

ABANDONING PROPERTY TAXES ASSESSED ON FALLOW NONPROFIT PROPERTY

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Financial distress has led to a rise in the shuttering of tax-exempt property owned by nonprofit organizations. Typically, nonprofits are not subject to property taxes if they use their properties for charitable purposes. Because these now-fallow properties are no longer being used, a debate has emerged over whether to assess them a property tax. On one side of the debate are those who argue for a strict construction of “charitable use”—one that would exclude non-fallow properties from exemption. Proponents of this construction argue that fallow nonprofit property should be taxed to share the burden of cash-strapped local governments. On the other side of the debate are those who argue for a broad construction of “charitable use”—one that reflects the purposes of nonprofit tax exemptions by excluding fallow nonprofit property from taxation. Proponents of the broad exemption argue that taxing these properties only serves to further strain financially troubled nonprofits, leading to fewer services for the people these nonprofits serve, and in turn placing greater demand on the government. Further complicating the issue is the diverse construction of tax exemptions across the fifty states. This Note examines the varying constructions and purposes of property tax exemptions for nonprofits. The Note concludes by suggesting a simple, more uniform system of taxing nonprofit property under the broad construction of “charitable use” so that fallow nonprofit property remains exempt. This approach would best serve the purposes of nonprofit tax exemptions and the people nonprofits serve.

I. INTRODUCTION

“I’m worth 20 million,” was the reply of John J. Geoghan, a convicted child molester and priest, to the fellow inmate who accused him of bankrupting the Roman Catholic Archdiocese of Boston and later strangled Geoghan behind bars.¹ The murderer explained that the priest was “arrogant” in claiming he was worth more than the \$10 million that the

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1. *Inmate Testifies Why He Killed Molester Priest*, N.Y. TIMES, Jan. 24, 2006, at A17.

Archdiocese of Boston paid in settling lawsuits stemming from Geoghan's molestation charges.²

Unfortunately, Geoghan was not the only priest that cost the Catholic Church millions in court costs and settlements.³ Although the exact number will never be known,⁴ the clerical abuse scandals across the United States forced the Catholic Church to pay more than \$400 million by 1992,⁵ and it is estimated that more than \$1.5 billion was paid in settlements by 2006.⁶ These settlements, coupled with the steady decline in donations resulting from both incriminating press⁷ and the 2008 economic recession⁸ have threatened the Catholic dioceses of several major cities with financial collapse.⁹ In hopes of controlling spending, many U.S. dioceses have cut social service programs, mortgaged property, and sold some real estate holdings.¹⁰ They have also begun closing churches and

2. *Id.*

3. See, e.g., Manya A. Brachear, *\$1.2 Million Deal for Priest Abuse*, CHI. TRIB., Dec. 18, 2008, at 33 (announcing the Catholic Archdiocese of Chicago's settlement agreement with a teenage boy and his mother); Tony Perry & Paloma Esquivel, *Priest Abuse Files Are Released*, L.A. TIMES, Oct. 25, 2010, at AA ("[T]he years of sexual abuse by Catholic priests in the San Diego Diocese . . . led to a \$198.1-million settlement with 144 victims in September 2007."); Sam Hemingway, *Vermont Roman Catholic Diocese, Priest Abuse Victims Reach \$17.65 Million Settlement*, BURLINGTON FREE PRESS (May 14, 2010, 2:25 PM), <http://www.burlingtonfreepress.com/article/20100514/NEWS02/100513034/Vermont-Roman-Catholic-diocese-priest-abuse-victims-reach-17-65-million-settlement> ("In addition to the \$17.65 million paid to the 26 [abuse] victims, the diocese agreed to pay undisclosed amounts of money to settle the cases of three other former altar boys who won large damage awards at trial.")

4. See INVESTIGATIVE STAFF OF THE BOS. GLOBE, BETRAYAL: THE CRISIS IN THE CATHOLIC CHURCH x-xi (2002) [hereinafter BOS. GLOBE STAFF, BETRAYAL] (explaining that many abuse claims are settled in private and have no public record).

5. JASON BERRY, LEAD US NOT INTO TEMPTATION: CATHOLIC PRIESTS AND THE SEXUAL ABUSE OF CHILDREN ix (2000).

6. ROBIN E. CLARK ET AL., THE ENCYCLOPEDIA OF CHILD ABUSE 83 (3d ed. 2007).

7. See Michael Paulson, *Refocused Church Seeking Donations*, BOS. GLOBE, Dec. 22, 2002, at A1.

8. See Tom Benning, *Slump Strains Church Finances As Need Grows*, WALL ST. J., Aug. 11, 2009, at A13. The recession has also caused church members' requests for financial support to increase as the number of those able to donate has decreased. *Id.* Thus, across the United States, "congregations of all sizes and denominations are struggling with issues of faith and finance as the recession grinds on." *Id.*

9. See Jo Renee Formicola, *The Further Legal Consequences of Catholic Clerical Sexual Abuse*, 49 J. CHURCH & STATE 445, 446, 457 (2007) ("[N]umerous civil lawsuits have created serious financial burdens for some Catholic dioceses, resulting in bankruptcy proceedings, and leading to legal questions . . ."); Kathleen Burge, *Chancellor Details Money Crunch: In Testimony, He Describes Bleak Archdiocese Picture*, BOS. GLOBE, Aug. 6, 2002, at B2 ("The archdiocese is already using the borrowed money to pay for its daily operations . . ."); Thomas Farragher & Michael Rezendes, *Law Given Authority to Seek Ch. 11: No Final Decision; Outside Backing for Cardinal Wanes*, BOS. GLOBE, Dec. 5, 2002, at A1 (announcing the authorization by a church finance council for the Archdiocese of Boston to seek bankruptcy protection); Michael Paulson, *Lennon Finds a Financial Squeeze: Unpopular Cuts Due Within Weeks*, BOS. GLOBE., Jan. 30, 2003, at A1 (declaring that the Catholic Archdiocese of Boston is in financial duress and announcing the Bishop's proposed remedies); Marc Gellman, Editorial, *Joe the Congregant: How the Financial Crisis Is Affecting America's Churches*, NEWSWEEK: THE DAILY BEAST, (Oct. 23, 2008, 8:00 PM), available at <http://www.thedailybeast.com/newsweek/2008/10/23/joe-the-congregant.html> ("Bad times for the economy, means bad times for [the churches].").

10. See, e.g., *Spotlight Investigation, Abuse in the Catholic Church: The Financial Cost*, BOS. GLOBE, <http://www.boston.com/globe/spotlight/abuse/cost> (last visited Nov. 1, 2011).

schools¹¹ that once charitably served their communities.¹² The economic downturn has also negatively affected hospitals,¹³ colleges,¹⁴ and museums.¹⁵ As these nonprofits lose donors, they continue to “have a fiduciary obligation to make the best use of their limited assets, and sometimes they must make the difficult decision to close facilities.”¹⁶

The increasing number of fallow nonprofit property has sparked a tax debate as cash-strapped towns have begun to tax the shuttered buildings of their charities—properties previously exempt from local taxes.¹⁷ The debate has gained national attention in Boston, the epicenter of the priest abuse scandal.¹⁸ Here, “[n]ine cities and towns have forced the Roman Catholic Archdiocese of Boston to pay property taxes on closed churches, schools, convents, and parish halls.”¹⁹ The Archdiocese’s tax assessment has divided the Boston community on matters of tax policy, leaving tens of thousands of dollars in dispute.²⁰ This division has been repeated throughout the country.²¹

Supporters of the tax argue that closed buildings are no longer tax exempt because the charity is not using them.²² They see the properties

11. See, e.g., Kathy McCabe, *Sadness Grips Closed Churches, but Some Gear for Appeals*, BOS. GLOBE, May 30, 2004, at No1; Rose French, *Archdiocese to Close 20 Churches, Merge Others*, STAR TRIB. (Oct. 16, 2010, 9:16 AM), <http://www.startribune.com/lifestyle/105086499.html?page=all&prepage=1&c=y#continue>; *50th Parish Closing in Cleveland Catholic Church Downsizing Blamed on Money, Attendance Woes*, FOXNEWS (June 30, 2010), <http://www.foxnews.com/us/2010/06/30/th-parish-close-cleveland-catholic-church-downsizing-blamed-money-attendance/>. See also Press Release, Nat’l Catholic Educ. Ass’n, *Statistical Report on Nation’s Catholic Schools Released* (June 30, 2009), available at http://www.ncea.org/news/pressrelease/article.asp?ARTICLE_ID=256& (outlining the decline in Catholic school enrollment and Catholic school closings).

12. See Catharine Pierce Wells, *Churches, Charities, and Corrective Justice: Making Churches Pay for the Sins of Their Clergy*, 44 B.C. L. REV. 1201, 1202–03 (2003).

13. See Jacob Goldstein, *The Financial Crisis Takes a Toll on Hospitals*, WALL ST. J. HEALTH BLOG (Oct. 1, 2008, 5:13 PM), <http://blogs.wsj.com/health/2008/10/01/the-financial-crisis-takes-a-toll-on-hospitals>.

14. See *College Closings Rare, but Could Rise in Turmoil*, EDUCATION ON MSNBC.COM (Nov. 16, 2008, 1:55 PM), <http://www.msnbc.msn.com/id/27752660>.

15. See Claude Solnik, *For Museums, Financial Crisis Is Not a Pretty Picture*, LONG ISLAND BUS. NEWS (Mar. 27, 2009), <http://libn.com/2009/03/27/for-museums-the-financial-crisis-is-not-a-pretty-picture>.

16. Kevin Kearns et al., *The Charitable Property Tax-Exemption Debate: The Financial Crisis Has Affected Public-Sector and Nonprofit Relations in One City, Which Has Taken an Age-Old Debate Nationwide*, NONPROFIT Q., Winter 2009, at 44, 47.

17. See Lisa Wangsness, *Strapped Towns Tax Catholic Properties: Church Forced to Pay for Shuttered Buildings*, BOS. GLOBE, May 31, 2010, at A1; Chad Cain, *Taxing Times for Diocese of Springfield*, GAZETTENET.COM (Aug. 7, 2010) (on file with author); David Reid, *Holy Taxes!: Closed Leeds Church Hit with First Tax Bill, Mayor Clare Higgins and City Assessors Seek to Tax All Shuttered Catholic Churches*, NORTHAMPTON MEDIA (July 15, 2010), <http://northamptonmedia.com/blog/07/15/2010/holy-taxes-2/>.

18. BOS. GLOBE STAFF, BETRAYAL, *supra* note 4, at 7 (“[I]t was Boston that became the epicenter of the scandal, because the story broke there, because of the sheer number of priests implicated there, and because of the Catholic character of the city. . . . Nowhere else has the impact of the scandal been more deeply felt.”).

19. Wangsness, *supra* note 17.

20. *Id.* (“[T]he assessed value of the St. Frances property has fluctuated between \$3 million and \$4 million; the tax bill for the property is about \$34,000 this year.”).

21. See, e.g., sources cited *supra* note 17.

22. Wangsness, *supra* note 17.

as “tempting tax targets because they are expansive and in desirable areas of town, meaning their potential property values are high.”²³ Thus, the high tax bills will help cities and towns in their own time of economic hardship.²⁴ As one pro-tax lawyer explained: “[The tax is] a firefighter, or a teacher, or a DPW worker—that’s not money that [we] can leave on the table.”²⁵

Opponents of the tax, on the other hand, contend that “[t]ax-exempt status is not some type of municipal gift . . . but is designed to recognize the services . . . [nonprofit] organizations provide to a community.”²⁶ Paying property taxes diverts money from charitable work and harms those served by such organizations.²⁷ Because nonprofits with shuttered property are already struggling to regain their financial footing, the tax assessment increases the likelihood fallow properties will remain closed and threatens the closure of additional property.²⁸ Thus, those affected are the community members of the tax assessor—families pursuing a spiritual life, children educated in schools, and poor served by nonprofit programs.²⁹

The absence of an explicit statutory provision and the scarcity of relevant case law leave the issue of taxing fallow charitable property unresolved. This Note examines this debate, ultimately recommending that individual states should both accommodate the financial strains of charitable organizations by interpreting “charitable use” broadly and serve the interests of the greater community by taxing fallow property outside the breadth of this definition. Part II provides a background on nonprofit organizations by exploring how they are regulated by federal and state governments and explains the historical tax treatment of these organizations. Part III analyzes the two major approaches to taxing vacant nonprofit property. Finally, Part IV advocates for national consistency by pressuring all states to broadly construe nonprofit exemption provisions. This statutory interpretation accounts for the financial distress of both the nonprofit organizations and the towns that assess their taxes.

II. BACKGROUND

This Part explores nonprofit organizations, highlighting the tensions that emerge when granting a nonprofit tax exemption. To begin, Section A examines the characteristics of nonprofit organizations, tracing their importance through U.S. history. Then, Section B introduces nonprofit regulation, pointing out differences that exist between federal and state

23. *Id.*

24. *Id.*

25. *Id.*

26. Cain, *supra* note 17.

27. See Wells, *supra* note 12, at 1202.

28. See Cain, *supra* note 17 (explaining that the archdiocese retains closed buildings that it may use for religious purposes other than formal services until the need to sell arises).

29. Wells, *supra* note 12, at 1202.

oversight. Finally, Section C examines problems that arise in regulating nonprofit taxation.

*A. Characteristics of Nonprofit Organizations*³⁰

Nonprofits have always played an important role in the day-to-day functioning of the United States.³¹ “Encompassing such institutions as colleges and universities, not-for-profit hospitals and research institutions, churches and other religious organizations, museums and cultural institutions, and charitable organizations of many varieties, this sector historically has performed many functions that in other countries are the primary responsibility of the government.”³² This became especially true in the 1990s, when the number of reporting public charities grew about 6.3% annually and the U.S. population grew only 1.1% per year.³³ As the density of public charities increased, so did their popularity and influence.³⁴

Today, most nonprofits are formed with the mission to assist the public and serve society as a whole.³⁵ Contrary to popular belief, however, nonprofit organizations are allowed to earn a profit, and they often do.³⁶ Unlike a for-profit organization, the excess revenue earned by a nonprofit is not distributed to investors seeking a return on a capital investment but is instead retained by the nonprofit itself to further the organization’s charitable purpose.³⁷

Nonprofits are concentrated into particular parts of the economy: health, education, social services, and the arts.³⁸ Health is the largest of these segments, requiring enough resources and workers to compete with for-profit and government health organizations.³⁹ Nonprofit higher education creates a second segment, including organizations devoted to regulating and improving education as well as nonprofit schools and re-

30. The nonprofit sector and the legal community use the terms “nonprofit organization,” “charitable organization,” and “charity” interchangeably. See Evelyn Brody, *Introduction, in PROPERTY-TAX EXEMPTION FOR CHARITIES* ix, ix (Evelyn Brody ed., 2002). The term “charitable organization” derives from “charitable use” tax provisions in state statutes. See *infra* note 118 and accompanying text. For clarity and consistency, this Note will replace “charitable” with “nonprofit.”

31. See CHARLES T. CLOTFELTER, *FEDERAL TAX POLICY AND CHARITABLE GIVING* 1 (1985).

32. *Id.*

33. DAVID R. STEVENSON ET AL., *STATE NONPROFIT ALMANAC 1997: PROFILES OF CHARITABLE ORGANIZATIONS* 12 (1997).

34. See *id.* at 14.

35. ROBERT N. SUGHRUE & MICHELLE L. KOPNSKI, *QUALIFYING AS A NONPROFIT TAX-EXEMPT ORGANIZATION: A GUIDE FOR ATTORNEYS, ACCOUNTANTS, AND EXECUTIVE MANAGEMENT* 2–3 (1991).

36. BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* 4 (7th ed. 1998).

37. SUGHRUE & KOPNSKI, *supra* note 35, at 2.

38. SHARON M. OSTER, *STRATEGIC MANAGEMENT FOR NONPROFIT ORGANIZATIONS: THEORY AND CASES* 18 (1995).

39. See Richard Steinberg & Walter W. Powell, *Introduction, in THE NONPROFIT SECTOR: A RESEARCH HANDBOOK* 1, 7 (Walter W. Powell & Richard Steinberg eds., 2d ed. 2006). Nonprofit hospitals, nursing homes, mental health centers, health insurers, and hospices are just several examples of this growing area of public service. See *id.*

search centers themselves.⁴⁰ The third type of nonprofit includes those involved in providing social care to the needy.⁴¹ Finally, artistic nonprofits include a range of organizations devoted to maintaining culture and pursuing experimental expression.⁴² Together, these nonprofit organizations form the nonprofit sector.⁴³

Organizations making up the nonprofit sector face constant financial struggles.⁴⁴ This has been especially true since the 2008 financial crisis. From 2009 to 2010, fundraising for nonprofit hospitals fell twenty-three percent,⁴⁵ potentially forcing employees to take salary cuts and to turn away patients.⁴⁶ Consequently, an increasing demand for nonprofit medical support remains unsatisfied in the current economy.⁴⁷ Many nonprofit education institutions engaged in “risky financial behavior” prior to the economic recession.⁴⁸ As a result, nonprofit universities across the country are “cutting jobs, freezing salaries, and delaying dormitory and lab construction.”⁴⁹ Nonprofits involved in social service have difficulty achieving their financing costs in times of economic crisis⁵⁰ because they are dependent upon private donations for revenue.⁵¹ Similarly, artistic nonprofits rely heavily upon private donations and suffer most notably in times of economic strife.⁵²

40. Lester M. Salamon, *Scope and Structure: The Anatomy of America's Nonprofit Sector*, in *THE NATURE OF THE NONPROFIT SECTOR* 23, 31 (J. Steven Ott ed., 2001).

41. Steinberg & Powell, *supra* note 39, at 7.

42. *Id.* (“The realm of the arts captures the full gamut of nonprofit enterprise, from famous, established museums . . . to experimental organizations pursuing avant-garde expressions . . . [to] popular and folk culture, produced by for-profit firms.”).

43. HOPKINS, *supra* note 36, at 5. “This sector of society has been termed among other titles, the *independent sector*, the *third sector*, the *voluntary sector*, and the *philanthropic sector*.” *Id.*

44. See SCORE, *BUSINESS FOR NON-PROFIT* 29 (2006), available at <http://www.scorelancaster.org/LinkClick.aspx?fileticket=YMhb67DtFzI%3D&tabid=391&mid=955>.

45. Chelsey Ledue, *Nonprofit Hospitals Struggling to Secure Charitable Donations*, HEALTHCARE FIN. NEWS (Nov. 9, 2010), <http://healthcarefinancenews.com/news/nonprofit-hospitals-struggling-secure-charitable-donations>. “Sample wide, median return on investment (ROI)—a measure of fundraising effectiveness—fell 23 percent in 2009 from \$4.63 to \$3.57. For cash donations alone, median ROI fell 17 percent to \$3.26.” *Id.*

46. *See id.*

47. *See id.*; see also Virginia Ann Hodgkinson & Murray S. Weitzman, *Overview: The State of the Independent Sector*, in *THE NATURE OF THE NONPROFIT SECTOR*, *supra* note 40, at 9, 13 (noting that the aging population, increasing poverty rate, and more-expensive health care are the forces responsible for this increase).

48. Stephanie Strom, *Nonprofits Paying Price for Gamble on Finances*, N.Y. TIMES, Sept. 24, 2009, at A16. This “risky financial behavior” included participation in “auction-rate securities, interest-rate arbitrage [and] complex swaps—which backfired on them.” *Id.* (quoting Clara Miller, Chief Exec., Nonprofit Fin. Fund).

49. *Id.* “For example, Brandeis University, with \$208 million in tax-exempt bonds outstanding, plans to close its art museum and sell off the collection to raise money.” *Id.* “Even Harvard, with some \$2.5 billion in tax-exempt bonds at the end of fiscal 2007, and Yale, with \$1.6 billion” have made similar cuts. *Id.*

50. *See, e.g.*, Mary Jo Patterson, *In Downturn, Charities Face Needs of Their Own*, N.Y. TIMES, Nov. 23, 2008, at NJ1.

51. *See* Hodgkinson & Weitzman, *supra* note 47, at 15. Religious organizations generally try to collect money in excess of internal operations costs, so that the remaining funds can be contributed to charitable causes. *Id.*

52. Patterson, *supra* note 50.

Despite their current economic problems, the charitable sector is a powerful force in the U.S. economy.⁵³ Nonprofit organizations have a major influence on U.S. employment because their work is often labor intensive, requiring consistent contributions by both professionals and volunteers.⁵⁴ “By the end of the twentieth century, the U.S. nonprofit sector was a trillion-dollar-a-year operation that employed more civilians than the federal government and fifty state governments combined.”⁵⁵ It is estimated that by 2007, this sector employed 7.2% of the U.S. labor force, which was more than the utility, wholesale trade, or construction industries.⁵⁶ In addition to employing a significant percentage of Americans, nonprofits require substantial contributions from volunteers.⁵⁷ “In 1994, 48[%] of all American adults volunteered at an average rate of 4 hours per week.”⁵⁸ The number of U.S. volunteers has steadily increased through the turn of the century.⁵⁹ In 2010 alone, “8.1 billion hours of volunteer service worth an estimated \$169 billion” was performed by adults living in the United States.⁶⁰

Charitable organizations are consistently relied upon for their dependability and quality.⁶¹ “The hallmark of a nonprofit organization is that it cannot redistribute its profits Thus, such organizations have a reduced incentive to cheat on the quality of their products, since this cheating will not result in an appropriable surplus.”⁶² Consequentially, Americans trust nonprofits because they recognize that charities are motivated by different incentives than their for-profit counterparts.⁶³ As a result, the average citizen is more apt to volunteer his or her time and make monetary contributions to such an organization.⁶⁴ Citing this rationale and its supporting statistics, some experts believe nonprofits supplement or replace public goods or services when society becomes dissatisfied with them.⁶⁵ For example, “private education is a response to the failure of public education; private charity is a response to the inadequacy of redistribution, and so on. . . . The nonprofit sector serves specialized

53. Elizabeth T. Boris & C. Eugene Steuerle, *Scope and Dimensions of the Nonprofit Sector*, in THE NONPROFIT SECTOR: A RESEARCH HANDBOOK, *supra* note 40, at 66, 66.

54. OSTER, *supra* note 38, at 7.

55. Michael O'Neill, *Developmental Contexts for Nonprofit Management Education*, 16 NONPROFIT MGMT. & LEADERSHIP 5, 11 (2005).

56. Garry W. Jenkins, *Incorporation Choice, Uniformity, and the Reform of Nonprofit State Law*, 41 GA. L. REV. 1113, 1122 (2007).

57. Hodgkinson & Weitzman, *supra* note 47, at 16 (“Private support in the forms of contributions and voluntary time are important sources of funding to the independent sector.”).

58. *Id.*

59. See Press Release, Corp. for Nat'l and Cmty. Serv., New Fed. Report Shows Greatest Spike in Volunteers Since 2003 (June 15, 2010), available at http://www.nationalservice.gov/about/newsroom/releases_detail.asp?tbl_pr_id=1777.

60. *Id.*

61. See OSTER, *supra* note 38, at 19.

62. *Id.*

63. *Id.*

64. See *id.*

65. See *id.*

needs of the population.”⁶⁶ Thus, the nonprofit sector serves as an important and irreplaceable “political stabilizer[.]”⁶⁷

B. Regulation of Nonprofit Organizations

The nonprofit sector is divided into various subsets, some of which are excused from paying federal and state taxes.⁶⁸ In other words, “[t]he distinction between nonprofit and exempt can be summarized by the following axiom: all exempt organizations are nonprofit; however, nonprofit organizations are not all exempt organizations.”⁶⁹ Nonprofits that are free from taxation do not have an “inherent right” to exemption based on any constitutional principle.⁷⁰ Rather, whether these charitable organizations satisfy tax-exempt requirements is determined by both federal and state legislatures.

1. Federal Regulation

This Note explores property tax exemptions for nonprofits, which is a regulation concern of state and local governments.⁷¹ Some state statutes nevertheless rely on federal regulation to define nonprofits, making exemption under the Internal Revenue Code (I.R.C.) a prerequisite to state property tax exemption.⁷² Therefore, federal nonprofit regulation remains imperative to understanding the exemption debate surrounding the taxation of vacant nonprofit property.

The federal tax-exempt status of an organization is considered the “most prized of all tax concessions sanctioned by Congress.”⁷³ Bruce R. Hopkins, a national expert on nonprofit tax issues,⁷⁴ believes that six basic rationales underlie a nonprofit organization’s qualification for federal tax-exempt status. First, tax exemptions were enacted to remain consistent with state and local property tax exemptions.⁷⁵ Second, tax exemption arises as a byproduct of other legislation where “exemption is granted to facilitate accomplishment of the purpose of another legislative

66. *Id.*

67. *Id.*

68. HOPKINS, *supra* note 36, at 7.

69. SUGHRUE & KOPNSKI, *supra* note 35, at 2.

70. HOPKINS, *supra* note 36, at 7 (explaining that nonprofit rights are absent from constitutional protection).

71. *See infra* Part III.

72. Janne Gallagher, *The Legal Structure of Property-Tax Exemption*, in PROPERTY-TAX EXEMPTION FOR CHARITIES, *supra* note 30, at 3, 10.

73. HOPKINS, *supra* note 36, at 8 (citation omitted).

74. *See id.* at ix. Hopkins is a lawyer who specializes in the representation of nonprofit organizations. *Id.* He has served on various committees and wrote many books concerning the subject of tax-exempt charitable organizations and is considered an expert in his field. *See id.*

75. *Id.* at 9–10. Although present-day amendments make exemption under the Internal Revenue Code a prerequisite to property tax exemption, “the development of state charitable-exemption law predated the adoption of the federal Internal Revenue Code, and . . . property-tax exemption, rather than being derived from federal law, was the basis for many of the concepts that found their way into the income-tax regulations and rulings.” Gallagher, *supra* note 72, at 10.

end.”⁷⁶ Third, other tax exemptions are granted purely for tax reasons.⁷⁷ This explanation embodies the concept that “receipt of what otherwise might be deemed income by a tax-exempt organization is not a taxable event.”⁷⁸ Instead, the organization is merely a vehicle through which “those participating in the enterprise may receive and expend money.”⁷⁹ The fourth rationale for tax-exempt status concerns U.S. public policy and the significance of political pluralism—the necessity of political diversity.⁸⁰ As a result of pluralism, determining the appropriate role of the government and nonprofit organizations has been a never-ending process for Congress.⁸¹ Fifth, nonprofit tax-exempt organizations exist because their purpose is directly important to a large segment of U.S. society, and this purpose is of greater consequence if the nonprofit is not taxed.⁸² Finally, tax-exemption “is predicated on the view that exemption is required to facilitate achievement of significance to the entirety of society.”⁸³

Citing these principles, the federal government has granted tax-exempt status to certain charitable organizations since the inception of the United States.⁸⁴ In the early United States, federal revenue was derived primarily through customs duties and excise taxes.⁸⁵ Federal taxes were imposed on less than one percent of the population, and this percentage omitted charitable organizations.⁸⁶ After the Civil War, the Revenue Act of 1894 was enacted to address the government’s financial burden from fighting and reconstruction.⁸⁷ Here, Congress imposed a tax on “corporations, companies, or associations doing business for profit,” but left “corporations, companies or associations organized and conducted solely for charitable, religious, or educational purposes” exempt from taxation.⁸⁸ Although the Revenue Act of 1894 was eventually declared unconstitutional,⁸⁹ every subsequent revenue act granted organizations

76. HOPKINS, *supra* note 36, at 10. Social clubs are an example of this category. *Id.*

77. *Id.*

78. *Id.* at 19.

79. *Id.*

80. *Id.* at 10. Political pluralism in the United States has origins in the distrust for the government. *Id.* at 11.

81. *See id.* at 13. When writing tax statutes, “Congress view[s] tax exemption for charitable organizations as the only way to consistently correlate tax policy to political theory . . . and s[ees] the exemption of charities in the federal tax statutes as an extension of comparable practice throughout the whole of history.” *Id.*

82. *Id.* at 10.

83. *Id.*

84. E.C. LASHBROOKE, JR., *TAX EXEMPT ORGANIZATIONS 3–4* (1985) (documenting the history of tax-exempt organizations beginning in biblical times).

85. *Id.* at 3.

86. *Id.* at 3–4.

87. *Id.*

88. Revenue Act of 1894, 28 Stat. 556 (1894), *invalidated by* *Pollock v. Farmers’ Loan & Trust Co.*, 157 U.S. 429 (1895).

89. *See Pollock*, 157 U.S. at 583 (“We are of opinion that the law in question, so far as it levies a tax on the rents or income of real estate, is in violation of the Constitution, and is invalid.”); *see also* LASHBROOKE, *supra* note 84, at 4.

having a charitable, religious, or educational purposes an exemption—a tradition formally embodied by the Internal Revenue Service (IRS) in 1954 when I.R.C. § 501(c)(3) was enacted.⁹⁰

After 1954, the federal government gave increasing attention to the management of nonprofits, using its influence to classify tax-exempt organizations and monitor the deductibility of donations to charities.⁹¹ Today, federal influence over charitable entities is extensive. The importance of the federal tax exemption, the widespread use of federal exemption definitions, and the national reach of the IRS have resulted in a “gravitational pull,” making the federal government the “dominant means” of nonprofit regulation.⁹² Since the original revenue act, Congress has used this power to extend tax-exempt status to a multitude of charitable organizations. For example, tax-exempt status was later extended to include horticulture organizations, scientific organizations, and societies for the prevention of cruelty to animals and children.⁹³ Currently, corporations, funds, and foundations are awarded tax-exempt status pursuant to section 501 if they are organized for the following purposes: (1) religious, (2) charitable, (3) scientific, (4) testing for public safety or education, (5) fostering national or international amateur sports competition, or (6) preventing cruelty to children or animals.⁹⁴ Under the statute, these exempt organizations are subject to only narrow limitations. For example, no part of the net earnings of the organization can be used to benefit a private shareholder or individual and the organization cannot attempt to influence legislation or politics.⁹⁵

Despite the breadth of section 501, exempt organizations of today do not enjoy the “sociopolitical status” they did in the past.⁹⁶ “The proliferation of exempt organizations as well as the expansion and diversification of established exempt organizations have made the business community, the general public, and regulatory authorities more aware of exempt organizations’ functions and business philosophies.”⁹⁷ As a result, the exempt organizations are under the “watchful eyes” of the IRS and Congress.⁹⁸

This surveillance has led to the creation of an organizational test and an operational test for evaluating nonprofit organizations.⁹⁹ If an organization does not meet both of these tests, it will not be tax exempt.¹⁰⁰ A nonprofit organization satisfies the organizational test if it was orga-

90. LASHBROOKE, *supra* note 84, at 4.

91. Jenkins, *supra* note 56, at 1123–24.

92. *Id.*

93. LASHBROOKE, *supra* note 84, at 30, 32, 35.

94. I.R.C. § 501(c)(3) (2006).

95. *Id.*

96. SUGHRUE & KOPNSKI, *supra* note 35, at 9.

97. *Id.*

98. *Id.*

99. See HOPKINS, *supra* note 36, at 54.

100. *Id.*

nized for a purpose that federal law deems exempt and if its articles of organization expressly prohibit the nonprofit from engaging in activities outside the scope of its exempt purpose.¹⁰¹ An organization meets the operational test if it is “operated exclusively” for one or more exempt purposes.¹⁰² According to IRS regulations, however, “exclusively” is often given the same interpretation as “primarily.”¹⁰³ In other words, “an organization will not be regarded as operated exclusively for exempt purposes if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.”¹⁰⁴

Organizations successful in satisfying these tests are defined by the federal government as a nonprofit and are therefore excluded from most federal taxation. Qualifying organizations typically have one of the following charitable purposes: (1) relieving the poor; (2) advancing religion; (3) advancing education; (4) building or maintaining public buildings, monuments, or works; (5) decreasing the burdens of government; (6) decreasing neighborhood tensions; (7) combating prejudice and discrimination; (8) promoting human and civil rights secured by law; and (9) preventing community deterioration and juvenile delinquency.¹⁰⁵ Whether an activity is charitable is a question of facts and circumstances.¹⁰⁶ The same facts and circumstances influencing tax exemption at the federal level manifest in the tax regulation of individual states.¹⁰⁷

2. *State Regulation*

Almost every tax-exempt organization is a product of state law.¹⁰⁸ Indeed, prior to the mid-1900s and the increase in federal influence over nonprofit entities, states were the primary controllers of charitable organizations.¹⁰⁹ Today, state governments directly influence nonprofits in three ways: (1) they monitor nonprofit formation, (2) they exempt non-

101. Treas. Reg. § 1.501(c)(3)-1 (2008). The *organizational test* consists of two separate parts: (1) the organization’s statement of purpose and (2) the organization’s statement of powers. SUGHRUE & KOPNSKI, *supra* note 35, at 16. To satisfy requirement (1), the organization’s stated purposes must fall within those enumerated in section 501(c)(3). *Id.* To satisfy requirement (2), an organization’s governance cannot be capable of engaging in activities outside those for which it was organized. *Id.* at 17. “This means that even if an organization’s purpose or purposes fall within the boundaries of section 501(c)(3), the mere power to engage in substantial activity not in furtherance of those purposes would cause the organization to fail the organizational test. This is true regardless of whether the organization ever actually exercises such powers.” *Id.*

102. I.R.C. § 501(c)(3) (2006).

103. Treas. Reg. § 1.501(c)(3)-1(c)(1) (2008).

104. *Id.*; SUGHRUE & KOPNSKI, *supra* note 35, at 20.

105. SUGHRUE & KOPNSKI, *supra* note 35, at 23–24.

106. *Id.* at 24.

107. See discussion *infra* Part III.

108. HOPKINS, *supra* note 36, at 846.

109. Jenkins, *supra* note 56, at 1123.

profits from costly taxes, and (3) they use nonprofits as vehicles to deliver services funded by the public.¹¹⁰

State legislatures have enacted various laws to regulate nonprofits. These include laws that require nonprofits to register with state authorities and annually disclose financial information, that prohibit nonprofits from engaging in fraudulent activities, that give state officials substantial authority to investigate nonprofit organizations, and that monitor the nonprofits' officers and directors use of nonprofit funds.¹¹¹ Prior to receiving any nonprofit benefits, each organization must be formed as a legally recognized entity under state law, a process that makes the nonprofit subject to the regulation of a particular state.¹¹² Like their for-profit counterparts, nonprofits are structured as corporations, unincorporated associations, or trusts.¹¹³ Most nonprofits choose the corporate structure "because the law as to [corporate] formation and operation is usually quite clear, and because it can provide a shield against personal liability for those individuals who are [a nonprofit's] directors and officers."¹¹⁴ As a result, state law has a large influence on the nonprofit sector—an influence that varies by jurisdiction.¹¹⁵ These variations affect "important policy issues, such as accountability standards, the number of directors required, donor standing with respect to lawsuits, liability standards, layers of supplemental regulation by specialized state agencies, the nature of approvals for fundamental transactions, and the intensity of enforcement by state charity officials."¹¹⁶

Because nonprofits are products of state law, state governments determine what tax benefits a nonprofit organization will receive. Typically, these tax benefits include exemptions from general sales tax, state corporate income tax, and property tax.¹¹⁷ All states have adopted nonprofit exemptions from property taxes and corporate income taxes, with most also choosing to exempt purchases or sales from local sales taxes.¹¹⁸ Economic research has shown that these exemptions allow nonprofits to compete against for-profit firms providing comparable services.¹¹⁹

Despite the widespread market influence of nonprofit tax exemption, states do not apply taxation uniformly. While some states apply the general sales tax exemption only to the gross receipts of a seller, others

110. Woods Bowman & Marion R. Fremont-Smith, *Nonprofits and State and Local Governments*, in *NONPROFITS & GOVERNMENT: COLLABORATION & CONFLICT* 181, 182 (Elizabeth T. Boris & C. Eugene Steuerle eds., 2d. ed. 2006).

111. Wells, *supra* note 12, at 1211.

112. Jenkins, *supra* note 56, at 1124.

113. HOPKINS, *supra* note 36, at 846.

114. *Id.* at 847.

115. Jenkins, *supra* note 56, at 1124.

116. *Id.* at 1126–27 (footnotes omitted).

117. Bowman & Fremont-Smith, *supra* note 110, at 201.

118. *Id.*

119. See Joseph J. Cordes & Burton A. Weisbrod, *Differential Taxation of Nonprofits and the Commercialization of Nonprofit Revenues*, in *TO PROFIT OR NOT TO PROFIT* 83, 88–89 (Burton A. Weisbrod ed., 1998).

choose to tax the receipts of services or to tax only tangible goods.¹²⁰ Nonprofit exemption from corporate net income tax also varies across states. While some states use a flat tax rate, others use graduated rates.¹²¹ Furthermore, states define taxable income differently and use alternative methods for allocating net income to a particular state.¹²²

Similarly, section 501(c)(3) does not automatically grant a state property tax exemption,¹²³ and the result is a patchwork pattern of exemption that varies by state. Thus, nonprofit-owned property is subject to many differences in taxation conditions and limitations depending on its location.¹²⁴ For example, while the exemption provisions of twenty or more states allow automatic exemption based solely on the name of the nonprofit holding the property, seventeen other states allow individual communities to choose which nonprofits deserve exemption.¹²⁵ Delaware gives counties the authority to exempt nonprofits, while other states leave the choice to local governmental units.¹²⁶ Leaving the choice to such local governing bodies results in an extremely complex taxation structure, with a parcel exempt from taxation by one unit, yet taxed by another overlapping unit.¹²⁷

Despite the state-to-state unpredictability, the property tax exemption is extremely important to religious organizations, private educational institutions, nonprofit housing developments, and arts organizations—the nonprofits most likely to own large portions of property.¹²⁸ A 2001 survey estimated that excluding churches, the value of charitable property in the United States was worth \$570 billion, and the property tax exemptions were worth between \$9 billion and \$15 billion.¹²⁹ Because this number excludes the vast holdings of the Catholic Church,¹³⁰ it is a gross underestimate of the total economic influence of property tax exemptions.¹³¹

The varied influence of state nonprofit regulation coupled with the government's increasing regulation of nonprofit organizations has led to a movement advocating uniformity and reform in nonprofit state law.¹³²

120. Bowman & Fremont-Smith, *supra* note 110, at 205.

121. *Id.* at 206.

122. *Id.*

123. *Id.* at 202.

124. *Id.*

125. *Id.*

126. *Id.* (noting that counties in Delaware have constitutional authority to grant property tax exemptions).

127. *Id.* New York employs such a regime. *Id.*

128. *Id.*

129. *Id.*

130. *See id.*; *see also* KEVIN CAHILL WITH ROB MCMAHON, WHO OWNS THE WORLD: THE SURPRISING TRUTH ABOUT EVERY PIECE OF LAND ON THE PLANET 44 (2010).

131. Bowman & Fremont-Smith, *supra* note 110, at 202.

132. *See, e.g.,* Jenkins, *supra* note 56, at 1115 (“[A]rgu[ing] that because of the incorporation habits of nonprofit corporations, coupled with the limited governmental resources devoted to the development and enforcement of nonprofit state law, private lawmaking initiatives . . . provide the primary means for achieving uniformity and reform of nonprofit law.”).

Supporters of the movement explain that not every state actively regulates its charities, and those that do often waste their time on issues more appropriately addressed by the federal government.¹³³ Some contemporary tax policy has proven that centralized control of tax regulation is more efficient than regulation that varies across every state.¹³⁴ The efficiency of centralized control has become more apparent since amendments to the Freedom of Information Act in 2007.¹³⁵ It is now possible for “organizations across the country . . . to learn the nature of the problems their counterparts [are] facing and the rationale used by the [IRS] in the individual rulings it issued.”¹³⁶ To accommodate this trend toward the increasing transparency of taxation, supporters of charitable tax reform advocate a system that is more predictable and that subjects nonprofits across the country to similar regulations and exemptions.¹³⁷

C. *Problems with Nonprofit Regulation*

The tax-exempt treatment of nonprofit organizations has long been the subject of intense political debate.¹³⁸ For example, the exemption of church property from taxation has been attacked as inconsistent with the separation of church and state, and the commercialization of medical services has led to the questioning of the hospital exemption.¹³⁹ Debates over the taxation of nonprofit organizations typically involve matters of uniformity.¹⁴⁰ Thus, it is no surprise that debates often include issues arising from the taxation of property. These issues typically fall into two categories. The first category stems from legislative provisions that require varied taxation depending upon the “type of property or the status of the owner.”¹⁴¹ The second category is the result of “administrative favoritism” that assigns varying values to properties of equal market

133. MARION R. FREMONT-SMITH, *GOVERNING NONPROFIT ORGANIZATIONS: FEDERAL AND STATE LAW AND REGULATION* xiii (2004) (explaining important changes in federal policy that make it easier for the government to “police” charities).

134. *See id.* at 241, 460; *see also* Alice M. Rivlin, *Uniform State Taxes Offer Shared Relief*, L.A. TIMES, Sept. 1, 1991, at D2 (“As the U.S. economy becomes more national and international, the case for more uniformity in state taxation increases. People and capital are more mobile than they used to be. The economy is increasingly dominated by large national and international firms and by service industries. Many services—legal, accounting, advertising, data processing, finance, catalogue sales—can be performed at a substantial distance from the customer.”).

135. *See* Electronic Freedom of Information Act Amendments of 1996, Pub. L. No. 104-231, 110 Stat. 3048 (2007).

136. FREMONT-SMITH, *supra* note 133, at xiv.

137. *See* Thomas Kelley, *Rediscovering Vulgar Charity: A Historical Analysis of America's Tangled Nonprofit Law*, 73 *FORDHAM L. REV.* 2437, 2498–99 (2005) (arguing that current nonprofit regulation is pushing charitable organizations towards a free market, while concurrently punishing them for doing so).

138. Joan M. Youngman, *Property Taxation: Fairness and Popularity, Perceptions and Reality*, in *TAX JUSTICE: THE ONGOING DEBATE* 221, 230 (Joseph J. Thorndike & Dennis J. Ventry, Jr., eds., 2002) (explaining the controversy that exists in many forms of tax policy, including the taxation of nonprofits).

139. *Id.*

140. *See id.* at 229.

141. *Id.*

price.¹⁴² Debates over the taxation of nonprofits typically arise under the first category. For example, a series of lawsuits in Pennsylvania during the late 1990s deprived several nonprofit organizations of exemption from property taxes.¹⁴³ In 1997, the state legislature responded by restoring most exemptions and “substantially broadening the concept of charity.”¹⁴⁴ As this example demonstrates, attacks on the tax exemption of certain property often fail to produce significant change and instead often result in the strengthening of exemption provisions.

The controversy over nonprofit property tax exemption is typically highly localized and is entwined with current political issues.¹⁴⁵ A contemporary example of such a debate has taken place in the Boston suburb of Scituate.¹⁴⁶ Here, St. Frances X. Cabrini Church was closed in 2004 by the Roman Catholic Archdiocese of Boston as part of a cost-cutting plan in the wake of financial problems associated with the clergy sexual abuse scandal, but the church has since been occupied by former parishioners holding vigils and otherwise protesting the church’s closure.¹⁴⁷ In 2005, Scituate assessed St. Frances its first \$40,000 tax bill for the thirty-acre property, claiming that the church was taxable since its occupation was not sanctioned by the Catholic Church.¹⁴⁸ The Boston Archdiocese protested the taxation in court but eventually withdrew the case when its initial motion for summary judgment was denied by the local Superior Court.¹⁴⁹ The Archdiocese of Boston decided that paying more than \$200,000 on the church’s property (assessed at \$4.5 million in 2005) was better than an uncertain and costly battle in appellate court.¹⁵⁰

The Scituate case leaves many taxation issues unresolved and illustrates the larger problem of defining a property’s use. An organization’s exemption from property taxes is based on two related requirements: (1) the property owner must be a charitable organization, and (2) the property must be used for a charitable purpose.¹⁵¹ Although property owned by nonprofits but used for a commercial purpose does not receive tax exemption in most states, state laws are less clear about whether property that is *unused* would fail the charitable-use test.¹⁵² In denying the Arch-

142. *Id.*

143. Bowman & Fremont-Smith, *supra* note 110, at 205.

144. *Id.*

145. *Id.* at 204; Youngman, *supra* note 138, at 230.

146. See Jennifer Mann, *Scituate Claims Win Against Archdiocese to Tax the Closed Cabrini Church*, PATRIOT LEDGER (Apr. 23, 2010, 7:03 AM), <http://www.patriotledger.com/business/x53549581/Scituate-claim-win-against-Archdiocese-to-tax-the-closed-Cabrini-church>.

147. See Wangness, *supra* note 17.

148. Mann, *supra* note 146.

149. See *Roman Catholic Archbishop v. Town of Scituate*, No. 2007-4500-E, 2009 WL 3103728, at *1, *2 (Mass. Super. Ct. Sept. 28, 2009) (denying the archdiocese’s motion for summary judgment); see also Wangness, *supra* note 17.

150. Wangness, *supra* note 17.

151. John D. Colombo, *Massachusetts Towns Taxing Empty Church Properties*, NONPROFIT L. PROF BLOG (June 2, 2010), <http://lawprofessors.typepad.com/nonprofit/2010/06/massachusetts-towns-taxing-empty-church-properties.html>.

152. *Id.*

diocese of Boston's motion for summary judgment against Scituate, one of the few opinions directly on point with this issue, the judge wrote:

The occasional or incidental use of . . . property by [a nonprofit organization] . . . shall not be deemed to be an appropriation for purposes other than religious worship or instruction. . . . The property tax exemption, however, depends upon the intended use of the property, and requires there at least be a distinct and fixed intent to use . . . otherwise, it is not a house of religious worship.¹⁵³

Because "intent" is such a critical part of determining fallow property's qualifications for tax exemption, unused nonprofit property will likely mirror the legal analysis of nonprofit property with an *anticipated* use.

The question of whether a prospective use of property entitles nonprofit property a present exemption from taxation varies across jurisdictions:

At war in the decisions are the facts, on the one hand, that an intention to make future use of property for exempt purposes may never be realized . . . and, on the other hand, that very frequently it is not possible for all phases of a plan to confer a public benefit to be realized at once . . . and it is prudent to anticipate future needs¹⁵⁴

In most jurisdictions, tax exemption requires that a nonprofit property's use be "present, actual or physical."¹⁵⁵ The exempt property owner's "intended, prospective, or future use" of the property is insufficient.¹⁵⁶ Other jurisdictions allow exemption from taxation on all nonprofit property regardless of whether the property is being presently used for the exempt purposes or is being held for use in the future.¹⁵⁷ Nevertheless, further complications arise in jurisdictions allowing tax exemptions for anticipated use. There are often hidden conditions and limitations, and a bona fide intention of future use must be proven.¹⁵⁸

Ultimately, the regulation of unused nonprofit property is both inconsistent and unpredictable. Even if unused property is compared to the tax law of anticipated use, state law is far from uniform. Although possible methods for state regulation will be explored in this Note, the need for state uniformity for this controversial tax matter is apparent.

153. *Scituate*, 2009 WL 3103728, at *2 (quoting MASS. GEN. LAWS ch. 59, § 5 (2010)).

154. Maurice T. Brunner, Annotation, *Prospective Use for Tax-Exempt Purposes As Entitling Property to Tax Exemption*, 54 A.L.R.3d 9, 14 (1974).

155. *Id.* at 18; *see, e.g.*, *Ill. Inst. of Tech. v. Skinner*, 273 N.E.2d 371, 374 (1971) (admitting that the court had "often held that property must be in actual use for the exempting purpose, to qualify for exemption," but upholding the exemption in the particular instance).

156. Brunner, *supra* note 154, at 18.

157. *Id.*

158. *Id.* at 19.

III. ANALYSIS

Despite recent financial hurdles, the role of nonprofit organizations in U.S. life is both expanding and evolving.¹⁵⁹ In addition to fulfilling distinct charitable purposes,¹⁶⁰ nonprofits function as employers, operate independent education institutions, control employment relations, own intellectual property, and defend and prosecute legal actions.¹⁶¹ As nonprofits increase involvement in the business sector,¹⁶² their purpose for maintaining property can become increasingly muddled.¹⁶³ This is especially true when a nonprofit claims that its property, although currently fallow, continues to serve a charitable purpose.¹⁶⁴ Consequently, case law has produced two conflicting approaches to assessing whether property held by a nonprofit for anticipated future use is subject to a charitable use tax exemption.¹⁶⁵ This Part demonstrates that these approaches cannot coexist. First, Section A introduces strict statutory construction and explains that states adopting this approach do so with much variation. Second, Section B introduces broad statutory construction and proves that although this approach grants exemption to broader classes of property, states adopting this approach are relatively consistent with its application. Finally, Section C illustrates that charitable exemption regulation must become more uniform across the United States.

A. Approach I: Strict Statutory Construction

The majority of states strictly interpret tax exemption provisions, focusing on the plain meaning of statutory language and excluding property not clearly within its scope from exemption.¹⁶⁶ These states construe exemption statutes against the property owner,¹⁶⁷ forcing the owner to bear the burden of proving his or her land exists within the plain mean-

159. See *supra* Part II.A.

160. *Id.*

161. See, e.g., JAMES R. LANGABEER II & JOHN NAPIEWOCKI, *COMPETITIVE BUSINESS STRATEGY FOR TEACHING HOSPITALS* 3–4 (2000) (hospitals); Elizabeth Gingerich, *Unraveling the Establishment Clause: Legal and Other Practical Concerns for the Church “Business,”* RUTGERS J.L. & RELIGION, Fall 2008, at 39, 41–42 (churches); John C. Knapp & David J. Siegel, *General Introduction*, in 3 *THE BUSINESS OF HIGHER EDUCATION: MARKETING AND CONSUMER INTERESTS* viii–x (John C. Knapp & David J. Siegel eds. 2009) (universities).

162. See Joseph J. Cordes & C. Eugene Steuerle, *Nonprofits and Business: A New World of Innovation and Adaptation*, in *NONPROFITS & BUSINESS* 1, 2 (Joseph J. Cordes & C. Eugene Steuerle eds., 2009).

163. See, e.g., *New Hampshire High Court Denies Tax Exemption to Churches in Suppressed Parishes*, J. MULTISTATE TAX’N & INCENTIVES, Feb. 2008, at 39, 39–40 (outlining the legal battle that ensued after a church’s reorganization).

164. See *id.*

165. See *supra* Part II.C.

166. See, e.g., *Glen Oak Cemetery Co. v. Bd. of Appeals of Cook Cnty.*, 192 N.E. 673, 674 (Ill. 1934); *Barr v. Geary*, 142 N.E. 622, 631 (Ind. App. 1924); *Town of Milton v. Ladd*, 206 N.E.2d 161, 164 (Mass. 1965); *YMCA v. City of Orange*, 128 A. 580, 581 (N.J. 1925); *Hedgcroft v. City of Hous.*, 244 S.W.2d 632, 636 (Tex. 1951).

167. See, e.g., *Christ Church v. Millburn*, 57 A.2d 506, 507 (N.J. 1948) (“One seeking exemption must establish it by proofs that are free from fair doubt.”).

ing of exemption.¹⁶⁸ Consequently, neither mere ownership nor intent to use is equivalent to actual use.¹⁶⁹ Even if land is acquired for a charitable purpose by a nonprofit organization, the need for a property owner to prove actual charitable use is not eliminated.¹⁷⁰

Although strict statutory construction appears to be rather straightforward, courts have added their own nuance to the rule, diluting exemption uniformity across the fifty states and causing unnecessary confusion. For example, some jurisdictions require a property's present, charitable use to meet the further requirement of exclusivity.¹⁷¹ If even a small tract of a larger property or a portion of a building fails to clearly satisfy the charitable use provision, these courts tend to assess a tax on the *entire* property.¹⁷² Conversely, other jurisdictions segment an organization's nonprofit property into that which meets the exclusive charitable use requirement and that which does not.¹⁷³ These states only assess taxes on the property that is not used for charitable purposes,¹⁷⁴ granting the remainder an exemption.

Courts that have construed exemption provisions to require actual use differ further in their treatment of property which is under development, adaptation, or construction. Some courts indicate that property in the actual process of development remains qualified for tax exemption although it is not yet in actual use.¹⁷⁵ Because there is a point at which it is reasonable to assume a charitable organization will not use its property for a charitable purpose in the immediate future, courts will grant the ex-

168. Brunner, *supra* note 154, at 20–22.

169. *In re* Assessment of Props. of Fite Found., 237 P.2d 427, 428, 432 (Okla. 1951) (“The use of property is the basis of tax exemption provided in the Constitution, and real estate acquired by a nonprofit benevolent corporation, though held for possible future use by such corporation, and dedicated to an ultimate use for charitable purposes by such corporation . . . but not presently so used may be subject to . . . tax until it is actually or constructively used for such a purpose.” (internal quotation marks omitted)).

170. Ill. Inst. of Tech. v. Skinner, 273 N.E.2d 371, 374 (Ill. 1971) (“[P]roperty must be in actual use for the exempting purpose to qualify for exemption. Evidence that land was acquired for an exempt purpose does not eliminate the need for proof of actual use for that purpose. Intention to use is not the equivalent of use.” (internal quotation marks omitted)).

171. *See, e.g.*, City of Perth Amboy v. Barker, 65 A. 201 (N.J. 1906).

172. Where a one-hundred acre tract had been purchased by the city to extend a water supply system, and only ten acres were actually being used for this purpose, the court in *Barker* held the entire tract was subject to property taxes. *Id.* Although the city planned on using the tract for a public purpose in the future, this made no difference to the court. *Id.* Although *Barker* deals exclusively with tax exemption for a public purpose, tax exemption for a charitable purpose has followed an identical pattern. *See also* Brunner, *supra* note 154, at 18–19 (describing tax provisions construed to require actual use).

173. *See, e.g.*, Osteopathic Hosp. of Me. v. Inhabitants of Portland, 26 A.2d 641, 641, 645 (Me. 1942) (holding that a hospital with multiple tracts of land would be assessed a property tax on those not currently in use).

174. *See id.*

175. *See, e.g.*, City of Clifton v. State Bd. of Tax Appeals, 48 A.2d 202, 203 (N.J. 1946) (holding that property dedicated for cemetery use was exempt from taxation when graves were being laid out and prepared for such use, but not actually occupied).

emption.¹⁷⁶ Nevertheless, other courts take a contrary view, denying exemption to buildings which are already under construction.¹⁷⁷ These courts believe that use should be measured on the day determinative of a property's tax status and an alternative holding that extends exemption to developing properties exceeds the plain meaning of statutory language.¹⁷⁸

A final disjunction among states applying strict statutory construction is their interpretation of who must use property for a charitable purpose. While some states hold that freedom from assessment extends only to property that the nonprofit institution occupies and uses for its *own* charitable purpose,¹⁷⁹ others are more lenient with this requirement.¹⁸⁰ Jurisdictions that strictly monitor this requirement use parallel logic to those courts requiring exclusive use.¹⁸¹ Such jurisdictions explain that immunity from exemption does not depend upon mere ownership and possession of property or upon the extent or length of the actual occupancy, but it depends upon exclusive operation which contributes immediately and solely to the advancement of the nonprofit's purpose.¹⁸² On the other hand, more lenient jurisdictions point to statutory intent. These courts explain that tax exemption statutes exist to promote benevolent, rather than self-benefiting institutions.¹⁸³ As long as a benevolent organization owns the property and such property is used for a charitable purpose, distinguishing amongst various charitable activities is a discernment courts need not make.¹⁸⁴

As this Section has demonstrated, states that interpret charitable exemption clauses strictly often assess nonprofit organizations taxes on unused property. This policy has created confusing jurisdictional splits, and the need for an alternative, more uniform approach is becoming increasingly apparent.

176. *See id.*; *Vill. of Hibbing v. Comm'r*, 14 N.W.2d 923, 927 (Minn. 1944). *But see State v. Ritschel*, 20 N.W.2d 673, 679 (Minn. 1945).

177. *See, e.g., Cedars of Lebanon Hosp. v. L.A. Cnty.*, 221 P.2d 31, 39–40 (Cal. 1950) (holding that a hospital must pay property taxes on a developing property that was eighty-five percent complete).

178. *See id.*

179. *See, e.g., Soc'y of Cincinnati v. Exeter*, 31 A.2d 52, 58 (N.H. 1943) (holding that real estate held for a charitable use outside of a society's charter was not exempt from taxation).

180. *See Camp Emoh Assocs. v. Inhabitants of Lyman*, 166 A. 59, 60–61 (Me. 1933) (holding that charitable property is exempt from taxation when used for a charitable organization's own purpose for only part of the year).

181. *Compare Osteopathic Hosp. of Me. v. Inhabitants of Portland*, 26 A.2d 641, 645 (Me. 1942) (holding charitable use must be exclusive for eligible tax exemption), *with Soc'y of Cincinnati*, 31 A.2d at 58 (holding a charitable organization must use property for its own purpose to be eligible for tax exemption).

182. *See Soc'y of Cincinnati*, 31 A.2d at 58.

183. *See Camp Emoh Assocs.*, 166 A. at 60–61.

184. *See id.* at 61.

B. Approach 2: Broad Statutory Construction

Courts refusing to adopt a strict interpretation for charitable exemption statutes choose to construe the exemption provisions of their statutes more liberally.¹⁸⁵ These states place few limitations on tax exemption, requiring only that nonprofits possessing property outside the scope of their charitable purpose not hold land for profit or otherwise use it to generate income.¹⁸⁶ In all of these states, property is often exempt without regard to its use, the exemption instead depending upon the purpose for which the property is held.¹⁸⁷ Some courts have taken this logic a step further and have automatically accorded exemption to specified institutions.¹⁸⁸ These states grant institutions that fall within predetermined exemption categories the equivalent of per se tax immunity.¹⁸⁹ For example, states have granted institutional exemptions to property owned by the public, by the state, or by a multitude of well-known charitable organizations.¹⁹⁰ Although these exemptions are always subject to review by the state and its courts,¹⁹¹ pre-exempt properties are rarely investigated; thus, few have ever been assessed a property tax.¹⁹²

Courts adopting a liberal interpretation of use have extended tax exemption to two types of property that are typically taxed by jurisdictions adopting a strict interpretation. The first of these property types is land upon which a building is being erected, prepared for use, or modified.¹⁹³ Courts have extended exemption provisions to property upon which a building is currently being constructed when the completed building will be used for a charitable purpose and when construction is proceeding without unreasonable delay.¹⁹⁴ Such courts are unwilling to interpret exemption provisions narrowly because doing so would deprive a nonprofit organization of its tax benefits when “accident or want of repair” made property unfit for use.¹⁹⁵ These courts further recognize that subjecting charitable property to taxation during the construction period

185. See, e.g., *Evergreen Mem'l Park Ass'n v. Evatt*, 46 N.E.2d 286, 289–90 (Ohio 1943).

186. See *id.* (finding it unnecessary to tax a nonprofit for its cemetery when no evidence existed that the lands in question were currently held by the owner with a view to profit).

187. Brunner, *supra* note 154, at 18–19.

188. See *Nat'l Bank of Burlington v. Huneke*, 98 N.W.2d 7, 11 (Iowa 1959) (noting that the character of the organization owning the property is determinative of exempt status).

189. Brunner, *supra* note 154, at 41.

190. *Id.*

191. See, e.g., *Huneke*, 98 N.W.2d at 11.

192. See Brunner, *supra* note 154, at 47–55.

193. *Id.* at 56–62.

194. *Trinity Church v. Boston*, 118 Mass. 164, 166 (1875) (“[R]eal estate held . . . not more than sufficient in extent to meet its reasonable requirements in this respect, and devoted . . . in good faith . . . upon which the work of erection already commenced is prosecuted without unreasonable delay . . . is entitled to the exemption given by the statute.”).

195. *Id.* at 165.

would “defeat the object” of property exemption statutes.¹⁹⁶ Since “exemption statutes are a legislative recognition of the benefits received by society as a whole from properties devoted to appropriate objects of exempt institutions,” taxing land when construction is occurring would discourage charitable organizations from undertaking improvement projects, possibly mitigating their benevolence.¹⁹⁷

Courts liberally construing exemption provisions typically extend exemption to charitable property held for future use. Unlike their counterparts who hold charitable use must be present and actual,¹⁹⁸ these jurisdictions consider exemption when a property is used prudently and legally, pending its ultimate charitable use.¹⁹⁹ This category of exemption is most frequently seen in cases where charitable use of land is contingent upon the passage of time, such as property held for a future cemetery.²⁰⁰ Because the property in question may not be put to exclusive, charitable use for several decades, courts see no advantage in forcing the entire property’s vacancy in the present.²⁰¹ If the property’s present use is not producing a profit for the charitable organization, intended future use is sufficient to preclude taxation.²⁰²

This Section has demonstrated that states that interpret charitable exemption clauses broadly do not assess nonprofit organizations taxes on unused property. Despite including a broader spectrum of property within their exemption definitions, states adopting this approach are more uniform in their exemption policies.

C. *The Complete Picture*

The treatment of fallow charitable property across the United States is extremely complex.²⁰³ This is because a number of its central concepts, including the definition of charitable use, are inherently unsettled among the fifty states.²⁰⁴ States adopting a strict statutory construction of charitable exemption provisions, therefore, exist simultaneously with those adopting a broad statutory construction. This simultaneous combination not only “provide[s] a rich medium for dispute,”²⁰⁵ but is

196. *S. Iowa Methodist Homes, Inc. v. Bd. of Rev. of Cass Cnty.*, 136 N.W.2d 488, 490 (Iowa 1965).

197. *Id.*

198. *See supra* Part III.A.

199. *See Brunner, supra* note 154, at 56–59.

200. *See, e.g., State v. Lakewood Cemetery Ass’n*, 101 N.W. 161, 163 (Minn. 1904) (exempting land held for the enlargement of a cemetery although currently used for a greenhouse). *See also St. Mary’s Sch. v. Concord*, 118 A. 608, 608–09 (N.H. 1922) (exempting property held for the construction of a school although currently used to maintain “war gardens”).

201. *See Lakewood Cemetery Ass’n*, 101 N.W. at 163.

202. *See id.*

203. *See Joan M. Youngman, The Politics of the Property-Tax Debate: Political Issues, in PROPERTY-TAX EXEMPTION FOR CHARITIES, supra* note 30, at 23, 23.

204. *Id.*

205. *Id.* at 23–24.

complicating the nonprofit sector's ability to predict and understand property taxation and is giving some types of nonprofits an advantage over others.

Consider again the St. Frances X. Cabrini Church discussed in Part II.C as an example. There, the Boston church shut its doors to official church services, but the building itself was still occupied by parishioners holding around-the-clock vigils for five and one-half years.²⁰⁶ In denying the Boston archdiocese's motion for summary judgment, the Boston Superior Court held that a nonprofit property tax exemption depends on the intended use of the property.²⁰⁷ Since it was unclear whether St. Frances would be used again in its official capacity, tax exemption was questionable.²⁰⁸

This holding highlights several issues at the heart of the nonprofit property tax debate. First, in those cases involving churches, a court must make decisions on the crux of the divide between church and state. The court in the Cabrini Church case decided that vigil masses held by parishioners on a property's premises were not equivalent to formal services held by a priest.²⁰⁹ Not all religions require formal services, however, and many of those which do not could have achieved tax-exempt status on similar sets of facts.²¹⁰ Moreover, some religions hold formal services to secularize a consecrated building.²¹¹ Tax assessors frequently rely upon the existence of these services to determine whether taxes should be assessed on a fallow church.²¹² Since use is much easier to rebut in situations where deconsecration services do not occur,²¹³ nonprofit organizations without this tradition are more likely to pay property taxes.

This example also highlights the impact of inconsistent property tax assessment on a particular community. Massachusetts is a state requiring actual, exclusive use of charitable property for it to be deemed exempt from taxes.²¹⁴ Thus, Boston-area churches, many of which are already suffering financially,²¹⁵ are frequently assessed tax bills which they are in-

206. Jennifer Mann, *Vatican Will Rule on Closed Scituate Church: Highest Court to Decide on 10 Parishes the Archdiocese Closed in 2004*, PATRIOT LEDGER (May 6, 2010, 7:59 AM), <http://www.patriotledger.com/lifestyle/faith/x1773729237/Vatican-will-rule-on-closed-Scituate-church>.

207. *Roman Catholic Archbishop v. Town of Scituate*, No. 2007-4500-E, 2009 WL 3103728, at *1, *2 (Mass. Super. Ct. Sept. 28, 2009).

208. *Id.*

209. *See id.*

210. INTERNAL REVENUE SERV., TAX GUIDE FOR CHURCHES AND RELIGIOUS ORGANIZATIONS 2-4 (2009), <http://www.irs.gov/pub/irs-pdf/p1828.pdf>.

211. *See, e.g.*, AN EPISCOPAL DICTIONARY OF THE CHURCH: A USER FRIENDLY REFERENCE FOR EPISCOPALIANS 474 (Don S. Armentrout & Robert Boak Slocum eds., 2000).

212. Telephone Interview with Wesley Hills, Reverend, St. Andrews Episcopal Church (Feb. 13, 2011). Reverend Hills is also an attorney and Chairman of the Standing Committee of the Episcopal Diocese of San Diego. *Id.*

213. *Id.*

214. *See Bd. of Assessors of Bos. v. Vincent Club*, 217 N.E.2d 757, 760 (Mass. 1966); *Assessors of Weston v. Trs. of Bos. Coll.*, 6 N.E.2d 363, 365 (Mass. 1937); *All Saints Parish v. Inhabitants of Brookline*, 59 N.E. 1003, 1004 (Mass. 1901).

215. *See supra* note 147 and accompanying text.

capable of paying. The result is a cycle of economic distress: the greater the number of churches that close, the more money the archdiocese pays in property taxes. The more money paid by the archdiocese, the more churches it closes. In the end, the people of greater Boston suffer most from this unfortunate cycle.²¹⁶ Churches are forced to turn worshipers away and direct the needy to a neighboring community²¹⁷—something that would not occur if Boston were governed by charitable exemption laws that broadly interpret use.

IV. RECOMMENDATION

Property tax exemption for nonprofits was founded upon ideals of philanthropy and social service.²¹⁸ Although the scope of charitable work has expanded and developed throughout U.S. history, these ideals still form the crux of the nonprofit sector and motivate its service to communities across the country.²¹⁹ This Note has demonstrated that the continued influence of nonprofits demands a more consistent approach in nonprofit property taxation.²²⁰ This Part presents a two-part solution to improving the treatment of nonprofit property that is fallow. First, Section A advocates for uniform exemption interpretation throughout *all* states. Second, Section B promotes adoption of a broad statutory construction of charitable use that allows fallow nonprofit property to remain exempt from taxation.

A. *Step 1: The Necessity of a Uniform Exemption System*

Contemporary tax policy is defined by its failure to live up to former Treasury Secretary William E. Simon's goal of appearing to be "a system that is designed on purpose."²²¹ This Note has described the taxation of nonprofit property as inconsistent and unpredictable²²²—a system without a clear purpose. This Section explains that correcting the seemingly random taxation system will require advocating simplicity throughout all fifty states.

216. See *supra* text accompanying notes 27–29.

217. See Wells, *supra* note 12, at 1202–03; see also George James, *Newark Archdiocese Reorganization Plan May Result in the Closing of 16 Churches*, N.Y. TIMES, May 20, 2004, at B1.

218. Stephen Diamond, *Efficiency and Benevolence: Philanthropic Tax Exemptions in 19th-Century America*, in PROPERTY-TAX EXEMPTION FOR CHARITIES, *supra* note 30, at 115, 115.

219. See *id.*; see also *supra* Part II.A.

220. See *supra* Part III.

221. DEP'T OF THE TREASURY, BLUEPRINTS FOR BASIC TAX REFORM 1 (1977), <http://www.treasury.gov/resource-center/tort-policy/Document/full.pdf>.

222. See *supra* Part II.B–C.

1. *Advocating for Simplicity*

Simplicity should be given great weight in determining modern taxation policy.²²³ Recently, President Obama stressed the importance of taxation simplicity by signing the Plain Writing Act of 2010.²²⁴ The Act requires all federal agencies—and in particular the IRS—to translate all documents with which the public must deal into “plain writing.”²²⁵ This sentiment was also reflected in the President’s subsequent State of the Union Address when he said, “the best thing we could do on taxes for all Americans is to simplify the individual Tax Code.”²²⁶

Tax simplicity often requires implementing a comprehensive approach to exemption provisions that does not force taxpayers to go through elaborate calculations in order to figure out whether or not they qualify.²²⁷ As explained in Part III, such a comprehensive approach does not apply to nonprofit property tax exemptions because exemption provisions vary significantly across states. While some states adopt a strict statutory construction that requires present charitable use,²²⁸ others are more lenient in this requirement.²²⁹ A further divide exists within these broader categories, with states placing varying emphasis on exclusivity, ownership, and construction.²³⁰ In short, the muddled exemption provisions for charitable property allow for little predictability or transparency. As a result, Nonprofit Z, with properties in multiple states will be hard-pressed to determine and budget for property taxes. Since simplicity demands that the purpose of a tax policy, including who pays and who does not, be presented in an open fashion,²³¹ the current taxation provisions for vacant, charitable property are inconsistent with this principle. This problem can only be solved by simplifying the exemption provisions of nonprofits across the United States. Thus, it is necessary to uniformly ease the property exemption requirements in each state.

2. *Advocating for Action*

Unifying nonprofit exemption provisions across all fifty states will require assistance from national lobbying organizations such as the Uniform Law Commission (ULC) or the America Bar Association (ABA). The ULC “provides states with nonpartisan, well conceived and well-drafted legislation that brings clarity and stability to critical areas of state

223. C. EUGENE STEUERLE, *CONTEMPORARY U.S. TAX POLICY* 14–15 (2d ed. 2008).

224. Plain Writing Act of 2010, Pub. L. No. 111-274, 124 Stat. 2861.

225. *Id.* § 4(b), 124 Stat. 2862.

226. Barack Obama, U.S. President, State of the Union Address (Jan. 25, 2011), *transcribed in* 157 CONG. REC. 461 (2011).

227. STEUERLE, *supra* note 223, at 15.

228. *See supra* Part III.A.

229. *See supra* Part III.B.

230. *See supra* Part III.A.

231. STEUERLE, *supra* note 223, at 15.

statutory law.”²³² The ULC has strengthened federalism “by providing rules and procedures that are consistent from state to state” since 1892.²³³ Similarly, the ABA distributes reports and policies on legal issues that are read by lawyers and governments throughout the world.²³⁴ Together, these organizations have advocated for uniformity in areas of the law that were once drastically segmented.²³⁵ It is inevitable that all states will not be amenable to the national simplification of nonprofit tax law; the support of the ULC and the ABA, however, will be a critical element in combating this problem.

*B. Step 2: Broad Statutory Interpretation
and Fallow Property Exemption*

Some scholars argue that a contemporary design to nonprofit taxation requires nonprofit exemption provisions to be interpreted strictly.²³⁶ They assert that nonprofits have transformed into businesses and must therefore bear a proportionate share of the state’s tax burden.²³⁷ These views, however, are inconsistent with the tradition and history of nonprofit taxation, and they fail to advance an efficient business purpose. This Section explains that, especially at a time when the effects of the 2008 financial crisis are threatening the success of nonprofit organizations,²³⁸ nonprofit taxation policy must remain consistent with these two well-developed policies.

1. The Presence of Tradition: Excluding Fallow Nonprofit Property from Taxation Is Consistent with Tradition

Three legal theories exist that explain why property tax exemptions are a necessary element in contemporary tax policy.²³⁹ Although these theories are interrelated to a degree, they each offer a distinct rationale of why modern U.S. society requires a charitable property exemption and ultimately explain why this exemption should extend to fallow charitable property, an interpretation more consistent with states that have adopted a broad statutory construction.

232. *About the ULC*, UNIF. LAW COMM’N, <http://nccusl.org/Narrative.aspx?title=About%20the%20ULC> (last visited Nov. 1, 2011).

233. *Id.*

234. *About the ABA*, A.B.A., http://www.americanbar.org/utility/about_the_aba.html (last visited Nov. 1, 2011).

235. See UNIF. LAW COMM’N, *supra* note 232. For example, as of September 12, 2011, the Uniform Adult Guardianship and Protective Proceedings Jurisdiction Act had become the law in thirty-one states. Adult Guardianship and Protective Proceedings Jurisdiction Act, UNIF. LAW COMM’N, <http://www.uniformlaws.org/Act.aspx?title=Adult%20Guardianship%20and%20Protective%20Proceedings%20Jurisdiction%20Act> (last visited Nov. 1, 2011).

236. See Brody, *supra* note 30, at ix.

237. *Id.* at xi.

238. See *supra* notes 45–52 and accompanying text.

239. See Evelyn Brody, *Legal Theories of Tax Exemption: A Sovereignty Perspective*, in PROPERTY-TAX EXEMPTION FOR CHARITIES, *supra* note 30, at 145, 146.

The first explanation for the existence of a charitable property tax exemption is historic tradition. Since the inception of the United States, nonprofits have been free from taxation as a result of multiple political trends.²⁴⁰ First, the property tax was levied against income-producing land to generate revenue for state and local governments.²⁴¹ Thus, land which produced no income was free from taxation because taxing it would provide little benefit to the state.²⁴² Unoccupied land as well as the land of charities and churches was free from taxation because states did not wish to “seek fiscal blood from a stone.”²⁴³ Historically, property owned by “seats of government, state or municipal, highways, parks, churches, public school houses, [and] colleges” was outside the scope of taxation because these organizations did not raise profit for investors but used earnings to further the “common good.”²⁴⁴ This philosophy still applies today. Nonprofit organizations do not retain their profits, instead using them to further their organization’s cause.²⁴⁵ Taxing charitable property, including that which is fallow, may threaten to cripple the charitable organization that owns the property.

Second, charitable property tax exemptions were allowed because the practice was “so entirely in accord with the public sentiment.”²⁴⁶ The United States respects its charitable organizations and the work that they do.²⁴⁷ Thus, statutory exemptions are inspired by the “almost universal, innate promptings of the human heart.”²⁴⁸ This sentiment remains a contemporary one. The United States sees nonprofits as self-sacrificing and believes that taxing charitable property would diminish the “warm glow” that such organizations are capable of producing.²⁴⁹ As such, taxing vacant charitable property would be inconsistent with this timeless principle.

Even if history did not play a role in a state’s decision to grant property tax exemption, scholars have argued that policymakers of today might still choose to design a charitable tax exemption system.²⁵⁰ The inevitability of charitable tax exemption for the nonprofit sector is grounded in a “sovereignty view.”²⁵¹ According to Evelyn Brody,²⁵² a scholar

240. Diamond, *supra* note 218, at 118–39.

241. *Id.* at 119.

242. *See id.*

243. *Id.*

244. *See* Yale Univ. v. New Haven, 42 A. 87, 91 (Conn. 1899).

245. OSTER, *supra* note 39, at 19.

246. Diamond, *supra* note 218, at 121 (citation omitted).

247. *See* Brian Galle, *Keep Charity Charitable*, 88 TEX. L. REV. 1213, 1222–23 (2010).

248. Diamond, *supra* note 218, at 121 (citation omitted).

249. Galle, *supra* note 247, at 1222.

250. *See* Brody, *supra* note 239, at 146. The fact that exemption provisions can be repealed is the basis for this argument. *Id.*

251. *Id.*

252. Brody currently teaches nonprofit law at Chicago Kent College of Law. She has edited and coauthored books on property tax law and charities and is a member of the Association for Research on Nonprofit Organizations and Voluntary Action. *Faculty Spotlight: Evelyn Brody Professor of Law*,

and professor specializing in nonprofit tax law, the sovereignty view manifests itself in two theories of exemption: base definition and subsidy.²⁵³ Both of these theories explain that “[f]or all its imprecision, tax exemption keeps government out of the charities’ day-to-day business, and keeps charity out of the business of petitioning government for subvention.”²⁵⁴

The base-defining theory is premised upon the idea that charitable activity does not advance to the standard of taxable activity. Although property tax revenue is a reliable source of local government capital,²⁵⁵ they have never relied upon receipt of charitable funds in calculating their budget.²⁵⁶ Thus, nonprofits “cannot be exceptions from a rule in which [they] were never included.”²⁵⁷ Moreover, if nonprofit organizations were assessed a property tax, it would burden the organization’s beneficiaries, donors, and employees.²⁵⁸ Because these beneficiaries are often low-income individuals, “any tax rate other than zero could be viewed as too high.”²⁵⁹ Broadly construing exemption provisions spares the indigent from unnecessary burdens without depriving state governments of anticipated funds.

Critics of the base-defining theory dismiss the idea of former reliance and consider nonprofits as an untapped resource with which to increase municipal revenue, thereby expanding government services.²⁶⁰ Implicit in this assumption, however, is the idea that governments fully and efficiently use their tax-derived revenues. This is not always the case.²⁶¹ Oftentimes, a private enterprise familiar with a local community can manage assets more efficiently and comport with a greater public good.²⁶² Indeed, nonprofits *are* the U.S. community and are thus more familiar with the needs of their specific community members than for-profit firms participating in a similar enterprise.²⁶³ This intimate relationship allows nonprofits to responsibly manage proceeds and budget re-

CHICAGO-KENT C.L., http://www.kentlaw.edu/faculty/spotlight/brody_03-03.html (last visited Nov. 1, 2011).

253. Brody, *supra* note 239, at 146.

254. *Id.*

255. Gallagher, *supra* note 72, at 3.

256. *See supra* note 240 and accompanying text.

257. Brody, *supra* note 239, at 147 (quoting *Yale Univ. v. New Haven*, 42 A. 87, 91 (Conn. 1899)).

258. *Id.* at 148 (citation omitted).

259. *Id.* (citation omitted). This theory is consistent with the view that income tax notions should support the base theory. Because low-income taxpayers pay little tax, organizations which serve them should be taxed in a similar fashion. *Id.* at 148–49.

260. *See* Gallagher, *supra* note 72, at 19; Wangness, *supra* note 17.

261. Vito Tanzi & Tej Prakash, *The Cost of Government and the Misuse of Public Assets* 3 (Int’l Monetary Fund, Working Paper No. 00/180, 2000).

262. *See* Henry B. Hansmann, *The Role of Nonprofit Enterprise*, 89 *YALE L.J.* 835, 895 (1980).

263. *See* John W. Gardner, *The Independent Sector*, in *AMERICA’S VOLUNTARY SPIRIT* ix, xii–xiv (Brian O’Connell ed., 1983), reprinted in JAMES J. FISHMAN & STEPHEN SCHWARZ, *TAXATION OF NONPROFIT ORGANIZATIONS: CASES AND MATERIALS* 5 (3d ed. 2010) (“To deal effectively with the ailments of our society today, individual initiative isn’t enough, there has to be some way of linking the individual with the community. In the independent sector, such linkages are easily forged. Citizens banding together can tackle a small neighborhood problem or a great national issue.”).

sources. Thus, providing revenue to the government through property taxes is often inefficient.

The second half of the sovereignty view explains charitable exemption as a government subsidy. Exemptions are frequently used to induce donations and motivate a nonprofit to engage in certain behaviors.²⁶⁴ The exemption often obligates a charitable organization “to carry out an agreed upon mission” that is consistent with public welfare.²⁶⁵ In such cases, a state grants exemption because charities lessen the burdens of the government, creating a classic *quid pro quo* scenario.²⁶⁶ Although the state loses tax revenue through this arrangement, the disadvantage of lost revenue may be surpassed by the advantage of producing a charitable activity that would otherwise be absent.²⁶⁷ Nonprofits owning vacant property continue to engage in charitable work outside the walls or boundary lines of their vacant property holdings.²⁶⁸ This is especially true today when hospitals, schools, churches, and arts organizations close some of their buildings yet continue to provide services highly demanded by the communities which they assist.²⁶⁹ Interpreting charitable exemption provisions broadly maximizes the number of nonprofits subsidized by states and decreases the burdens of local governments. Further, a broad interpretation of exemption provisions permits charities to expand the scope of their services because a portion of their limited income is not automatically allocated to tax bills.²⁷⁰

This Subsection has demonstrated that states which interpret charitable exemption clauses broadly adopt a policy consistent with historic tax traditions and the principles underlying exemption privileges, promoting the efficiency of nonprofits. Thus, states should adopt a broad interpretation of charitable use, abandoning property taxes assessed on fallow nonprofit property.

2. *The Absence of Purpose: Taxing Fallow Nonprofit Property Does Not Advance a Business Purpose*

As nonprofits increase the scope of their charitable purpose, many have also increased their engagement in commercial activity.²⁷¹ These nonprofits attempt to “get ahead” by participating in the same commercial activities as their for-profit counterparts.²⁷² In response to this trend,

264. Brody, *supra* note 239, at 149.

265. HERRINGTON J. BRYCE, PLAYERS IN THE PUBLIC POLICY PROCESS: NONPROFITS AS SOCIAL CAPITAL AND AGENTS 75 (2005).

266. Brody, *supra* note 239, at 149.

267. *Id.* at 165.

268. *See supra* notes 15–16 and accompanying text.

269. *See supra* notes 45–52 and accompanying text.

270. *See* Joseph J. Cordes et al., *What Is the Property-Tax Exemption Worth?*, in PROPERTY-TAX EXEMPTION FOR CHARITIES, *supra* note 30, at 81, 81.

271. Burton A. Weisbrod, *The Nonprofit Mission and Its Financing: Growing Links Between Nonprofits and the Rest of the Economy*, in TO PROFIT OR NOT TO PROFIT, *supra* note 119, at 1, 1.

272. *Id.* at 3.

Congress enacted Unrelated Business Taxable Income (UBIT), a tax on activities by nonprofits that do not accord with their charitable purposes.²⁷³ An analysis of the tax policy and doctrine surrounding the IRS's taxation of business income not only applies, by analogy, to the taxation of nonprofit property, but it also proves that there is no legitimate business purpose for assessing a tax on fallow nonprofit property.

Exempt organizations engage directly in commercial activities when the returns from such activity produce a premium greater than that which the nonprofit can earn from passive investment²⁷⁴ or when the nonprofit captures a premium by avoiding the corporate income tax.²⁷⁵ The IRS responded to the nonprofit sector's pursuit of commercial profit in 1950 when it enacted UBIT.²⁷⁶ Although the legal doctrine concerning UBIT has been described as "a morass,"²⁷⁷ several IRS rules emerge from the confusion. First, "[a]n exempt organization is not taxed on its income from an activity substantially related to the charitable, educational, or other purpose that is the basis for the organization's exemption."²⁷⁸ Second, "if an exempt organization regularly carries on a trade or business not substantially related to its exempt purpose . . . the organization is subject to tax on its income from that unrelated trade or business."²⁷⁹ Third, a "trade or business generally includes an activity carried on for the production of income from selling goods or performing services."²⁸⁰ Finally, UBIT activities must "show a frequency and continuity"²⁸¹ and must not contribute in size or extent to the exempt function that a nonprofit is intending to serve.²⁸²

The IRS (along with tax practitioners and academics such as Professor John Colombo) justifies these rules with multiple policy arguments.²⁸³

273. See Revenue Act of 1950, ch. 994 § 422, 64 Stat. 906, 948–50 (codified as amended at I.R.C. §§ 502, 511–13 (2000)); DEP'T OF THE TREASURY, TAX ON UNRELATED BUSINESS INCOME OF EXEMPT ORGANIZATIONS 1 (2010), www.irs.gov/pub/irs-pdf/p598.pdf (describing current UBIT regulation).

274. John D. Colombo, *Commercial Activity and Charitable Tax Exemption*, 44 WM. & MARY L. REV. 487, 526–27 (2002) ("[E]xempt charities may have excess capacity from capital investments made to pursue [its] charitable mission that can be used to produce commercial revenues at costs below those incurred by for-profit firms.").

275. *Id.* at 527–29.

276. See Revenue Act of 1950, ch. 994 § 422, 64 Stat. 906, 948–50 (codified as amended at I.R.C. §§ 502, 511–13 (2000)).

277. Colombo, *supra* note 274, at 497.

278. DEP'T OF THE TREASURY, *supra* note 273, at 1. See also Colombo, *supra* note 274, at 497 ("Put another way, the regulations appear to say that if commercial activity is conducted directly by an exempt organization but is 'insubstantial' in relation to the exempt organization's charitable activities, the commercial activity will not affect exempt status. If the commercial activity is substantial, however, then it potentially jeopardizes exempt status, unless the activity is 'in furtherance of' the entity's exempt purpose.").

279. DEP'T OF THE TREASURY, *supra*, note 273, at 1.

280. *Id.* at 3 (internal quotation marks omitted).

281. *Id.* at 3. "Business activities of an exempt organization ordinarily are considered regularly carried on if they show a frequency and continuity, and are pursued in a manner similar to comparable commercial activities of nonexempt organizations." *Id.*

282. *Id.*

283. See Colombo, *supra* note 274, at 529–46.

First, UBIT combats unfair competition between nonprofit and for-profit firms in similar industries when the nonprofit firm uses the economic benefits of exemption to subsidize commercial activity.²⁸⁴ Second, UBIT protects the tax base.²⁸⁵ Third, UBIT discourages commercial activity from diverting the attention of nonprofit managers and resources away from the organization's primary charitable purpose.²⁸⁶ Fourth, UBIT decreases the inefficiency in capital markets that results when nonprofits are not solely focusing production on charitable output.²⁸⁷ Finally, UBIT exists as a way to protect charitable assets from undue risk.²⁸⁸

Although UBIT policies address the taxation of business income, it follows that the analysis can apply to the taxation of property used for a business purpose. If this inference is made, the only policy rationale for assessing a nonprofit organization a property tax exists when the nonprofit is seeking a financial return through the commercial use of the property. The nonprofits described throughout this Note are merely owners of abandoned or vacant property that is not used for *any* purpose, let alone a *commercial* purpose. The property owners are not engaging in unfair competition, adjusting the tax base, diverting the attention of resources, affecting the efficiency of capital markets, or assuming undue risk.²⁸⁹ Instead, they are attempting to survive the aftermath of a financial crisis while continuing to serve their communities. As such, states should not assess them a property tax.

It has been said that “[p]roperty tax consistently ranks as one of the most unpopular taxes in America.”²⁹⁰ This is because the tax is “highly visible, can be inconvenient to pay, and is based on an assessment process that may be, or seem to be, biased and unfair.”²⁹¹ This Part has demonstrated that continuing to assess property taxes on fallow, charitable property will perpetuate a trend of inconsistency and unpredictability

284. *Id.* at 529–30. “An example would be a sort of ‘predatory pricing’ in which an exempt organization prices its product below its competitors because it does not have to recoup the costs of taxation.” *Id.* at 530. “[E]ven though unfair competition was the primary rationale for enacting the UBIT,” it is an insignificant concern in practice. *Id.* This is because “there is little incentive for [non-profit] organizations to subsidize the expansion of commercial activities with the tax savings incurred by exemption.” *Id.*

285. *Id.* at 532. The UBIT, however, does not sufficiently protect the tax base. *Id.* First, “related” activities are sometimes not taxed at all. *Id.* Second, profit-producing activities can be exempted from the UBIT. *Id.* Third, charities disproportionately allocate “unrelated” business activities in order to decrease tax liability. *Id.*

286. *Id.* at 534–35. Professor Colombo calls this the “diversion problem.” *Id.*

287. *Id.* at 538. The basis of this argument is that without UBIT, “all corporate enterprises would be worth more in the hands of an exempt charity, which could avoid the corporate income tax, than in the hands of private investors.” *Id.* at 540; *see also* Henry B. Hansmann, *Unfair Competition and the Unrelated Business Income Tax*, 75 VA. L. REV. 605, 614–15 (1989).

288. If an exempt nonprofit directly engages in commercial activity, charitable assets may be lost in the pursuit of such extraneous activities. Colombo, *supra* note 274, at 544. Here, UBIT is another way to “funnel” commercial activity into “separate corporate containers,” thereby creating one more barrier to nonprofit liability. *Id.* at 545.

289. *See supra* notes 284–88 and accompanying text.

290. Gallagher, *supra* note 72, at 3.

291. *Id.*

that is contrary to tax tradition and lacks a business purpose. The only solution for achieving a transparency and consistency in the realm of nonprofit exemption provisions is for all fifty states to adopt a policy of broad statutory construction.

V. CONCLUSION

President Barack Obama once said, “We. . . need to invest in ideas that can help us meet our common challenges, because more often than not, the next great social innovation won’t be generated by the government [but by the nonprofit sector].”²⁹² The nonprofit sector has played an important role in developing the United States’ past, and is expected to serve its future.²⁹³ Accordingly, both the federal government and the states must employ contemporary and simplistic taxation policies that allow nonprofit organizations to best serve their charitable purposes. In regards to the exemption of fallow nonprofit property, such a policy requires all fifty states to broadly construe charitable use, thereby allowing property exemption. Because the entire nonprofit sector is suffering the strains of the 2008 financial crisis, this approach is necessary to maintain the vitality of the nonprofit sector and to protect the millions served by its breadth.²⁹⁴

292. Barack Obama, U.S. President, Colorado Springs Campaign Speech (July 2, 2008), *available at Full Transcript of Obama’s Prepared Remarks*, DENVER POST (July 2, 2008, 11:38 AM), http://www.denverpost.com/breakingnews/ci_9765136.

293. *See id.*

“There is a lesson to be learned from generations who have served. . . . It’s the lesson that in America, each of us is free to seek our own dreams, but we must also serve a common purpose, a higher purpose. When you choose to serve . . . you are connected to that fundamental American ideal that we want Life, Liberty and the Pursuit of Happiness not just for ourselves, but for all Americans. That is why this is a great nation. Because time and again, Americans have been willing to serve on stages both great and small; to draw on the same spirit that launched America’s improbable journey to meet the challenges of each defining moment in our history.”

Id.

294. Although this Note has primarily used examples of churches, it is important to realize that these same concepts can be applied to each segment of the nonprofit sector. For an analysis on the breadth of these sectors, see *supra* Part II.A.

