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POSITION PAPER

Should Religious Institutions Be Required to File Form 990s? (Issue No. 4)

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The 2011 Grassley staff report claims that the United States Constitution "does not require the government to exempt churches from federal income taxation or from filing tax and information returns."[1] Rather, according to the report, exemption and any potential information return requirements fall within constitutional boundaries as privileges, not rights.[2] This position paper responds to these assertions, as set forth in the Committee report[3] and as framed in Issue No. 4 by the Commission on Accountability and Policy for Religious Organizations:

- Should churches be required to file Form 990 unless they meet special criteria as described in the staff report?
- Would such filing exceptions be feasible without violating constitutional principles?
- Should churches be required to file an "e-postcard" or similar document with the IRS annually?[4]

Somewhat ironically, the Committee report notes the testimony of Congressman Rangel concerning the U.S. Constitution's interplay with religious institutions' exemption from IRS annual information return requirements:

[1]Staff report to Senator Charles Grassley (R-IA) dated Jan. 6, 2011, regarding review of media-based ministries, at 17 (hereinafter "Committee report").

[2]Id. at 18.

[3]See id. at 33.

[4]The word "church" is often used as a term of convenience to encompass churches, synagogues, mosques, temples, and other houses of worship. In this paper, such houses of worship shall be referred to as "religious institutions" or "religious organizations," and are distinguishable from other organizations that include religious aspects as components of their activities and are subject to Form 990 filing requirements.

> What in God's name could be even remotely considered a violation of the constitutional right of churches to say that they should file an annual report as to how much money they got and what they did with it?[5]

Au contraire! Or, in the American vernacular, not so fast! While perhaps seemingly innocuous to some, this issue strikes at the heart of fundamental religious liberties that our country has held dear throughout its history, as reflected in over 200 years of tax exemption and freedom consistently accorded to religious institutions as a matter of constitutional right.

This paper is produced from the authors' perspectives as legal practitioners engaged in the daily work of representing hundreds of religious institutions and other tax-exempt organizations, and particularly with respect to specific components of the IRS Form 990 itself. The authors believe that the federal imposition of initial and ongoing IRS Form 990 reporting requirements upon U.S. religious institutions would violate the First Amendment. Further, such significant changes would be contrary to long established social policies, which predate the U.S. Constitution, reflecting the importance of keeping religious institutions separate and apart from governmental oversight and taxation.

A. Historical Background on Religious Institutions' Exemption from Taxation.

1. Historical Religious Tax Exemption Generally.

Since before our country began, its religious institutions have been exempt from taxes. Such treatment is consistent with worldwide historical treatment of religious institutions as exempt.[6] As the U.S. Supreme Court observed in the landmark case of *Walz v. Tax Commission:*

> Few concepts are more deeply embedded in the fabric of our national life beginning with pre-revolutionary colonial times, than for the government to exercise at the very least this kind of benevolent neutrality toward churches and religious exercise generally, so long as none was favored over others and none suffered interference.[7]

As U.S. Supreme Court Justice O'Connor further observed, the early American leaders "accorded religious exercise a special constitutional status," with all agreeing that "government interference in religious practice was not to be lightly countenanced."[8]

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[5] Id. at 19 (quoting Federal Tax Rules Applicable to Tax-Exempt Organizations Involving Television Ministries Hearing Before Subcomm. on Oversight of House Committee on Ways and Means, 100th Cong. 54-55 (1987)).

[6] See, e.g., S. Diamond, *Efficiency and Benevolence: Philanthropic Tax Exemptions in 19th Century America*, E. Brody, *Legal Theories of Tax Exemption: A Sovereignty Perspective*, D. Dessingue, *The Special Case of Churches*, all collected in Property-Tax Exemption for Charities (E. Brody, ed.) (2002); R. Rodes, Jr., The Last Days of Erastianism: Forms in the American Church-State Nexus, 62 Harv. Theo. Rev. 301, 317 (1969) ("Churches have been wholly or partially exempt from secular taxes since the time of Constantine at least; only the most rigorous ideologues feel that such exemption violates state or federal constitutional provisions.").

[7] 397 U.S. 664, 676, 90 S. Ct. 1405, 1415 (1970).

[8] City of Boerne v. Flores, 521 U.S. 507, 564 (1997) (O'Connor, J., dissenting) (citing A. Adams and C. Emmerich, A Nation Dedicated to Religious Liberty: The Constitutional Heritage of the Religious Clauses, at 31

Two critical tax principles are implicated here. First as Justice Marshall famously pointed out long ago, "the power to tax involves the power to destroy."[9] Second, the power to tax is that of a sovereign. Religious institutions may be subject to the sovereign in limited ways (e.g., payroll taxes, health and safety regulations), but all such intrusions must be strictly scrutinized and guarded against overreaching.[10]

2. Historical Religious Tax Exemptions as Codified in Federal Income Tax Legislation.

While the protection of religious liberty has long been part of our country's legal fabric, it was only a little over a century ago that Congress first imposed an income tax on corporate entities. In doing so, Congress specifically exempted "corporations, companies, or associations organized and conducted solely for charitable, religious, or educational purposes."[11] Following the 1909 Revenue Act and the ratification of the Sixteenth Amendment, such exemption was maintained in the Revenue Act of 1913.[12]

No information returns whatsoever were required for any tax-exempt organizations until the 1943 Revenue Act. Again, the new law specifically exempted "religious organization[s]" and organization[s] ... operated, supervised, or controlled by or in connection with a religious organization."[13] Over the next several years, new laws were passed to impose taxes and related reporting requirements on unrelated business activities of all tax-exempt organizations, including religious institutions.[14] The rationale for applying these new legal requirements to religious

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(1990)). See also Hosanna-Tabor Evangelical Lutheran Church and School v. EEOC, 565 U.S. ____ (Jan. 11, 2012), slip. op. at 9 (citing the U.S. Constitution's "scrupulous policy [] in guarding against a political interference with religious affairs") (quoting J. Madison, Letter to Bishop Carroll dated Nov. 20, 1806).

[9]McCulloch v. Maryland, 17 U.S. 316, 431 (1819). See also Murdock v. Pennsylvania, 319 U.S. 105, 112 (1943) ("The power to tax the exercise of a privilege is the power to control or suppress its enjoyment.").

[10]The question of whether all organizations presently tax-exempt under Section 501(c)(3) must or should continue to be exempt from income taxes is beyond the scope of this article. Nevertheless, it has been persuasively argued among constitutional scholars that for such purposes, religious institutions are qualitatively different and therefore are exempt from income taxes as a constitutional right, not a privilege. See, e.g., K. Halcom, Taxing God, 38 McGeorge L. Rev. 729, 765-66, 772-73 (2007); Goodwin, Would Caesar Tax God? The Constitutionality of Governmental Taxation of Churches, 35 Drake L. Rev. 383, 384 (1985). See also, Walz, 397 U.S. at 676 ("All of the 50 states provide for tax exemption of places of worship, most of them doing so by constitutional guarantees. For so long as federal income taxes have had any potential impact on churches - over 75 years - religious organizations have been expressly exempt from the tax.").

[11]Revenue Act of 1894,Ch. 349, 332, 28 Stat. 509, 556 (declared unconstitutional in Pollock v. Farmers' Loan & Trust Co., 157 U.S. 429, *aff'd on rehearing,* 158 U.S. 601 (1894)). See also Revenue Act of 1909, 27 Ch. 6, § 38, 36 Stat. 11, 112 (1909).

[12]Ch. 16, 38 Stat. 114.

[13]Revenue Act of 1943, Ch. 63, 58 Stat. 21, 37. Whether the latter category of religious organizations - i.e., integrated auxiliaries - should enjoy identical tax exemption privileges as churches is not separately addressed in this paper.

[14]Revenue Act of 1950, ch. 994, 64 Stat. 906, 948; Tax Reform Act of 1969, Pub. L. 91-172, 83 Stat. 487, 494-96.

institutions is that such commercial activity is qualitatively different from sacerdotal functions and religious worship. Such activity therefore operates to remove otherwise applicable First Amendment protections, but solely for such commercial, non-religious activities.[15]

For purposes of this paper, the Tax Reform Act of 1969 is notable in the following two respects, each of which reflects a continuing deference to religious institutions as being autonomous and free from governmental intrusion (except, as stated above, for commercial activities). First, the 1969 Act added Section 508 to the Internal Revenue Code, requiring new nonprofit organizations to apply for an official determination of tax-exempt status *except for* religious institutions, their integrated auxiliaries, and conventions or associations of churches (i.e., non-hierarchal churches).[16] Second, the 1969 Act imposed new annual information return requirements on schools, colleges, and publically supported charities. Again, however, the new law reaffirmed the exemption requirement for religious institutions, their integrated auxiliaries, and conventions or associations of churches.[17]

B. Summary of Constitutional Issues with Form 990 Reporting Requirements for Religious Institutions.

Fast forward to 2012. In the wake of financially successful "megachurches" and scandals involving abuse of religious institutions, demands have been made for unprecedented stepped-up IRS scrutiny of religious institutions and specifically through the vehicle of IRS Form 990 reporting.[18] Whether such demands are borne of religious animus or not is unknown.

As a constitutional matter, must religious institutions be exempt from annual Form 990 information reporting requirements and the initial IRS registration requirements? Should they be, based on policy considerations? Key reasons that such requirements should, and perhaps even may not, apply to religious institutions is that (1) they are problematic under the Free Exercise Clause of the First Amendment, (2) they run afoul of excessive entanglement issues under the First Amendment, and (3) they are otherwise incompatible with the fundamental nature of religious bodies. Moreover, to the extent concerns of tax abuse exist – as demonstrated by some "bad apples" – extensive compliance and enforcement tools already exist for addressing these matters. These tools include such as separate reporting requirements and penalties for certain taxes as well as civil and criminal laws prohibiting fraud and other egregious misconduct. Accordingly, such unprecedented IRS reporting requirements should not now be imposed on all religious institutions.

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[15] See Treas. Reg. § 1.511-2(a)(3)(ii); Walz v. Tax Commission, 397 U.S. 664 (1970).

[16] See Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487, 494-96.

[17] See id. 83 Stat. at 519-23.

[18] See Committee report at 24-26, 30-31.

C. Untenable Violations of the First Amendment Free Exercise Clause, Through the Chilling Effects of IRS Registration and Form 990 Reporting Requirements.

The Free Exercise Clause of the First Amendment is intended to protect religious liberty by prohibiting invasions thereof by the government.[19] Consequently, even a regulation that is neutral on its face may, in its application, offend constitutional neutrality if it unduly burdens the free exercise of religion.[20] The relevant inquiry is thus whether the government has placed a substantial burden on religious belief or practice and, if so, whether a compelling governmental interest justifies the burden.[21] Given the extensive compliance and enforcement tools that already exist to address financial improprieties within religious institutions, as well as the clear constitutional protections accorded to religious freedom, the authors are hard pressed to understand what new government interest is so compelling as to justify imposing mandatory registration and reporting requirements for all religious institutions, particularly in light of the serious potential chilling effects on religious bodies.

Requiring compulsory government-registered religious institutions is starkly inconsistent with U.S. history and the spirit, if not the letter, of the First Amendment itself. They are already responsible to local, state, and federal government for legitimate purposes, such as fire code safety, payroll taxes and other employee-related matters, and other areas involving laws that are directly applicable to them. The concept that religious institutions must prove to the IRS - the *tax*-enforcement government agency - that they are sufficiently "religious" smacks of other governmental regimes that have typically hostile to religious liberties (e.g., communism and fascism) and largely abhorrent to U.S. citizens. The intent may or may not be to threaten religious freedom, but the effect of doing so is certainly sufficient to render IRS church reporting requirements constitutionally suspect under the Free Exercise Clause.

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[19] Jimmy Swaggert Ministries v. Board of Equalization of California, 493 U.S. 378, 384, 110 S. Ct. 688, 693 (1990) (citing Abington School Dist. v. Schempp, 374 U.S. 203, 222-23 (1963)).

[20] Id. (citing Wisconsin v. Yoder, 406 U.S. 205, 220 (1972)).

[21] Id. (citing Hernandez v. Commissioner, 490 U.S. 680, 699 (1989) (citations omitted)). See also Walz. 397 U.S. at 669, 90 S. Ct. at 1411 (fundamental purpose of the First Amendment is "to insure that no religion be sponsored... and none inhibited . . . [The U.S. Supreme Court] will not tolerate... governmental interference with religion."). See also Employment Division, Department of Human Resources of Oregon v. Smith, 494 U.S. 872, 905, 110 S. Ct. 1595, 1614 (1990) (Compelling government interest regarding criminal use of peyote, an illegal drug, warranted any resulting burden on religious interests: "The compelling interest test effectuates the First Amendment's command that religious liberty is an independent liberty, that it occupies a preferred position, and that the Court will not permit encroachment upon this liberty, whether direct or indirect, unless required by clear and compelling governmental interests of the highest order.") (O'Connor, J., concurring); and Gonzales v. O Centro Espirita Beneficente Uniao do Vegetal, 546 U.S. 418 , 424, 126 S. Ct. 1211, 1215-16 (2006) ("the Federal Government may not, as a statutory matter, substantially burden a person's exercise of religion," absent a showing of a compelling government interest and use of the least restrictive means available).

D. Impermissible Degree of Excessive Entanglement Under the Establishment Clause.

The Establishment Clause of the First Amendment exists to prevent the government from officially preferring one religion or denomination over another.[22] Under the Establishment Clause analysis, a legislative act involving religion must satisfy the three-pronged test as developed under Lemon v. Kurtzman[23] and its progeny. First, the law must have a secular purpose. Second, it must have a primary effect that neither advances nor inhibits religion. Third, it must not foster an "excessive government entanglement" with religion.[24] As further developed in Agostini v. Felton,[25] the entanglement prong remains highly relevant. The second prong also implicates the Free Exercise inquiry and raises additional concerns about the serious chilling effect of requiring all religious institutions to register and report regularly to government taxing authorities.

With respect to the excessive entanglement inquiry, the U.S. Supreme Court has acknowledged that some limited degree of entanglement is inherent, given churches' day-to-day operations that are affected by numerous areas of government regulation such as building, zoning, and health and safety regulations.[26] On the other hand, the Court has consistently rejected legislation that calls for a government inquiry into the religious nature of an activity or product.[27] Likewise, legislation involving a "comprehensive, discriminating, and continuing state surveillance" amounts to constitutionally impermissible "excessive entanglement."[28]

Religious institutions already interact with the government in a variety of ways; they are thus already somewhat "entangled." The relevant question under the Establishment Clause is thus whether regular Form 990 reporting (and requiring initial IRS registration) for religious institutions would unreasonably *increase* such entanglement to constitutionally impermissible levels.[29] In answering this question, as with the Free Exercise analysis, the overarching

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[22]K. Halcom, Taxing God, 38 McGeorge L. Rev. at 752 and n. 162 (2007) (citing Larson v. Valente, 456 U.S. 228, 244 (1982)).

[23]403 U.S. 602 (1971).

[24]Id. at 612-13 (quoting Walz v. Tax Commission, 397 U.S. 664, 674 (1970)).

[25]521 U.S. 203, 232-33 (1997).

[26]Lemon, 403 U.S. at 614; Hernandez v. Commissioner, 490 U.S. 680, 696-97 (1989) (citing Presbyterian Church in U.S. v. Mary Elizabeth Blue Hull Memorial Presbyterian Church, 393 U.S. 440, 451 (1969)); Tony and Susan Alamo Foundation v. Sec'y of Labor, 471 U.S. 290, 305-06 (1985); Jimmy Swaggert Ministries, 493 U.S. at 389.

[27]See, e.g., Lemon, 403 U.S. at 613, 620; Texas Monthly, Inc. v.Bullock, 489 U.S. 1, 17 (1989); Jimmy Swaggert Ministries, 493 U.S. at 396.

[28]Lemon, 403 U.S. at 619.

[29]See Walz, 397 U.S. at 674, 90 S. Ct. at 1414 ("The test is inescapably one of degree."). Indeed, the jurisprudential winds have blown in different directions during our country's history, but the continuing dangers are starkly evident from repeated political and legal efforts to keep religion "in" or "out," depending on the issue at hand.

constitutional principle must be kept in mind that the government must maintain some distance from religion.[30]

E. Constitutional Violations Resulting from Requiring Religious Institutions to Register with the IRS.

Our country has never required all religious institutions to register with the government. Why now? And why particularly from the federal taxing authority - the IRS? Religious organizations are inherently organic, made up of like-minded congregants seeking soul-saving and heart-felt opportunities for individual and communal expressions of faith. In contrast, the IRS's mandate is to oversee commercial activities and ensure that our country's coffers are properly filled. Several more questions thus demand satisfactory answers before an IRS reporting system for religious institutions could be constitutionally or otherwise imposed.

For example, would a religious institution lose its legitimacy if it failed to register with the IRS, such as recently occurred with other organizations that consecutively failed to file their Form 990s? Must a religious institution follow the IRS's now amplified rules about "good governance," as reflected in several Form 990 questions and purportedly reflective of legal compliance, as opposed to its own theological principles?[31] How can the government deny a religious institution the right to exist, without infringing on constitutional protections?

Moreover, of what real value and use would such registration information be to the federal government? What if the leaders in power were in fact hostile to religion? With such a registry, a plethora of opportunities would abound for potential discrimination and persecution, which likely would result in intolerable chilling effects. While such a requirement may seem relatively innocuous now, it invites and allows for misuse and discriminatory practices by government insiders such as regularly practiced in other less religiously tolerant countries. Religious persecution is endemic within human societies, and maintaining such registration information would provide more fodder for those hostile to religion.[32] As the U.S. Supreme Court once observed: "Governments have not always been tolerant of religious activity, and hostility toward religion has taken many shapes and forms - economic, political, and sometimes harshly oppressive."[33]

In contrast, no discernible benefit – much less a compelling government interest – can be readily identified from requiring and maintaining such lists. Indeed, such a requirement leads logically to the conclusion that a church must necessarily be government-sponsored, or at least

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[30] Lemon, 403 U.S. at 611-13.

[31] See *infra* at 9 and n.37.

[32] Of particular horrific note, Germany's churches and many of their leaders, including well known theologian Dietrich Bonhoeffer, faced extreme persecution and even death under the Nazi regime.

[33] Walz, 397 U.S. at 673, 90 S. Ct. at 1413. See also Everson v. Bd. of Educ., 330 U.S. 1, 11 (1947) ("The people [in Virginia], as elsewhere, reached the conviction that individual religious liberty could be achieved best under a government which was stripped of all power to tax, to support, or otherwise to assist any or all religious individual or group.").

government-approved, in order to be allowed to engage in religious worship activities. That step would be unprecedented in our country's history, and indeed unconstitutional under both the Establishment Clause and the Free Exercise Clause.

F. Constitutional Violations Resulting from Requiring Religious Institutions to File Form 990 Reports.

The IRS Form 990 exists in three versions: (1) the simplified IRS Form 990-N, which is a basic information "postcard" that functions essentially as a "heads-up" report to the IRS; (2) the IRS Form 990-EZ, which is a shortened version of the Form 990 and requires limited financial and other organizational information; and (3) the full-blown IRS Form 990, which has been significantly expanded in recent years.[34] For reasons stated above regarding initial IRS registration requirements, the Form 990-N – even in its very simplified format – would violate constitutional safeguards for religious institutions if required as a condition of any religious institution's legitimate existence. The Form 990-EZ would also be highly problematic for this reason, as well as for its additional required information disclosures that are substantially identical to those in the full version Form 990. The specific areas of inquiry in both the Form 990-EZ and the Form 990 further demonstrate the constitutional problems inherent in such reporting requirements as applied to religious institutions.

First, Part I of Form 990 calls for various "summary" information such as the organization's "mission or most significant activities." Presumably, a religious institution could simply report something like "spreading the gospel of Jesus Christ" or "promoting Hinduism." But why is this information relevant to the IRS? Perhaps it would be to assure the government that the reporting religious organization is indeed operating as permitted under section 501(c)(3). This argument is asserted in the Committee report as a purportedly compelling reason for government oversight through Form 990 reporting.[35] But a religious organization has *never* been obligated under the First Amendment to prove its legitimacy to the government as an ongoing, routine matter.[36] This rationale is thus clearly deficient. Other portions of the Form 990's "summary" (and corresponding portions of the Form 990-EZ) seek financial information to be expanded elsewhere in the Form 990, which is likewise problematic for the underlying information revealed, the potential chilling effects, and the abundant potential for resulting government intrusions and persecution of religious organizations and individuals. Moreover, any disclosed information that is truly of legitimate concern to the government can be obtained and addressed by other already existing means, as discussed further herein.

Part III of both Form 990 and Form 990-EZ asks for a description of the organizations "mission" and for descriptions of "each of the organizations three largest program services by expenses," including related financial information for such activities. Again, such questions call for unprecedented intrusion into the nature, function, benefits, and indeed the very heart of

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[34] See www.irs.gov for available Form 990s.

[35] See Committee report at 24-30.

[36] Cf. I.R.C. § 7611 (a religious institution may be required to defend its legitimacy, but only under a heightened governmental inquiry threshold).

religious organizations, which since before our country's formation have been uniformly viewed as far outside the purview of permissible government involvement.

The Form 990's and Form 990-EZ's broad, far-reaching questions in Part III about program activities and related expenses seek information in the latter category. Several other areas of Form 990 inquiry are likewise constitutionally suspect and practically problematic. For example, Questions 13 through 15, and 21 of Part IV, and their accompanying Schedules F and I, ask for information about foreign activity. Churches have long been involved with missionary activity in countries where, if known, people could be harmed and even killed, if information about such activities were known. Consider China for example. China reportedly has a large and expanding Christian population despite repeated and extensive government efforts to control and minimize such growth. With access to mission-minded churches' Form 990 information, which by law must be publically available, hostile foreign governments could make great inroads in ferreting out, punishing, and further persecuting religious converts. Just the possibility of such persecution would likely produce a chilling effect on religious institutions, resulting more restricted religious activities - i.e., less missions work in certain countries.

In addition, questions like number 10 through 15 of Part VI are of concern in terms of their potential to harm a religious organization's development or even bring into question its legitimacy. These questions are aimed at good governance practices, such as maintenance of document retention policies, whistleblower policies, conflict of interest policies, and compensation review practices. While these are all laudable areas for developing a well-run charitable organization, they cannot legally be prerequisites for a legally valid religious institution.[37]

Whereas negative answers on the Form 990 for other section 501(c)(3) charities may result in audits and possible sanctions, which could be helpful overall for improving their quality generally, the landscape is markedly different for religious institutions. Given their constitutional protection, questions about *governance* and not legitimacy, as a religious institution per se go too far under either the Establishment Clause's "excessive entanglement" analysis or the Free Exercise Clause's protections for religious organizations. Moreover, these areas of inquiry ignore the fundamental nature of thousands of religious organizations, often run as house churches, other relatively small bodies, and still other groups operated on shoestring budgets.

Part VII and accompanying Schedule J of the Form 990, and Parts IV and VI of the Form 990-EZ, seek information about key leaders' compensation. Legally, this information should be disclosed to the IRS through the paid recipients' own Form 1040 reporting, as corroborated by Form W-2s and Form 1099s. Accordingly, this information should not be necessary for religious institutions to report yet a third time via Form 990 or Form 990-EZ. Further, in the event of

[37] See Hosanna-Tabor Evangelical Lutheran Church and School v. EEOC, 565 U.S. ____ (Jan. 11, 2012), slip op. at 2-3 (Alito, J., concurring) ("[T]he autonomy of religious groups, both here in the United State and abroad has often served as a shield against oppressive civil laws. To safeguard this crucial autonomy, we have long recognized that the Religion Clauses protect a private sphere within which religious bodies are free to govern themselves in accordance with their own beliefs.").

unreasonable compensation paid to such leaders as an abuse of charitable assets, the IRS is fully able to impose severe sanctions.[38]

Part VIII of Form 990 (and corresponding Part I of Form 990-EZ) asks for detailed information about revenues, and its related Schedules B and M seek disclosure of specific contributors' names. Again, a serious chilling effect is likely to result from such mandatory disclosures. Many donors to religious organizations prefer to keep quiet, even anonymous, as a matter of religious practice. Given the public disclosure requirement that accompany Form 990 reporting, these donors likely will be far less inclined to give as they otherwise would. Under our country's constitutional jurisprudence, even the possibility of such a serious adverse threat to religion's free exercise should be enough to warrant avoiding such intrusion.

Moreover, reporting information through publically available Form 990s may run counter to a religious institution's culture and governance. Church practices vary widely in the extent of financial disclosures made to their congregants and others. By requiring compensation and revenues to be made public – not only to the members but freely available to anyone – a chilling effect likely would result for religious institutions that choose not to practice such transparency. Religious institutions are often made up of close-knit believers who tithe significant portions of their income as an exercise of faith. It would run counter to long-standing tradition and legal principles to suddenly impose public financial disclosure requirements on such organizations, akin to that of public charities supported largely by strangers across a broad spectrum.

Part IX's required disclosures about expenses (and corresponding questions in Part I of the Form 990-EZ) likewise endanger the free exercise of religion. As the Illinois Court of Appeals expressed recently in a well-publicized case involving financial aspects of a nonprofit hospital, "nothing is more practical than the numbers."[39] If the U.S. government's purpose is how, or at some point could be, to keep religious organizations from operating as they see fit and spreading their influence, these types of mandatory disclosures could be very effective. That is most definitively not the U.S.'s heritage (originally borne of extensive overseas persecution), constitutional history, or current law.[40]

G. Do the "Bad Apples" Spoil the Whole Bunch? Other Legal Safeguards are Sufficient.

Finally, the Committee report contains a lengthy discussion of "bad apples" - that is, anecdotal abuses that would arguably warrant greater governmental oversight and control of

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[38] See *infra* at Section G.

[39] Provena Covenant Medical Center v. Department of Revenue of State of Illinois, 384 Ill. App. 3d 734, 894 N.E.2d 452 (4th Dist. 2008), *aff'd*, 236 Ill. 2d 368, 925 N.E.2d 113 (2010). The hospital ultimately lost its property tax exemption, based in large part on both the Illinois Court of Appeals and the Illinois Supreme Court's detailed analysis of its financial information related to charity care.

[40] See A. Adams & C. Emmerich, A Nation Dedicated to Religious Liberty, at 52 ("The nations' religious groups come largely from traditions that reject the Enlightenment tenet that they are subservient to government. . . . To assert the absolute supremacy of the state over religious institutions and over the individual conscience is to take a step toward totalitarianism.").

religious organizations.[41] But eviscerating two hundred-plus years of constitutionally protected religious freedoms for religious institutions – notwithstanding several other legal avenues available for guarding against such abuses – is quite a monumental, unprecedented stretch here. Other legal avenues for guarding against abuses should be sufficient in light of the countervailing religious freedom considerations long held to be compelling.

First, individuals who seek to abuse the tax-exempt status of religious institutions through impermissible private benefit can be investigated and sanctioned. All individuals who receive financial compensation - whether from churches or otherwise - are legally obligated to file personal income tax returns. Such returns require mandatory self-disclosure of all compensation. To the extent persons do not properly disclose their compensation, they will be subject to serious tax penalties.[42] For example, payment of any "excess compensation" is sanctionable under section 4958 of the Internal Revenue Code, including up to 200% of the amount of the excess benefit.[43] Such individual mandatory disclosure requirements are buttressed by required IRS Form W-2 and IRS Form 1099 filing requirements, likewise with accompanying penalties for noncompliance.[44]

Other IRS policy mechanisms already exist as well for possible abuses related to payroll taxes and unrelated business income taxes. First, as employers, all religious institutions must complete and remit IRS Form 941's along with accompanying withheld taxes. This is a recognized area of permissive "entanglement." In the authors' experience representing hundreds of tax-exempt organizations, the IRS does not hesitate to investigate, demand payment, and impose serious penalties, for an organization's violation of payroll tax laws. Second, religious institutions are likewise required to file IRS Form 990-Ts for any unrelated business income taxes. Again, religious institutions are subject to tax liability and penalties for noncompliance.

On the donor side, potential abuses with respect to charitable contributions can be investigated through individuals' and corporate entities' tax returns. The IRS is well capable of conducting audits of charitable contribution reporting and does so regularly, as some readers may be able to attest.

Religious institutions can also legally be audited by the IRS. Under section 7611 of the Internal Revenue Code, an organization is subject to IRS examination for determination of (1) whether it is actually a legitimate religious body, (2) whether it is operating as an exempt organization, (3) whether it is carrying on a taxable unrelated trade or business subject to UBIT, (4) whether it is otherwise subject to federal tax, and (5) whether it has engaged in an excess benefit transaction.[45] Referrals for such audits may be made according to a "reasonable belief"

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[41] See Committee Report at 20-33 and notes 59-112 thereto.

[42] See, e.g. I.R.C. § 7201 (felony crime for tax evasion), § 7203 (failure to file tax returns or pay taxes), § 7206 (false statement to IRS); § 7212 (interfering with IRS operations); and § 4958 (penalties for excess compensation).

[43] See I.R.C. § 4958.

[44] See I.R.C. §§ 6674, 6721, 6722.

[45] See I.R.C. § 7611; See also I.R.M § 4.76.7.1.

standard of whether any tax violations have occurred.[46] Due to the same constitutional concerns for protecting religious freedoms that have been addressed herein, the threshold is admittedly higher for initiating full-scale audits.[47] This statutory higher threshold does not apply, however, for many tax enforcement areas involving religious institutions including employment tax audits, criminal investigations, tax liability of others, and other willful misconduct.[48] Accordingly, it would be a serious misstatement to claim that Form 990 reporting is critical to ferreting out tax abuses within religious institutions, and thereby that such concerns should trump religious freedoms, when other investigation and enforcement tools are at hand.

With respect to potential fundraising abuses, investigatory and punitive powers also lie with the states' Attorney General offices. Notably, religious institutions are uniformly exempt from Attorney General registration and regular reporting requirements imposed on other tax-exempt organization, presumably based on the same constitutional religious freedom considerations identified above. Nevertheless, given the States Attorney General offices' power to protect both consumers from unsavory fundraising schemes and charitable assets belonging to public charities, they can receive complaints, investigate alleged wrongdoing, and impose sanctions on wrongdoers. In the authors' own legal practice, the Illinois Attorney General's office provides a very real presence and threat to those who seek to abuse religious organizations and harm others.

The Evangelical Council for Financial Accountability (ECFA) further provides significant public interest protection against unscrupulous persons and organizations through its valued accreditation standards. While the ECFA does not have power to enforce the tax laws, its accreditation represents an important and significant incentive for the vast majority of "good apples" who seek to comply with applicable laws in good faith.

Finally, a plethora of state and federal criminal and quasi-criminal laws already exist to prevent and punish wrongdoing and other abuses of tax-exempt organizations. Fraud, theft, embezzlement, and tax evasion have been and will continue to be illegal.

The extensive legal sanctions available to the government for tax abuses and other misconduct demonstrate that the real problem usually lies with individuals. In other words, tax-exempt organizations themselves are not "bad apples," it is the people who control them and misuse them for their own gain. Consequently, investigating and punishing such person through individual audits, sanctions such as available under section 4958, and criminal penalties should be highly effective.[49]

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[46] I.R.M. § 4.76.7.4.2.

[47] The higher threshold is namely that an "appropriate high-level Treasury official" must reach the requisite reasonable belief. Such official means "the Secretary of the Treasury or any delegate of the Secretary whose rank is no lower than that of a principal Internal Revenue Officer for an internal revenue region." See I.R.C. § 7611(a)(2) and (h)(7).

[48] See, e.g. I.R.C. § 7611(i) (exclusions); see also E. Gonzalez, T. Miller, D. Jones, Update On Churches Examinations Under IRC 7611,1992 EO CPE Text.

[49] See e.g., N.J. Rabbi Gets 5-Year Sentence in Corruption Case, and D.C. Council Member Reportedly to Plead on Nonprofit Fraud Allegations, as reported in *Chronicle of Philanthropy* (Jan. 5, 2012).

H. Concluding Remarks

Requiring Form 990 initial and ongoing reporting would represent an unconstitutional and unnecessary intrusion on religious institutions, resulting in intolerable chilling effects and irreparable injury to them. No compelling government interest justifies such an unprecedented legal change, particularly in light of our country's history and jurisprudence. To infringe upon the freedoms of law-abiding religious institutions as the price for such stepped-up government surveillance and policing would be untenable. Accordingly, no new IRS registration or Form 990 reporting requirements should be imposed on religious institutions.

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