

RELIGIOUS PROPERTY TAX EXEMPTIONS: A STICKY ISSUE

BY DARREN MOORE

Last week an article appeared on Forbes online that caught my attention. The article discussed a Tennessee case in which a megachurch sought (ultimately unsuccessfully) property tax exemption for portions of its real property used for a bookstore and a fitness center. You can read more of the details in the article.

Essentially the church argued that part of its religious worship was operation of these facilities to create a “third space” environment. Many churches are engaging in such activities – bookstores, fitness centers, coffee shops, etc. The question of taxation is often analyzed from a federal income tax standpoint. Are these activities related or unrelated to the church’s exempt purpose? If unrelated, are they substantial? If unrelated are there exceptions to payment of unrelated business income tax (such as being operated for the benefit of members only, being operated by volunteers, etc.)? What is often (and unfortunately so) overlooked is property tax exemption, a very important benefit for churches.



Property tax exemption does not track federal tax exemption. It is a different scheme altogether. Each state is responsible for determining how it will tax (or exempt) various institutions. In my home state of Texas, for example, churches are exempt but a 501(c)(3) animal rescue clinic is not. The specific state statute has to be consulted to determine eligibility for property tax

exemption. Again, in Texas, for example, among other things churches may seek exemption of real property owned by the church and used as a place of regular religious worship but only as to that portion of the property reasonably necessary for engaging in religious worship. Most observers would agree this includes the church sanctuary. But what else? The choir rehearsal room? The fellowship hall? The church offices? The green space behind the church used for the annual Easter Carnival? These are issues that require interpretation. Likewise, the question of a church bookstore and fitness center require interpretation. The problem arises because the First Amendment makes it a little sticky for a local county official (the tax assessor initially and later the court) to interpret whether these ancillary areas are “reasonably necessary” for engaging in religious worship.

This problem isn’t isolated to property tax issues. In fact, while the Internal Revenue Code recognizes an exemption from federal income tax for religious organizations, neither the Internal Revenue Code nor the

Treasury Regulations define the term “religious.” Likewise, the term “church” is found, but not defined, in the Internal Revenue Code. The IRS has tackled the question by looking at a number of factors that it considers indicia of being a church (in Stephen Colbert-speak: evidence of churchiness). Courts have likewise looked to such “indicia.” But in these instances, the IRS and/or the courts are merely trying to determine whether the organization itself – in totality – is a church. The local tax assessor has a much more difficult (constitutionally-speaking) question: are specific areas reasonably necessary for engaging in religious worship which begs the question of whether the activities undertaken in those areas is, in fact, religious worship. That’s sticky.

And so we are left with an ad hoc state by state (if not county by county) analysis of religious property tax exemption. One solution would be to draw a bright line: no exemption at all or exemption only for the primary sanctuary. An alternative would be to base property tax exemption on whether the property is used for a related purpose utilizing the body of law that has developed under Section 513 of the Internal Revenue Code with respect to unrelated business income. Either would be better than spending the nonprofit’s money and the government’s money on legal fees and court costs.

Until then, though, don’t neglect concern for property tax exemption and consult a local lawyer who can tell you the “lay of the land” in your specific county.