter with the money of poor believers rather than with his own money?" See Hillerbrand, Hans J., "Martin Luther: Indulgences and Salvation," in Encyclopedia Britannica, 2007.

[43] Banks, Adele M. "Evangelical Probe Conducted by Senate Finance Leader" Huffington Post. January 8, 2011.

The First Amendment reads as follows: "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances."[44]

The first part of the First Amendment, which prohibits the establishment of religion, is known as the Establishment Clause. The second, which allows for free choice of religion, is known as the Free Exercise Clause. Many Americans over the years have interpreted these two clauses as a prohibition on *any* government interference on their worship practices. However, in order to fully understand and appreciate the religious rights that the First Amendment protects (and how it pertains to the exemption of churches filing the I-990), it is important to view the First Amendment in context of the time of its framing and the income tax structure at the time of the Framers, how it has evolved from "no taxation without representation" to a constitutionally permissible progressive (and increasingly complex!) income tax, and how this new income tax structure relates to the tax exemption that churches enjoy today. Before the tax exempt status of organizations emerged, the *desire* for tax exemption needed to emerge by the formalized progressive taxation of companies. Formalized progressive taxation did not occur until nearly a century after the Revolutionary War.[45] The First Amendment was drafted as part of the Bill of Rights, a package of rights that the framers of the Constitution ratified to augment the Constitution in 1791.[46] At the time, the federal tax system was very different than it is today.[47] The representatives of the newly independent states were very adamant against imposing a complex income tax structure by a central government.[48] The Framers had just fought a long and bloody war with England upon which one of its main premises was "no taxation without representation." In drafting the Constitution, the Bill of Rights framers likely remembered their resentment and subsequent war at the requirement to fund England's trading company war by the sudden imposition of numerous and arbitrary heavy taxes.[49]

This sentiment of equal taxation by population proportion is evident in the language of Article I, Section 8, Clause I of the Constitution (known as the Taxing and Spending Clause), which states that Congress shall have the power to impose taxes, duties, imposts, and excises, but it was required that the taxes, duties, imposts, and excises

[44] U.S. Const. Amend. I
[45] Rev. Act 1861.
[46] John C. Miller. Origins of the American Revolution. 31, 99, 104 (1943).
[47] Id.
[48] Id.
[49] Id.

should be equal throughout the United States.[50] This sentiment against direct taxation without representation was further enumerated by Article I, Section 9, Clause 4, which stated that "no capitation, or other direct tax shall be laid, unless in proportion to a census or enumeration herein before to be taken."[51]

Though the Constitutional Framers were clear in their original intent to keep taxation equal through fair representation (as shown by the enumeration clause mentioned in the above paragraphs) as a *result* of being taxed by centralized government to fund a war, the first progressive income tax ironically emerged as a *result* of needed war funding. The American Civil War in 1861 created the need for the United States Government to raise funds quickly. The solution was a progressive income tax, The Revenue Act of 1861.[52]

While the tax was expired shortly after the Civil War's end, an angry taxpayer challenged the Constitutionality of the 1861 Act in the 1880 case *Springer v. the United States*.[53] In *Springer*, the taxpayer plaintiff claimed the progressive income tax was unconstitutional because it was taxation without representation.[54] The *Springer* Court unanimously ruled against the plaintiff, not on grounds of lack of merit, but rather on grounds that it would create an administrative nightmare of tax refunds impossible to enforce if they ruled on the side of the plaintiff.[55] Thus, the ruling did not properly reflect the Supreme Courts' view on the constitutionality of the progressive income tax.[56]

In response to resistance of taxpayers to their "taxation without representation," Congress passed the Revenue Act of 1894, which for the first time granted tax deductions for donations to certain charitable religious organizations.[57] The 1894 Act however, did *not* distinguish between churches and non-churches within religious organizations, rather it exempted from tax "corporations, companies, or associations organized and conducted solely for charitable, religious, or educational purposes."[58] Thus in 1894, the modern IRS defined church exception for the I-990 would not have applied, had the filing requirements been enacted at that time because there was no IRS defined church distinction from religious organizations.[59]

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[50] Id.
[51] Art. I, Section 9, Clause 4
[52] Rev. Act 1861
[53] *Springer v. the United States*, 102 U.S. 586, 587 (1881).
[54] Id.
[55] Id.
[56] Id.
[57] Act of August 15, 1894, ch. 349, 28 Stat. 553.
[58] Revenue Act of 1894, ch. 349, Section 32, 28 Stat 112.
[59] Id.

While many might erroneously believe that the public policy reasons behind the tax exemption of churches and religious origins was rooted in the Establishment Clause, the true reason for this exemption was practical in nature. At the time the Revenue Act of 1894 was enacted, the United States was in a deep depression, and churches were the most efficient and often the only available way to distribute aid to the needy.[60] The role of church aid was especially vital because this depression occurred when neither state nor federal governments distributed publicly-funded subsidies to the poor, and offering tax deductions to those who donated to religious-based aid groups was an efficient way for the U.S. Government to distribute aid to the needy.[61]

Both the Revenue Acts of 1861 and 1864 was later repealed by the 1865 case of *Pollock v. Farmer's Loan and Trust Company*.[62] In *Pollock*, plaintiff shareholder sued the defendant for giving part of his dividend revenues in taxes to the United States Government under the Revenue Act of 1861, claiming that the progressive income tax of land revenues was unconstitutional because it was a form of direct because tax on real estate is a direct tax,[63] and therefore, a tax on income from real estate is a direct tax too.[64]

The Supreme Court reasoned that because the tax upon *Pollock's* plaintiff was a taxation against the revenues from land, this was a direct tax. The Constitution requires that the income taxes from land were a form of direct taxes that must be apportioned according to a census based on the population.[65] Taxing income from land was not allowed according to a census based on the population (it would have been too impractical). Therefore, the progressive income tax on land revenues (taxation without representation) was ruled unconstitutional because there was no taxation based on a census of the population.[66]

Progressive income taxes became constitutional upon two major events. The first was when corporate income taxes without apportionment (taxation without representation under the original Framers interpretation) were deemed constitutional in the 1909 United States Supreme Court case, *Flint v. Stone Tracy Company.*[67] Soon after,

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[60] E. Bogart, An Economic History of the United States, 22 (3d. Ed. 1920).
[61] Hoff, Reka. *The Financial Accountability of Churches for Federal Income Tax Purposes: Establishment or Free Exercise?* 11 Va. Tax Rev. 71.
[62] *Pollock v. Farmers' Loan & Trust Co*., 157 U.S. 429 (1895), *aff'd on reh'g*, 158 U.S. 601 (1895).
[63] Id..
[64] Id..
[65] Id..
[66] Id..
[67] The court in *Flint* reasoned that a corporate excise tax without apportionment was constitutional because Congress had the power to lay such a tax. The court reasoned that if a tax was deemed unfair, the responsibility lay not upon the courts, but upon the citizens by whom its members were elected. *Flint v. Stone Tracy Co.* 220 U.S. 107. 109 (1913).

the 16th Amendment of the United States Constitution was ratified by the States in 1913.[68] This amendment made general income taxation by apportionment constitutional, overruling the Court's decision in *Pollock*.

The increase in progressive taxation led to an increased desire from tax-exempt organizations to look for ways to claim exemption, now that progressive taxation decreased their available donorbase.[69] This desire was exacerbated by the First World War, which led the U.S. Government to increase taxes in 1917.[70] This need led to the Revenue Act of 1917, which increased tax rates while lowering exemptions.[71] Like the majority of dichotomous delegates who lobbied against a vertical church-state relationship in the original pre-Constitution hearings,[72] most of the prominent charities that were represented in the Senate Hearings leading up to the 1917 Act were faith based.[73] One of the major proposed revenue increases under the 1917 Act was to increase the postage rates on *all* news publications.[74]

The publishers of many of the most prominent Christian tax exempt organizations were present to lobby the proposed unrelated business taxes at the 1917 hearings of the Ways and Means Committee that determined the terms of the 1917 Act.[75] Leading the Christians lobbying against the proposed tax hikes upon privately owned church publications was Mr. Philip E. Howard, the president of the privately owned *Sunday School Times* based in Philadelphia, Pennsylvania.[76] Howard, concerned for the financial future of his publication, lobbied for a special church tax exception from a proposed postage tax increase on all privately owned journals published by churches.[77]

Howard explained to the committee, that "many denominations do not have privately owned journals at all, but are served by those who undertake to publish privately owned journals, often at great sacrifice."[78] Howard also stated that many churches, like the Roman Catholic Church, published privately owned magazines that if the

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[68] U.S. Const. Amend. XVI.
[69] Arnsburger, Paul, Ludlum, Melissa, Riley, Margaret, and Stanton, Mark. "A History of the Tax-Exempt Sector: an SOI Perspective." Statistics of Income Bulletin, Winter 2008. Internal Revenue Service, 2008 [hereinafter Arnsburger, *et. al.*].
[70] Id..
[71] Id..
[72] 1 Jeff. Works, 45
[73] *Revenue to Defray War Expenses*. 65th Cong. 9-10 (1917).
[74] Id.
[75] Id.
[76] Id.
[77] Id..
[78] Id.

proposed bill was passed, would be indirectly forced to stop publishing because their revenues would not cover their operating costs because they were not operating for profit.[79]

In making the arguments that the Revenue Act's inability to separate private church not for profit publications from regular religious tax exempt organizations, Howard *implicitly* argued that if the Act was passed, many sects would be discriminated against under the Establishment Clause. Howard indirectly stated this discrimination would occur because these sects would have very limited means to spread their religious messages and communicate with parishioners, which Howard categorized as "the most indispensable […] in conserving and quickening the deepest spiritual issues of our national life."[80]

Perhaps in response to this aggressive lobbying by Howard and his compatriots in the private Christian publishing business, the passage of the 1917 Revenues Act also came with the birth of the tax exemption of side business revenues of churches.[81] The exemption of unrelated business income for churches was to go unchallenged until 1969.[82]

This nonrelated business exemption for churches led to an increasingly complex tax exempt income tax code that mirrored the increasingly complex *general* income tax code. The progressive complications of both codes led to need for more reforms as the increase in complexity led to more abuses of the tax code (which led to the compulsory I-990 filings of today) were likely not foreseeable by the original Constitutional Framers.

Several other widespread reforms took place over the decades since the 1917 Act, such as the Revenue Act of 1943, which required the majority of tax exempt organizations to file the I-990, but again exempted churches and religious organizations[83] from filing the I-990.[84] The records of the 1943 Senate Hearings[85] are void of any pro-faith appeals like Mr. Howard's, nor did they record any special reason for this exemption.[86] Thus, this exemption of churches and religious organizations was likely the result of an extension of Mr. Howard's lobbying work and the predominant view of churches as a primary source of aid to the needy.[87] However, the 1943 House Report did note

[79] Id..
[80] Id.
[81] Arnsburger, et. al., *supra* note 69.
[82] *See* S. Rep. No. 552, 91st Cong., 1st Sess. 52, reprinted in 1969 U.S. Code Cong. & Admin. News 2027, 2029.
[83] I.R.C. § 54(f); (§6033 of the present Code)
[84] J. Baker, Government and the Mission of Churches: the Problem of Integrated Auxiliaries, 3 (Staff Report, Baptist Joint Committee on Public Affairs, 1977), [hereinafter Government and the Mission of Churches].
[85] H.R. Rep. No. 871, 78th Congr., 1st Sess. 24-25 (1943) [hereinafter H.R. Rep. No. 871].
[86] Id.
[87] *Revenue to Defray War Expenses*. 65th Cong. 9-10 (1917).

the concern that certain unscrupulous tax exempt organizations were claiming tax exemption in order to compete with for profit businesses and thus the United States Government was seeking remedial action.[88]

The Revenue Act of 1950 came from a growing government concerns that many tax exempt organizations were abusing their tax-exempt status under the following five categories: loaning money back to the donors,[89] payments of more than reasonable compensation to the organization's employees,[90] purchases of properties back to the donor,[91] or sales of property back to the donor.[92] In forming the Revenue Act of 1950, the House Committee expressed its concern that much of the intended tax-exempt revenues were never making it to the welfare of those the tax-exemption was originally intended to preserve.[93] Rather, funds were circulating directly back to the "donors" at a profit to both the donor, who did not have to pay taxes on these donations, and the donee, who could claim a tax exemption on income earned through private investments.[94]

The Senate modified the Act slightly, labeling it "too harsh," but added reporting requirements, including to include gross income, expenses, disbursements for exempt purposes out of income and principal, prior aggregate accumulations, and balance sheet).[95] Though churches and religious organizations were once again exempt from filing the I-990,[96] the mechanisms for hiding assets within the church remained just as susceptible to financial abuses as other tax exempt organizations.

The Tax Reform Act of 1967 was the next major reform to the tax exempt filing structure, with increased reporting regulations. Churches and their auxiliary organizations were once again exempt from these additional filing requirements (perhaps because there was limited data to suggest fraud, given their exemption from additional filings in years prior), because the main tax exempt target of the 1967 Act were private foundations.[97] Thanks to data gathered from I-990 and other external reports, nonprofits were increasingly being flagged and found guilty of tax evasion. However, rather than being primarily motivated by eliminating financial corruption, this Act was a result of

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[88] H.R. Rep. No. 871, *supra* note 85.
[89] Worthing, *The Internal Revenue Service as a Monitor of Church Institutions: The Excessive Entanglement Problem*, 45 Fordham L. Rev. 929, 931 (1977).
[90] Id., at 931.
[91] One major abuse was the lease back scheme, in which tax exempt organization A buys commercial business B and rents it back to the owner for profit while B enjoys tax exempt status. Government and the Mission of Churches, *supra* note 84.
[92] *H.R. Rep. No. 2319*, 81st Congr., 2d Sess. 42 (1950).
[93] Id.
[94] Id.
[95] 1939 CODE § 153(a) (now 1954 CODE § 6033(b)).
[96] Revenue Act of 1950, ch. 199, 64 Stat. 906, 948.
[97] H.R. RES. 561, 82d Cong., 2d Sess., 98 CONG. REC. 3489 (1952).

a culmination of nearly a decade of Red Scare investigations that targeted mainly educational based foundations suspected of "abuse."[98] Leading to the 1967 Act were several government led anti-Communist investigations to curb the Communist influence on academia. This thinly veiled anti-Communist agenda was evident in the transcripts of a 1952 report by The Select Committee to Investigate Foundations and other Organizations, otherwise known as the Cox Committee, which reported the following:

> [D]irected to conduct a full and complete investigation and study of educational and philanthropic foundations and other comparable organizations which are exempt from Federal income taxation to determine which such foundations and organizations are using their resources for purposes other than the purposes for which they were established, and especially to determine which such foundations .. .are using their resources for un-American and subversive activities or for purposes not in the interest or tradition of the United States....[99]

The Cox committee's findings concluded that

> The foundations, for the most part, have made no secret of their mistakes, and have stated frankly that in recent years they have recognized the increasing need to be constantly alert to avoid giving unintended aid to subversives. The Committee believes that on balance the record of the foundations is good. It believes that there was infiltration and that judgments were made which, in the light of hindsight, were mistakes, but it also believes that many of these mistakes were made without the knowledge of facts which, while later obtainable, could not have been readily ascertained at the time decisions were taken.[100]

These excerpts show that the heart of these financial investigations was not to root out tax fraud, but to pinpoint Communist sympathizers within academia.[101] Because the heart of these financial investigations and proposed increases in tax accountability was merely a thinly veiled means to monitor and stamp out potential Communist funders of academia, it was little wonder that educational foundations, not churches, were the main

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[98] *Select Committee to Investigate Foundations, Final Report, H.R. Rep. No. 2514*, 82nd Cong., 2d Sess. 8 (1953), [hereinafter Select Committee 1953].

[99] *See* Select Committee, *supra* note 98. A private foundation is a tax exempt organization under section 501(c)(3) which is not a church, a school, a medical organization, or an organization which test for public safety, or which does not receive substantial support from the public or from government. Int. Rev. Code of 1954, §509(a).

[100] Id.

[101] Id.

targets for scrutiny under the subsequent increased regulations of 1967.[102] Thus, churches were to escape additional filing regulations for another two years.[103]

The Tax Reform Act of 1969, which extended the provisions of 1967, increased the amount of filing requirements of tax exempt organizations, as well as increased penalties for violations.[104] For the first time, the tax exemption of unrelated business income that was lobbied for in 1917 so fiercely by private Christian publishers was challenged.[105] The subsequent 1969 Act granted no similar tax exception for revenues earned from privately held religious publications.[106]

In explaining the reasons for the passage of the 1969 Act's passage, the House Committee explained that churches were just as susceptible to the same frauds and abuses that all other tax exempt organizations are, and should be susceptible to the same kinds of regulations for their nonrelated business income.[107] In doing so, the 1969 House Committee reasoned that churches engaged in profit-making activity should lose immunity from tax exemption administrative oversight under the First Amendment, though churches remained excluded from the

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[102] Id.

[103] Tax Reform Act of 1969, Pub. L. No. 971-172, §101, 83 Stat. 492 (codified at scattered sections of Int. Rev. Code of 1954).

[104] Under the new regulations, penalties could range as high as 200 percent of disapproved expenditures in violation of no private inurement. Int. Rev. Code of 1954, §§ 4941(b)(1), 4943(b).

[105] One of the most prominent perceived investigated tax abuses that emerged from the vigorous Red Scare investigations was that of the Christian Brothers in 1958, a group of Christian businessmen who were not ordained ministers who used the tax exempt umbrella of a church to operate a purely for-profit winery business that competed directly with other for-profit winery businesses not operating under a tax exempt umbrella. This led to a regulation change that added detail to the Joint Commission definition of church under Section 170 of the code to tax such for profit income. *See* T.D. 6301, 1958-2 C.B. 197, 222. See also Whelan, *"Church" in the Internal Revenue Code: The Definitional Problems*, 45 Fordham L. Rev. 885, 903-905 (1977) [hereinafter Whelan, "Church"]. *See also* Whelan, *Governmental Attempts to Define Church and Religion*, 446 Annals 32 (1979). In this additional revenue definition in 1958, the purely for profit revenues of the Christian Brothers was distinguished from the side revenues from the Jesuit Loyola University's station WWL-TV operated out of New Orleans. The reason for this distinction was that the WWL-TV station was operated in part by ordained priests (though unlike Christian Brothers, Loyola University had the benefit of political protection from Senator Huey Long, who was a prominent member of the Senate Finance Committee at the time). Id.

[106] Rev. Act 1969.

[107] The House Report of 1969 explained,

> There is inequity in taxing certain exempt organizations on their "unrelated business income" and not taxing others. It has become apparent that organizations now subject to the provision and those not subject to it are equally apt to engage in unrelated business. For example, numerous business activities of churches have come to the attention of the committee. Some churches in operating chains of religious bookstores, hotels, factories, companies leasing business property, radio and TV stations, newspapers, parking lots, record companies, bakeries, cleaners, candy stores, businesses, restaurants, etc.

H.R. Rep. No. 413 (Part 1), 91st Cong., 1st Sess. 46-47 (1969), reprinted in 1969 U.S. Code Cong & Admin. News 2027, 2082.

annual filing requirements.[108] The only Senate explanation for this continued filing exclusion was that requiring churches to file: it was "in view of the traditional separation of church and state."[109] Thus, some vestigial influences of Mr. Howard's 1919 lobbying work remained in place through the 1969 Act.

However, a major problem with the House's reasoning behind drafting this lost tax oversight immunity in the 1969 Act was that they did not address the original 1919 Free Speech and Equal Protection concerns of taxing for independent privately held religious publishing companies. The advent of the internet and its relatively cheap marketing and publishing options did not yet exist for churches in 1969 as it does today, and thus Howard's 1919 arguments against taxing the privately held Christian publishing industry remained relevant but unaddressed. Thus, the 1969 Act still potentially discriminated against sects who might not have the funds or resources to publish their own materials, though this concern has become less relevant as of recent years, given modern (and cheaper) online publishing methods.[110] The 1969 Act's additional reporting requirements became applicable to all churches' side publishing businesses as of 1976.[111]

Another (bigger and still relevant) constitutional problem with the 1969 Act, which is still relevant and problematic today, is that churches were defined based on a set of seemingly arbitrary rules based on the certain aspects of the Judeo-Christian notion of church.[112] There are numerous problems with defining "church" for tax laws in ways that do not violate the First Amendment's principles, as the word "church" is nowhere in the Constitution.[113]

These fourteen criteria are as follows: 1) distinct legal existence, 2) recognized creed of worship, 3) definite and ecclesiastical government, 4) formal doctrine and discipline, 5) distinct religious history, 6) membership not associated with any other church or denomination, 7) organization of ordained ministers, 8) ordained ministers selected after prescribed course of study, 9) literature of its own, 10) established places of worship, 11) regular congregations, 12) regular religious services, 13) Sunday schools for the indoctrination of its young, and 14) schools for the preparation of its ministers.[114]

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[108] Id.
[109] Senate Comm. on Finance, 91st Cong., 1st Sess. Tax Reform Act of 1969, Compilation of Decisions Reached in Executive Sess. 53 (Comm. Print 1969).
[110] *See* Liatraud, Marian. "What's Changing, What's Not." Christianity Today, January 25, 2010.
[111] If an organization or church carried on a trade or business prior to May 27, 1969, the application of the tax was deferred until taxable years beginning on or after January 1, 1976. Int. Rev. Code of 1954, §512(b)(16). *See Joint Comm. on Internal Rev. Taxation, General Explanation of Tax Reform Act of 1969*, 91st Cong., 2d Sess. 66-67 (1970).
[112] *See American Guidance Foundation, Inc. v United States*, 490 F. Supp. 304, 306 (D.D.C. 1980).
[113] Whelan, "Church", *supra* note 105.
[114] *As cited* in *Lutheran Social Serv. of Minn. v. United States*, 758 F.2d 1283, 1286-87 (8th Cir. 1985).

These criteria, while broad in attempt to avoid unconstitutional exclusion, still excluded certain religious sects, such as the Society of Friends (Quakers) or the Christian Scientists, who to this day have protection of the First Amendment Religion Clause. [115]

In addition to the initial IRS defined exclusion of religious sects from their nebulous "church" definition, the IRS found it increasingly difficult to categorize subcategories of religious organizations operating within churches, such as youth groups, mission organizations, and international relief associations, which often partnered with other churches.[116] The 1969 Act attempted to resolve this issue by amending Section 6033 of the 1954 tax code to extend the public reporting mechanisms to "churches, their integrated auxiliaries, conventions, or associations of churches."[117] The phrase "conventions or associations of churches" was designed to separate the hierarchal churches like the Catholic Church operating under the corporation sole model (which later became a mechanism for fraud[118] that was one of the major amendment reforms to the 2006 Pension Protection Act) and the non-hierarchal churches like the Baptists, who were associations of autonomous congregations.[119] The increase in complexity of tax exempt religious definitions showed the increasingly complex and expensive burden of defining churches for the IRS, given the enormous diversity within churches and their organizational structures.[120]

The 1969 fourteen nebulous definitional church criteria in turn led to increased resistance from religious organizations whose church activities were denied church status based on nebulous and discriminatory IRS

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[115] *See Feldstein v. Christian Science Monitor*, 555 F. Supp. 974, 975 (D. Mass.1983).

[116] See, e.g., *Lutheran Social Serv*., 758 F.2d at 1287 (ruling that in light of the IRS criteria, Lutheran Social Service of Minnesota is not a church). *See also American Guidance Foundation, Inc. V. United States*, 4980 F. Supp. 304, 306 (D.D.C. 1980) (acknowledging that some of the IRS criteria are "relatively minor," but ruling that the foundation failed to meet the "central" and "minimal" standards of a church: organized ministry serving an established congregation with regular religious services and religious education for its young and dissemination of a doctrinal code). Thus, these criteria are loosely followed by the courts.

[117] See Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487, 519-23; I.R.C. § 6033(a)(2)(A)(i).

[118] This was a 2008 reform that was one of the top concerns the IRS had about fraudulent churches or religious organizations abusing their tax-exempt structure. Previously, individuals were schemed by churches and religious organizations into becoming a "bishop" or a "parson" under the corporation sole model, and told that if they joined the model, their income under that church would be tax exempt. The IRS published Rev. Rul. 2004-27, 2004-12 I.R.B. 625 to educate and warn the public about this scheme, which defrauded many guileless individuals attempting to evade taxes. *See* IRS Rev. Rul. 2004-27, 2004-12 I.R.B. 625.

[119] Whelan, "Church", *supra* note 105.

[120] As the tax exempt code became more complex, the religious definitional problems over the last few decades has resulted in notable and expensive suits from various religious organizations for the right to be defined as an IRS church. The Church of Scientology, a very prominent example, sued the IRS when it was denied church status on grounds of significant commercial activity, claiming religious persecution. This litigation persisted for over a decade at taxpayers' expenses. *See Founding Church of Scientology v. the United States*, 412 F.2d. 1197, 1199 (1969).

definitions.[121] In addition, the advent of television ministries, such as the Billy Graham Hour, made the IRS church definition increasingly more arbitrary, archaic, and discriminatory.

In 2006, Congress passed the Pension Protection Act to combat widespread financial abuse of tax exempt status through increasing inflicting stricter regulations for noncompliance and evasion and increased rewards for whistleblowers.[122] In addition, the Act altered many reporting processes by reforming the I-990 reporting system in an attempt to catch asset hiding schemes.[123]

There were also some supplemental changes made to the I-990 reporting forms in 2008.[124] One of the first reforms in the 2008 Amendments were mandatory tax-exempt I-990 filings for tax exempt organizations with gross receipts of $25,000 or less. One of the main tax abuses that the IRS was trying to eliminate by passing this act were emerging tax exempt "subsidiaries" of companies in which a "parent" company would dump assets into the small subsidiary tax exempt organization, then claim the deduction as tax-exempt.[125] A parent company could then

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[121] These frustrations by religious organizations upset at their perceived abuse of government powers unconstitutionally imposing themselves upon religious belief were succinctly defined by a 1988 publication by the Presbyterian Church (U.S.A.). Leaders, angry that their ministries were denied "church" status (not presumably by tax exempt grounds, but by fundamental religious grounds), stated,

> When the state grants exemption from taxes to religious organizations, the basic definition of what constitutes religious activity must be made by those organizations. With increasing frequency, taxing jurisdictions seek to collect taxes from religious organizations on particular property or activity in the face of statutory provisions exempting "churches, conventions, or councils of churches and their integrated auxiliaries" from tax liability. In such instances, the justification is most often that the property or activity is not sufficiently "religious" to qualify, although wholly owned, operated, controlled, and defined by the religious organization as part of its life and work. We urge Presbyterians, when dealing with such situations, to recognize that the issue is not "whether the church should pay taxes." The issue is: "Who defines the church's nature and ministry?" Presbyterians must resist any attempt by taxing authorities to define some of the properties and activities wholly controlled and defined by the church as nonreligious…. We concede that some properties and operations of religious organizations may be subjected to taxation by legislative act; but we will resist all efforts to do so by administrative determination, in the face of statutes that exempt churches from taxation, that some properties or activities wholly controlled and operated by the church as part of its mission are "nonreligious."

This statement expressed growing church resentment for the government classification of some of their activities as nonreligious, while conceding that they were taxable. *See* "God Alone is the Lord of the Conscience," A Policy Statement Adopted by the 200th General Assembly (1988) (Louisville: Office of the General Assembly, The Presbyterian Church (U.S.A.), 1989), pp. 37-39.
Furthermore, most of these classifications are predicted to become obsolete in the next decade, given the rise of the trend of internet churches and multi-site campuses. *See* Marian Lietraud. "Churches: What's Changing and What's Not." Christianity Today, January 5, 2010.

[122] Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (codified as amended in scattered sections of 26 U.S.C. and 29 U.S.C.).

[123] Id.

[124] Id.

[125] Id.

potentially dump infinite amount of assets into infinite individual tax exempt organizations with gross receipts of $25,000 or less, and cheat the system by counting these "donations" as tax-deductible.[126]

Requiring all tax exempt organizations (regardless of gross receipts) to count these as deductibles would reduce the risk of tax evasion through infinite deductions to sham charitable organizations. Because the ultimate purpose of IRS charitable deductions is to increase philanthropic actions that contribute to the public good, rather than putting the money back into one's own pocket by creating bogus philanthropic organizations, a lack of reporting methods can create resentment and lessened incentive for honest reporting and payments by taxpayers who would have to pick up the tab for the difference.[127]

The 2006 Act required controlling organizations to report income to and from controlled organizations, as well as transfers to and from controlled organizations. It doubled the excise taxes for transferring funds from one organization to another. This preventative excise tax measure discourages illegal asset dumping.

Unrelated business income tax returns must be available for public inspection under the 2006 Act. Previously this was not required. This increased public transparency with tax exempt organizations, and reduced the incentive to use their tax exempt status as a cover for operating a for-profit, yet tax-exempt business on the side. While in the short term this might mean an increase in complexity, it reduces the risk of unscrupulous nonprofits claiming tax-exempt status to prevent their incomes from being taxable.

Pre-2006, noncash contributions (such as donations of valuable art), were not required to be on the Form I-990 or any addendum. The previous system left the potential problem of taxpayers "donating" valuables in the hopes of hiding major assets within tax exempt organizations. Conversely, the IRS also now reserved the right to deny as a deductible used clothing or other items that might have minimal monetary value (such as a threadbare K-mart t-shirt).[128] The 2006 Act also increased limitations on donated joint ownership of property.[129]

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[126] Id.

[127] *See*, Kenneth J. Kies, *The Obama Budget, 2019, and the Impending Fiscal Nuclear Winter*, 123 Tax Notes 601 (2009). Kies writes,

> From March 2008 to March 2009, annual deficits projected by the Congressional Budget Office from 2008 through 2018 increased by $6 trillion. First, federal receipts have fallen through the floor – income taxes in 2009 will raise roughly $550 billion less than previously expected. Second, expenditures have skyrocketed. In fiscal year 2009 alone, the government is projected to spend $838 billion more than was expected just 12 months ago. And, third, deficits caused by this huge mismatch in policy can no longer be mitigated with cash surpluses generated by the payroll tax.

[128] Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (codified as amended in scattered sections of 26 U.S.C. and 29 U.S.C.) [hereinafter Pension Protection Act of 2006].

[129] Id.

Because donations to churches are often in-kind, with the intention of redistribution to the needy (this is seen through clothing and food drives), it is important to have these reporting methods in place, because it is much more difficult for the government to track donated goods to extremely needy individuals who likely won't file income tax returns (like recipients of clothing or food drive items). Unfortunately, a lack of reporting methods leaves much room for abuse in hidden assets.[130]

Under the new 2006 reporting standards, charitable contributions by individuals must verified by official bank statements with the corresponding name of the charity on debit or credit transactions, copies of cashed checks written to the charity issued from the bank, or written confirmation from that tax exempt organization. Prior to 2006, acceptable methods of proof of charitable donations included individual private ledgers. The problem with these pre-2006 individual ledgers was that dishonest taxpayers could potentially claim a cash charitable deduction while using the cash for personal use, and there would be no neutral third party source required or available to back up the individual's personal ledger.[131]

Requiring individual donors to give official bank documentation or official tax exempt documentation reduced the amount of fraudulent charitable deductions because it gives individual charitable contributors less leeway to lie on their records and reduced the tax burdens on honest taxpayers footing the bill of the dishonesty of others.[132] The author of this article believes that requiring third party documentation is a good *general* practice that reduces the accounting burden on most tax exempt organizations and reduces the probability of natural human error in calculations, when the majority of transactions are large noncash transactions. Most modern banks have automatic financial statements that allow for debit card transactions available through PDF format,[133] to effectively streamline with the IRS's new PDF-based paperless addendum filing system.[134]

This may be more difficult with *specific* churches and religious organizations, however, and may thus not be the most optimal solution for these *specific* tax-exempt organizations, and may be a problematic constitutional barrier to reporting the I-990. Churches are and have been historically cash-based donation entities.[135] While many churches have modernized and allowed online giving that will allow automatic financial statements to generate with each

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[130] Id.
[131] Id.
[132] Id.
[133] Susan Clearly Morse, Stewart Karlinsky, & Joseph Bankman, Cash Businesses and Tax Evasion, 20 Stan. L. & Pol'y Rev. 37, 39-40 [hereinafter Morse, Cash Businesses]
[134] See Pension Protection Act of 2006, *supra* note 128.
[135] Morse, Cash Businesses, *supra* note 133.

online donation that occurs (and thus would enable reporting standards from the banks), not all have, and many still have a heavy reliance upon purely cash donations, and thus church employees are in the same high risk category as other cash-based income earners.[136]

A visit to most Sunday services will allow an observer to watch the "passing of the plate", into which parishioners will toss bills. For the cash donation based parishioners who *do* wish to have their deductions deducted, the entire reporting burden would fall upon the church (which, as a tax-exempt organization that relies upon donations, especially in this economy, may be significant).

One might argue that the largest median individual weekly cash donation will never exceed $20, the highest bill denominator, and that the average parishioner would therefore not likely attempt to make this a tax-deductible expense worthy of reporting, especially if he or she did not attend church often. One could also argue that to ease the reporting burden, churches ask parishioners to donate with checks (automatic bank statements will include copies of cashed checks). However, there may exist tithing tax-deduction seeking parishioners, especially Christian, who believe in making donations anonymously in front of other parishioners for religious reasons[137], and would likely decline this option, because of the names on the individual checks would identify themselves and the weekly amount donated. Infringing on this religious belief may be constitutionally impermissible, especially if a particular church does not have modern online donation capabilities that allow for alternative anonymous donation methods.[138]

The underlying *motive* of the independent third party based reporting system is to prevent fraud by cash donations using the methods discussed above. If there is little risk for fraud, then there should be no additional reporting burden, which becomes cumbersome on both ends at no gain. Therefore, the ideal reporting solution should allow for anonymous cash-based donations while decreasing the reporting costs on both sides.

Due to the religious based desire for anonymous giving,[139] coupled with the increase in checking fees, a more efficient way to implement the new cash reporting standards in churches would be to instate a *minimum* cash threshold of reporting. For example, if a parishioner can establish that he or she is a member of a certain

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[136] Id.

[137] The Christian notion of anonymous tithing can be summed in the following passage: "Be careful not to practice your righteousness in front of others to be seen by them. If you do, you will have no reward from your Father in heaven. So when you give to the needy, do not announce it with trumpets, as the hypocrites do in the synagogues and on the streets, to be honored by others. Truly I tell you, they have received their reward in full. But when you give to the needy, do not let your left hand know what your right hand is doing, so that your giving may be in secret. Then your Father, who sees what is done in secret, will reward you." Matthew 6:1-4.

[138] Ken Walker. "Missionary Money: Easier to Give, Worth Less than Ever." Christianity Today, October 25, 2011

[139] Matthew 6:1-4, *supra* note 137.

congregation (such as through a church-issued membership certificate), and has bank statements showing regular weekly withdrawals of a constant reasonable dollar amount (perhaps with a minimum threshold of nothing too large to fit into an offering plate, like $100), this should be suffice as reasonable external proof to the IRS for tax-deduction purposes. This reporting method would not violate First Amendment Establishment Clause rights to worship freely. If the weekly "too much cash to reasonably fit into an offering plate amount" threshold was breached, then an external proof should be established either through the individual's checking account or through the church (there should be no weekly cash donations over the median threshhold).

Pre-2006[140], there was little management over the flow of funds into donor foundations, which were separate funds that operated under a tax exempt organization umbrella. There was widespread mismanagement of these funds as individual donors asked the tax exempt organization to use their tax-deductible donations to flow back to the individual donors.[141] These abuses pulled income that otherwise would have been federally taxed directly back into the individual donor's pocket, at full benefit to the donor and no benefit to the tax exempt organization the donation purported to support.[142] These "double dipping" practices therefore were in direct opposition of the original intent of the tax-exempt structure.

This is one of the main reasons this paper argues for the mandatory reporting of the I-990 for churches. IRS Form I-990 requires tax-exempt organizations to publicly reveal the highest paid members of the tax exempt organization and how much they were getting paid.[143] Publicly revealing identities of governing church board members and revealing the top governing members' salaries *prevents* the protective umbrella of anonymity that otherwise would protect unscrupulous church leaders from shifting assets back and forth between umbrella organizations.[144] If they were flagged for an audit, the IRS could then compare these governing board members with individual bank statements' transactions.[145]

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[140] Pension Protection Act of 2006, *supra* note 128.
[141] Id.
[142] "Tax Guide to Churches and Religious Organizations," Publication 1828 (11-2009) Catalog Number 21096G U.S. Department of the Treasury, 2009.
[143] Id.
[144] Id.
[145] In 2009, the Department of Treasury issued the following statement:

> Starting in January 2011, organizations that process debit and credit card payments for merchants must annually report the amount of these payments to the recipient businesses and to the IRS. Treasury and IRS are actively working on the implementing regulations and soliciting input and feedback from taxpayers, banks, and credit card processers.

If all religious organizations were required to file the I-990, this new debit and credit processing regulation will make it easier to flag fraud when whistleblowers expose fiscally corrupt churches, because donors can use the

The above examination of American taxation history as it relates to tax exempt organizations reveals that the original attitudes towards income taxes at the time of the Framers was that taxation without representation (or apportionment) was unconstitutional. This was reflected in the United States Supreme Court's reasoning in *Pollock* where the Court opined that progressive income taxes without apportionment (taxation without representation) was *not* constitutional, because the constitutional framers never intended a complex tax structure, having recently escaped a system of what they viewed to be tyrannical rule through taxation without representation.[146]

Because of their aversion to a strong and arbitrary centralized tax structure, it is unlikely that the Framers would have forseen the First Amendment's Establishment Clause as connected with something as complex as the modern complex income tax structure, due to the 16th Amendment repealing many of their anti-progressive income tax values. If the Framers could not have forseen this apportionment requirement repealed by the 16th Amendment, then it is highly unlikely that they would have forseen the complexity of the income tax code with its countless taxation without representation provisions that followed it (and the subsequent demand for a special set of tax exempt rules for charities operating as small businesses).[147]

As the income tax structure for tax exempt organizations increased in complexity (mirroring the increasing complexity of the general federal income tax structure overall), loopholes were created over the decades to cheat the system,[148] resulting in which led to more legislation[149] and yet more loopholes to combat the newer legislation in the tax exempt structure.[150]

Good accounting and full disclosure principles that govern regular nonexempt organizations are applicable and necessary to churches as well, and churches' exemption of filing an I-990 is a vestigial misinterpretation of the First Amendment's Establishment Clause that a minority of churches abuse[151] at the expense of both parishioners[152] and honest tax filing church leaders.[153] Thus, requiring churches to file an I-990 would eliminate unnecessary

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external IRS source to compare the expenditures of the church with their donations. "Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance," U.S. Department of the Treasury, July 8, 2009.

[146] Miller, John C., Origins of the American Revolution. 1943. pp. 31, 99, 104

[147] *See*, Kenneth J. Kies, *The Obama Budget, 2019, and the Impending Fiscal Nuclear Winter,* 123 Tax Notes 601 (2009).

[148] Id.

[149] Id.

[150] Id.

[151] *See* Banned From Church, *supra* note 31.

[152] Id.

[153] Id.

complexity in the tax code. Furthermore, due to the discriminatory nature[154] of the I-990 filing exemption for churches as defined by the IRS, requiring IRS defined churches to annually file an I-990 may be *required* under First Amendment principles.

To fully understand the First Amendment's applicability to requiring churches to file a Form I-990, one must examine how the Supreme Court has historically interpreted the First Amendment as it applies to tax regulation of churches.

IV. FIRST AMENDMENT: PROTECTION FROM STATE IMPOSED RELIGION, NOT REGULATION

Because the historical resistance of churches to offer full cooperation with government imposed tax regulations (such as the I-990) is based on the First Amendment ideal of "separation of church and state," and because the First Amendment is part of the U.S. Constitution, the following section will first examine the origins and Framers' intent of the First Amendment's Establishment and Free Exercise Clauses. Then this section will examine the United States Supreme Court's interpretation of the constitutionality of the separation of church and state as it applies to the First Amendment's. Finally, this section will explain how the interpretation of the First Amendment relates to the constitutionality of imposing a requirement for all churches to file an I-990 in accordance with the tax reform ideals of the Pension Plan Act of 2006 in the historical context of prior tax reforms.

The origins of the First Amendment's Establishment and Free Exercise Clauses lie within the early American ideal of freedom from a state imposed religion. However, the ideal of complete separation of church and state was not a universally held early American value. Those who did not adhere to certain taxes and levies were punished, as were those who expressed views that were deemed heretical in nature. The Salem Witch Trials of Salem, Massachusetts[155] were a prominent example of such heretical based punishments.

Immediately before the Constitution was drafted, many of the colonies and states attempted to legislate the establishment of a religion.[156] In 1784, the House of Delegates attempted to pass a bill proposing the provision of Christian teachers for the teaching of the Christian religion.[157]

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[154] Whelan, "Church" in the Internal Revenue Code: The Definitional Problems, 45 Fordham L. Rev. 885
[155] In 1692 in Salem, Massachusetts, 19 individuals were hanged on Gallows Hill for suspected witchcraft. The chain of events that led to the infamous "witch hunt" began with a combination of abnormal behavior of two children combined with suspected voodoo practice of an old slave. 64 Tul. L. Rev. 187.
[156] *Reynolds v. the United States*, 98 U.S. 145, 166–67 (1879).
[157] Mark A. Belies, Religion and Republicanism in Jefferson's Virginia, 31-32 (1995).

This bill brought considerable resistance from prominent Constitutional Framers, most notably James Madison, who drafted that "religion is the duty we owe creator" and that it was not within the cognizance of the civil government.[158] Thomas Jefferson, noted Revolutionary who, despite being a religious man, was also adamant for the national codification of a *vertical* separation of church and state. This desire for national *lateral* separation of church and state is evident in his published papers upon leave in France upon the drafting of the Constitution.[159] Jefferson, a Baptist sympathizer who strongly opposed the persecution of Baptists by a strong Virginia State Anglican Church,[160] was fearful of the potential persecutory vertical effects of a centralized religiously biased government imposing mandatory religious sanctions upon their fellow Americans of a different sect.[161] Rather, Jefferson wished for all denominations to be able to worship freely.[162] However, Jefferson did not advocate for the *absolute* separation of *general* church practices from the government interference or promotion, as long as they did not advance or deny a particular *sect* the rights to worship free of persecution. This was evident when Jefferson approved the use of the United States Capitol Building for the use of church services in 1821.[163]

At the time of the Constitution's framing, individual *states* and *local authorities* were given the right to govern their religion. While the turn of the century, Massachusetts was the only state that had a statute imposing mandatory morning prayer in public schools, though there were many *local* authorities *within* other states who had similar policies.[164]

Since the framing of the Constitution, the ideal of "separation of church and state," has led many Americans to erroneously believe that the First Amendment entitles all exercise of religion to be free of any and all government interference, yet the United States Supreme Court has denied the legitimacy of this ideal repeatedly throughout early American history. One of the most prominent early examples was the case *Reynolds v. The United*

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[158] Semple's Virginia Baptists, Appendix.
[159] See Letter from Thomas Jefferson to the Members of the Baptist Church from Buck Mountain in Albemarle (April 13, 1809), in 16 THE WRITINGS OF THOMAS JEFFERSON at 363-364.
[160] Mark A. Belies, Religion and Republicanism in Jefferson's Virginia 31-32 (1995)
[161] From the early settlement of Rhode Island in the 1630s to the time of the Federal Constitution in the 1780s, the Baptists were often beaten and tyrannized. See Letter from Thomas Jefferson to the Members of the Baptist Church from Buck Mountain in Albemarle (April 13, 1809), in 16 THE WRITINGS OF THOMAS JEFFERSON at 363-364.
[162] See Letter from Thomas Jefferson to the Members of the Baptist Church from Buck Mountain in Albemarle (April 13, 1809), in 16 THE WRITINGS OF THOMAS JEFFERSON at 363-364.
[163] Id.
[164] By 1910, 11 more states joined Massachusetts in making prayers obligatory, thus codifying their local practices that were already in place, no state had ever codified an outright ban on these practices, though they did occasionally outlaw it by judicial order. *School District of Abington, Pennsylvania et. al. v. Schemp, et al*., 374 U.S. 203, 269-270 (1963).

States, in which the United States Supreme Court upheld that laws may interfere with practices of governmental actions, though they may not interfere with religious belief and opinions.[165] This case was significant because the *practice* in question, polygamy, was inextricably related to the religious *beliefs* of the defendant, who was Mormon.[166] The Court's reasoning in *Reynolds* was that interference with religious practice is permissible in cases in which the particular behavior of that practice is in violation of social duties and at odds with good order.[167]

The Court drew its conclusion from the common law traditions of England, from which the common law of the United States was forged, to justify their reasoning, stating that because polygamy was always deemed an abhorrent crime in England, the practice of polygamy was in violation of social duties and in odds with good order because it involved "innocent victims."[168]

So far this paper has established that the original *intent* behind the First Amendment's Establishment and Free Exercise Clauses was a result of inner turmoil and persecution of Christian sects and the concern of a persecutory, *vertical* government imposing a state religion that persecutes a minority Christian sect. Thus, the First Amendment's original purpose of the Establishment and Free Exercise Clauses was *not* intended to create a universal ban on all government regulation upon religious practices, nor was it intended to ban a complete separation of positive government promotion of religion, as long as this positive involvement did not favor one Christian sect over another.

The "no violation of social duties" and "innocent victims" *Reynolds* standard was the balancing standard for this government interference with religious practices in 1879, *before* the legalization of the progressive income tax,[169] the emergence of the tax-exempt organization,[170] and the modern day tax exempt IRS subclass of churches.[171] The *Reynolds* opinion also expressed the early American Anglo-centric, Christian[172] preference of this structure over time in relation to the English common law as the only possible *external* international source of law from which inspiration of the First Amendment's applicability could be derived. Since *Reynolds*, many of the churches that have provoked outrage over perceived abuses have been those publicly condemned by mainstream America as

[165] *Reynolds v. the United States*, 98 U.S. 145, 166–67 (1879)
[166] Id.
[167] I Id.
[168] Id.
[169] *Flint v. Stone Tracy Co., supra* note 67.
[170] H.R. Rep. No. 871, 78th Congr., 1st Sess. 24-25 (1943).
[171] Id.
[172] *Reynolds v. the United States*, *supra* note 165.

aberrant cults[173] in violation of social duties[174] or financially exploitative churches[175] undeserving of the same tax exempt status because their activities create "innocent victims."

But what is appropriate *modern* balancing standard for exercise of personal belief and government "interference" upon actions that exercise that personal belief to prevent "innocent victims," especially given an increasingly complex tax exempt structure that now includes religious organizations that (unlike those of the Founders' days) are not of a traditional Judeo-Christian structure?[176] More specifically, how would such a balance apply to tax legislation imposing mandatory I-990 disclosure upon churches as defined by the IRS? Who would be the "innocent victims" if the "right to interference" to if churches are *not* required to file the I-990? How has this "right to interference" changed over time along with the evolving income tax code?

There are two balancing tests this paper will explore in whether or not it is constitutionally permissive *and* required to have churches file the I-990. The first is the 1982 Supreme Court case *Larson v. Valente*, which established that tax laws that favor some sects over others (like the requirement to file an I-990 that favors some religious sects over others based on outdated, nebulous IRS definition of "church") violates the First Amendment and thus should be repealed.[177] The second is *Lemon v. Kurtzman*,[178] which followed outlined a 3 prong test for establishing First Amendment constitutionality of imposing government regulations on church practices in applying a universal law that (such as imposing a new IRS regulation to require *all* religious organizations to file an I-990).[179]

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[173] *See United States v. Ballard*, 322 U.S. 78, 78 (1944). In *Ballard*, a tax exempt revocation case in which the Supreme Court held that evidence had been properly withheld in regards to the proving the "truth" of the unpopular religious organization's core beliefs, which included that the founder personally shook hands with Jesus Christ. Id.
[174] *See Snyder v. Phelps*, 580 F.3d 206, 209 (2009), where family of killed veteran unsuccessfully sued church for inciting anti-military and anti-Catholic protests at their son's funeral. The Court in this case cited First Amendment right to assemble and free speech rights for their decision, stating, "judges defending the Constitution "must sometimes share [their] foxhole with scoundrels of every sort, but to abandon the post because of the poor company is to sell freedom cheaply. It is a fair summary of history to say that the safeguards of liberty have often been forged in controversies involving not very nice people." Id.
[175] *See Worldwide Church of God, Inc. v. California*, 449 U.S. 900, 904 (1980).
[176] For example, many of these criteria are irrelevant for many First Amendment protected Buddhist sects, which are religious but do not have a defined number of body of believers and encourage individual meditation sessions rather than regularly scheduled worship meetings. *See* Winston, Diana. Wide Awake: a Buddhism Guide for Teens. 31, 2003.
[177] *Larson, Commissioner of Securities, Minnesota Department of Commerce, et al v. Valente, et. al*. 456 U.S. 228, 229 (1981).
[178] *Lemon, et. al, v. Kurtzman, Superintendent of Public Instruction of Pennsylvania, et. al.* 403 U.S. 602, 605 (1971), [hereinafter *Lemon, et. al, v. Kurtzman*].
[179] Id.

The best test to use to evaluate the constitutionality of the current IRS I-990 exemption for IRS-defined churches is *Larson v. Valente*.[180] In *Larson*, church plaintiffs challenged the constitutionality of a tax reporting statute that arbitrarily discriminated against some religious sects based on a 50 percent membership revenues contribution.[181] While the lower courts used the three pronged *Lemon* test (to be discussed in the next section of this paper) to determine the constitutionality of this legislation, the *Larson* Court reasoned that because the *Lemon* test was used primarily in cases where the legislation in question would apply uniform benefit across *all* religions, it was not the best balancing test in cases where legislation would *discriminate* against all religions.[182] The Supreme Court ruled in favor of the plaintiffs.[183] Thus, *Larson* Court created the following test for determining the constitutionality of discriminatory tax laws: if tax legislation discriminates against religious sects in a way that the challenged rule does not serve any compelling state interest purpose, then the legislation is unconstitutional.[184]

The current tax legislation that does not require churches defined by the IRS as churches to report an I-990 is similar to the fact patterns *Larson* case because the IRS definition of church discriminates against some religious denominations through an outdated and arbitrary definitional model using their fourteen criteria guidelines. The problem with these criteria is that they are vague in both definition (how often does a congregation to meet to have "regular religious services?") and application (both the IRS and the U.S. Supreme Court have stated that not all criteria need to be met to qualify as a church for tax purposes, and that these fourteen criteria are mainly guidelines, perhaps to acknowledge that a strict definition of religion may be in and of itself a violation of the Establishment Clause[185]). Even with the vagueness of these guidelines that are designed to encompass all religions equally, by definition some are designed to exclude certain sects and religious organizations.[186] Furthermore, most religious organizations denied church status for IRS purposes are *not* denied on the basis of these fourteen criteria, but rather because the church's activities resemble that of a commercial activity or that the church was engaging in political activity, further undermining the usefulness of these criteria for the state.[187] Rather, the current tax legislation

[180] Id.
[181] Id.
[182] Id.
[183] Id.
[184] Id.
[185] *See American Guidance Foundation, Inc. v United States*, 490 F. Supp. 304, 306 (D.D.C. 1980).
[186] Many of these criteria are inapplicable to some religious organizations and sects, such as most televangelist and internet ministries (no established place of worship or regular congregants) and certain Buddhist sects (no established worship services). *See* Whelan, "Church" in the Internal Revenue Code: The Definitional Problems, 45 Fordham L. Rev. 885 (1980).
[187] *See Founding Church of Scientology v. the United States*, 412 F.2d. 1197, 1198 (1969).

providing exemption of I-990 filing only serves to further complicate an already overwhelmingly complex income tax code[188] and increase the opportunities for fraud by arbitrarily lowering the standard of accountability for a favored subset of religious groups.[189] Therefore, because it has no demonstrated useful state purpose, the current discriminatory and nebulous IRS church definition criteria fails the *Larson* test and is therefore unconstitutional.

A three pronged constitutionality test of tax laws was further defined by the 1971 Supreme Court case *Lemon v. Kurtzman,* which created a test that can be used today in determining whether requiring churches to file an I-990 is constitutionally permissive.[190] In light of the recent controversial rulings since 2005, and absent the outcome of a pending Supreme Court appeals case to further clarify the *Lemon* test,[191] this paper will use the classic *Lemon* "endorsement" test as the standard of review because that has been the typical standard of review in tax court constitutionality cases since the 1971 *Lemon* ruling.

In *Lemon,* plaintiffs challenged the constitutionality of a state statute enabling state funded secular teaching materials sent to private religious schools.[192] The *Lemon* Court established a three prong test for the First Amendment constitutionality of legislation regarding government legislation regulating religious practices.[193] The first *Lemon* prong is that the government action must have a secular legislative purpose.[194] The second prong is that the government's action must not have the primary effect of advancing or inhibiting religion.[195] The third prong is that the government's action must not result in excessive entanglement with religion.[196] The first prong, the *Lemon* Court reasoned, was met because the secular legislative purpose of the statute was to provide children with secular

[188] *See* "Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance," U.S. Department of the Treasury, July 8, 2009.
[189] *See* Liatraud, Marian. "What's Changing, What's Not." Christianity Today, January 25, 2010.
[190] *Lemon, et. al, v. Kurtzman, supra* note 178.
[191] The relative makeup of the current court is similar to that of the *McCreary* Court, with current conservative Justices Alito, Roberts, Thomas, Breyer, and Scalia unlikely to waver in favoring the 6th Circuit's ruling in any future cases that may appear before the Court. While Obama appointee Justice Kagan was a hopeful for strict separationists, her conservative Jewish background will likely impede her from upholding the 6th Circuit's ruling should the issue ever arise again in the near future, as well as the fact that Kagan might not qualify to sit for the ruling, given her tenure at the Office of the Solicitor General that will create a conflict of interest in many cases. Thus, with a religiously sympathetic majority holding the Court, the likelihood that the Court would create an alternate test for the *Lemon* test in the near future is highly unlikely. This is evident in the fact that the new Court denied cert to *McCreary* in February 2011. http://www.supremecourt.gov/Search.aspx?FileName=/docketfiles/10-566.htm (November 28, 2011 6:00 P.M.
[192] *Lemon, et. al, v. Kurtzman, supra* note 178.
[193] Id.
[194] Id.
[195] Id.
[196] Id.

statewide learning materials.[197] Under the statute, any teacher who received supplementary income was prohibited from teaching religious subjects as long as he or she received that supplementary income[198].

The Court ruled that the second prong was met because the secular materials in and of themselves did not promote or inhibit religion. However ruled the third prong was not met.[199] The Court reasoned that under the school program, a "comprehensive, discriminating, and continuing state surveillance [would] inevitably be required to ensure that [restrictions against teaching religious doctrine were] obeyed and that the First Amendment otherwise respected." This would in turn create "an excessive and enduring entanglement between state and church." The program would result in an unconstitutional "intimate and continuing relationship between church and state," since state officials could inspect books of church schools and determine which expenditures were religious and which were secular.[200]

Many constitutional law scholars, like scholar Leonard Levy, have long criticized the test as being too broad, too subjective, and too inconsistent, accusing judges of using the test to justify their support for or opposition to particular aid programs.[201] In addition, the *Lemon* test has undergone considerable scrutiny since 2005.[202]

In the landmark 2005 case *McCreary County, Kentucky v. ACLU of Kentucky*, plaintiffs challenged the constitutionality of a public display of the Ten Commandments at a courthouse.[203] The *McCreary* Supreme Court ruled that because Ten Commandments stood alone in the courthouse, it was unconstitutional because it promoted the Judeo-Christian faith.[204] Soon after, the McCreary County Courthouse added other displays (including the Declaration of Independence) to the Ten Commandments to supplement it as a secular historical display. However, upon appeal, the 6th Circuit Court ruled the display unconstitutional because all of the historical display items (such as the Declaration of Independence) had the word "God" inscribed upon them.[205]

In *Van Orden v. Perry*, which was ruled on the same day, as *McCreary*, the United States Supreme Court ruled in a 5-4 decision that a similar display, a Ten Commandments monument on the Capitol of Texas among other

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[197] Id.
[198] Id.
[199] Id.
[200] Id.
[201] See Levy, Leonard W. The Establishment Clause: Religion and the First Amendment (2d. ed. Rev., Chapel Hill: The University of North Carolina Press 1994)
[202] See *McCreary County, Kentucky v. ACLU of Kentucky*, 545 U.S. 844 (2005).
[203] Id.
[204] Id.
[205] Id.

monuments and historical markers, was constitutional because among other factors, it did not stand alone and the plaintiff waited 40 years to file suit (unlike the plaintiff in *McCreary*, who filed the suit soon after the monument was constructed).[206] The "swing vote" in both *McCreary* and *Van Orden* was Justice Stephen Breyer, who concluded that a combination of the long history of the Ten Commandments monument's 40 year presence on Texas grounds, its donation by an interfaith committee, and the presence of other nonreligious monuments surrounding the Ten Commandments monument made the display constitutional."[207]

Many courts and scholars believe that their perceived inconsistencies since 2005 are grounds for the abolition of *Lemon* test. This is evident in the words of Justice Scalia, who said, "I join in the opinion of the Chief Justice because I think it accurately reflects our current Establishment Clause jurisprudence we currently apply some of the time."[208]

However, neither the *Van Orden* nor the *McCreary* rulings clarified or created further boundaries in the *Lemon* test. Rather, the Supreme Court still deems this test valid, despite warnings from Justice Clarence Thomas that the Court needs to "clean up the mess" they created in 2005.[209] Perhaps in response to growing pressure from Justice Thomas, the Supreme Court accepted briefs for certiorari for *McCreary* in 2011.[210] In their brief, petitioners on behalf of McCreary pleaded the Court to reconsider the 6th Circuit's decision for several reasons. The first reason was that the 6th Circuit failed to clarify why the modified Ten Commandments display did not meet the Lemon standards, thus leaving petitioners with no course of action but to remove the display completely.[211] Petitioners sought clarification on this matter, urging that despite respondent's brief stating otherwise, that past displays do not "forever taint" that display.[212] The second reason was a more general need to clarify the confusion that the 6th Circuit's decision caused upon the intra circuit and inter-circuit conflicts.[213] The third (and related to the second) was that *stare decisis* should not be used to perpetuate an "inconsistent, unprincipled analysis spawned by the

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[206] See *Van Orden v. Perry*, 545 U.S. 677, 678 (2005)
[207] Id.
[208] See Van Orden, *supra* note 206.
[209] See *Utah Highway Patrol Association v. American Atheists*, 565 U.S. ___ (2011), in which the United States Supreme Court denied certiorari to plaintiffs whose lower courts used the Lemon test to determine the constitutionality of displaying crosses to honor slain Highway Patrol officers at roadside memorial sites.
[210] See *McCreary County v. ACLU of Kentucky*, 2010 U.S. Briefs 566, 9 (U.S. Jan. 10, 2011), *cert. denied* (February 11, 2011).
[211] Id.
[212] Id.
[213] Id.

continuing usage of *Lemon*.[214] Thus, the brief called for a new test to supplant the *Lemon* test, to bring more clarification. The Court denied *certiori* without publishing reasons for denial.[215]

In the wake of the 2005 Supreme Court rulings, there has been the clamoring of some proponents of abandoning *Lemon* altogether, as apparent in the unsuccessful bid for *certiori* in the *McCreary* case.[216] However, abandoning the *Lemon* test altogether without a replacement binding Supreme Court alternative test would be a bad policy decision for two reasons.

The first reason that abandoning the *Lemon* test is a bad policy decision is that upon remand, the 6th Circuit's upholding that *McCreary's* Ten Commandments display as unconstitutional (despite an altered historical display including secular materials) is not binding precedent over the ruling in *Van Orden*, which ruled that additional secular display items would render an identical religious display in a public setting constitutional.[217] Rather, the 6th Circuit ruled that the additional display items were not sufficient enough to render the display secular, without including in their opinion why these additional display items were not sufficient, nor what remedy the Kentucky courthouse petitioners had to make these additional display items sufficient to make them constitutional. Id. Without including a remedy for constitutionality, *McCreary's* 6th Circuit Court failed to address the vital redressibility factor that is required to bring a suit into court, rendering their decision useless as a precedent.[218] The *McCreary* case was granted review for certiorari in 2011, but was denied, though the opinion was not published.[219]

The second reason that abandoning the *Lemon* test altogether without a binding alternative is that virtually all jurisprudence, given enough cases, will have borderline cases like Van Orden that may be interpreted as inconsistencies if put together side by side (and in the case of *McCreary*, far out of context due to judicial creativity in the 6th Circuit's second ruling).

The fact that borderline cases inevitably exist does not mean that laws should be abandoned, especially without a binding precedent alternate test, else laws and the existing lawmaking process themselves become meaningless.[220] Without a reasonable alternate test, allowing creative interpretation of the *Lemon* test based on nonbinding precedent

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[214] Id.
[215] Id.
[216] Id.
[217] See *Van Orden*, supra note 206.
[218] See *Lujan v. Defenders of Wildlife*, 504 U.S. at 562 (1992).
[219] Id.
[220] See *ACLU Neb. Foundation v. Plattsmouth*, 419 F. 3d 772, 778 (CA8 2005)(*en banc*)("taking our cue from Chief Justice Rehnquist's opinion for the Court and Justice Breyer's concurring opinion in *Van Orden* "establishes an 'exception' to the *Lemon* test in certain "borderline cases.").

cases of creative interpretation or abandoning it altogether has served only to obfuscate the law. Thus, to apply post-2005 *Lemon* rulings (that are nonbinding derivations from the 6th Circuit's nebulous ruling) to tax law in particular would serve only to further add to the IRC's increasingly enormous complexities as it has to non tax related post-2005 *Lemon* cases. This concern of convolution in the absence of a reasonable alternative was manifest the fact that despite the borderline cases of *McCreary* and *Van Orden* (in which each Court voiced their concerns regarding the *Lemon* test's shortcomings), neither Court's majority opted to abandon the *Lemon* test altogether in favor of an alternative.[221]

Therefore, this paper's analysis will use the Lemon test, as have numerous courts have continued to use the *Lemon* test since the 2005 *McCreary* and *Van Orden* rulings.[222]

V. LEGISLATION REQUIRIING ALL CHURCHES TO FILE AN I-990 MEETS THE LEMON TEST

New legislation (government action) requiring churches to file an I-990 would meet the *Lemon* test. Under the first prong of the *Lemon* test, the government action has a *secular* legislative purpose, thus meeting the first prong. The proposed main *secular* legislative purpose of requiring financial disclosure is to lessen violations of the no private inurement requirements of 501(c)(3) organizations.[223]

Requiring all tax exempt organizations to file an I-990 does not have the primary effect of advancing or inhibiting religion, thus meeting the second prong. This is inherent in the fact that religious organizations not defined as churches by the IRS are currently required to file Form I-990 if they do not meet the threshold of proof required to file as a church under IRS standards, even if belief structure was virtually identical. This is especially relevant in the present economy, in which church alliances may be key in ensuring the survival of financially struggling churches.[224] One might argue that because the additional I-990 filing requirement may impose a minimal

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[221] See *American Civil Liberties Union of Ohio Foundation Inc. v. DeWeese*, 633 F. 3d 424, 431 (CA6 2011)(applying *Lemon*); *Green v. Haskell Cty. Bd. Of Comm'rs*, 568 F. 3d 784, 797-798, Skoros v. New York, 437 F. 3d 1, 13 (CA2 2006)(stating, "the *Lemon* test has been much criticized over its 25 year history. Nevertheless, the Supreme Court has never specifically disavowed *Lemon's* analytical framework…. Accordingly, we apply *Lemon*." (citations omitted)); *American Civil Liberties Union of Ky. v. Mercer Cty*., 432 F. 3d 624, 636 (CA6 2005)("Because *McCreary County* and *Van Orden* do not instruct otherwise, we must continue to apply *Lemon*, including the endorsement test").

[222] See *Skoros*, *supra* note 221. *See ACLU Neb. Foundation v. Plattsmouth*, 419 F. 3d 772, 778 (CA8 2005)(*en banc*)("taking our cue from Chief Justice Rehnquist's opinion for the Court and Justice Breyer's concurring opinion in Van Orden "establishes an 'exception' to the Lemon test in certain "borderline cases.").

[223] Because the no private inurement requirements apply to both religious and nonreligious tax exempt organizations under 501(c)(3), this requirement is secular. *See* "Tax Guide to Churches and Religious Organizations," Publication 1828 (11-2009) Catalog Number 21096G U.S. Department of the Treasury, 2009.

[224] See Liatraud, Marian. "What's Changing, What's Not." Christianity Today, January 25, 2010.

additional reporting burden at an increased cost to the religious organization, it unconstitutionally impedes religion.[225]

However, the 1998 case *Adams v. Commissioner* established the rule that "the Supreme Court has established that uniform, mandatory participation in the federal income tax system, irrespective of religious belief, is a compelling governmental interest", even if it impedes personal religious beliefs.[226] In *Adams*, plaintiff, a Quaker, sought an injunction against paying federal income tax because her personal pacifist beliefs precluded her from funding the United States military.[227] The court ruled against the plaintiff reasoned that the tax system could not function if denominations were allowed to challenge the tax system because tax payments were spent in a manner that violates their religious belief.[228] Because the broad public interest in maintaining a sound tax system is of such high order, religious belief in conflict with the payment of taxes affords no basis for resisting the tax.[229] Imposing a uniform system of I-990 reporting would likewise be uniform across all religious organizations attempting to claim tax exemption, and a lack of such a uniform requirement ultimately only serves to further obfuscate an already massively complex tax structure based on arbitrary, laxly enforced, and increasingly obsolete denominational differences based on the traditional Judeo-Christian church model.[230] Therefore, despite the additional minimal annual reporting requirement, this proposed new system would neither advance nor inhibit religion, thus passing the second *Lemon* prong.

The proposed requirement for all religious organizations to file the I-990 would not result in excessive entanglement with religion, thus meeting the third *Lemon* prong. While some might argue that the requirement of an annual return would result in a similar unconstitutionally impermissible “excessive and enduring entanglement” with church and state, this concern is moot. Requiring churches to file an I-990 might be viewed as excessive because it require detailed financial information about the church’s management structure reported to the IRS. It might be viewed as too enduring because imposing such a requirement would be annually mandatory.

Mandatory church filings of the Form I-990 is distinguishable from excessive and enduring state “entanglement” described in *Lemon*, and is therefore constitutional for three reasons. First, there is a reasonable limit

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[225] “Tax Guide to Churches and Religious Organizations,” Publication 1828 (11-2009) Catalog Number 21096G U.S. Department of the Treasury, 2009.
[226] *Adams v. Commissioner*, 110 T.C. 137, 139 (T.C. 1998).
[227] Id.
[228] Id.
[229] Id.
[230] *As cited* in *Lutheran Social Serv. of Minn. v. United States*, 758 F.2d 1283, 1286-87 (8th Cir. 1985).

to the amount of information reporting necessary to assess whether or not churches are filing in accordance with their tax exempt status requirements.[231] Second, unlike the statute in *Lemon*, which would potentially have required constant surveillance of the classroom practices to ensure that subsidized religious teachers were purely secular in their teaching approaches,[232] the proposed mandatory church I-990 information filings would only be required once a year. Finally, the high risk reporting nature of church funds makes the governmental interest overriding. An applicable "overriding governmental interest" in view of high risks precedent for the third *Lemon* prong is the 1983 ruling in *Lawrence v. Commissioner*, in which the court ruled investigating the tax income of a high risk taxpayer (who claimed that reporting was against his religious beliefs) was constitutional, given an overriding government interest in ensuring that high risk taxpayers pay the correct taxes due.[233] Like the plaintiff in *Lawrence*, churches are high-risk taxpayers,[234] due to their heavy cash based donation structure,[235] as discussed earlier. Therefore, due to this high risk of church abuse, uniform tax reporting procedures for all religious organizations is not excessive entanglement with religion.[236]

VI. SOLUTION: ELIMINATE "CHURCH" AND "AUXILIARY OF CHURCHES" DEFINITIONS.

In conclusion, the nebulous IRS definition of churches that exempts them from the I-990 reporting burden was unconstitutionally impermissible from its inception due to its impermissible exclusivity of churches that did not fall into the stereotypical Judeo-Christian model. The nebulous nature of these fourteen church definitional criteria, combined with the incredibly complex revenue code to accommodate the great diversity of different church structures, has only served to further complicate an already complex progressive income tax structure that led to the heavily resisted "auxiliary of churches" definition. The current progression of modern churches towards internet based and multi-site ministries have rendered most of the current IRS church definitional criteria obsolete. The obsolete church definitional criteria based on the traditional Judeo-Christian church model will likely exclude the majority of current Judeo-Christian churches in the coming decades, especially given the progression towards the multi-site and internet church based models. This obsolete nebulous church definitional criteria based on the traditional Judeo-Christian church also excludes certain sects that are not Judeo-Christian in origin.

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[231] *Lemon, et. al, v. Kurtzman*, *supra* note 178 at 624-625
[232] Id. at 621
[233] *Lawrence v. Commissioner*, T.C. Memo 1983-497 (1982)[hereinafter *Lawrence v. Commissioner*].
[234] Id.
[235] Morse, Cash Businesses, *supra* note 133.
[236] *Lawrence v. Commissioner*, *supra* note 233.

The IRS has two potential constitutional solutions to reform the unconstitutional and outdated *status quo* of the absence of I-990 church filing requirements. The first option is to modify these fourteen criteria to accommodate emerging trends in church structures. However, this "solution" will likely only serve to further complicate an already complex code and potentially exclude sects that still operate under the traditional Judeo-Christian church model. This first solution would also potentially invite a time consuming and costly legislation process from different conflicting sects on the legitimate definition of church (as it has happened over the years).[237]

The second solution is to simply eliminate the IRS church definition and require all tax exempt religious organizations to file the I-990. This would be the more efficient and less costly route because it would likely involve costly litigation only from a minority of churches who are behaving fiscally dishonest. Any litigation or resistance stemming from churches resisting full disclosure will help differentiate honest church leadership from dishonest church leadership. This differentiation will hopefully lead to less waste of tax exempt donor dollars, as churchgoers will avoid churches with dishonest reputations.

[237] *See Founding Church of Scientology v. the United States,* 412 F.2d. 1197, 1199 (1969).